

Case No: 1381/7/7/21

**IN THE COMPETITION APPEAL TRIBUNAL****BETWEEN:****JUSTIN LE PATOUREL****Applicant / Proposed Class Representative****-and-****(1) BT GROUP PLC****(2) BRITISH TELECOMMUNICATIONS PLC****Respondents / Proposed Defendants****2 CF BUNDLE****24 – 25 JUNE 2021**

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BETWEEN**

**JUSTIN LE PATOUREL**

**Applicant / Proposed Class Representative**

and

**(1) BT GROUP PLC**

**(2) BRITISH TELECOMMUNICATIONS PLC**

**Respondents / Proposed Defendants**

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**AMENDED COLLECTIVE PROCEEDINGS CLAIM FORM**

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*References to the Claim Form Bundle ("CF **Bundle**") will be in the form [CF Bundle/Tab number/Page number].*

*References to the Bundle containing the witness statement of Justin Le Patourel ("**JLP Bundle**") will be in the form [JLP Bundle/Tab number/Page number]*

*References to the Bundle containing the witness statement of Robert Paul Murray ("**RPM Bundle**") will be in the form [RPM Bundle/Tab number/Page number]*

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## INTRODUCTION AND SUMMARY

1. This is an application for a collective proceedings order (“**CPO**”) filed pursuant to Rule 75 of the Competition Appeal Tribunal Rules 2015 (SI 1648/2015) (“**the Rules**”) to commence collective proceedings under section 47B of the Competition Act 1998 (“**the Act**”). The Applicant, Justin Le Patourel (“**the Proposed Class Representative**”), makes this application for a CPO permitting him to act as the class representative.
2. The claims which it is proposed to combine in these collective proceedings (the “**Claims**”) are “standalone claims” under section 47A of the Act for damages caused by breaches of statutory duty by the Proposed Defendant<sup>s</sup> (“**BT**”) in charging unfair prices to certain of its customers in breach of s.18 of the Competition Act 1998 (the “**Chapter II Prohibition**”).
3. In summary, BT has throughout the Claim Period charged excessive prices to customers supplied with certain residential landline services. Although the Claims are not “follow on” claims, they arise out of a review, conducted by Ofcom in 2017, of “the market for standalone landline telephone services” (“**the 2017 Review**”). Ofcom conducted the 2017 Review pursuant to its powers under the Communications Act 2003 to review communications markets for the purposes of deciding whether to impose *ex ante* regulation.
4. The 2017 Review addressed the prices paid by consumers for certain residential landline telephone services, where those services are bought by the customer on a standalone basis, rather than as a part of a bundle with non-voice services such as broadband. In summary, Ofcom found that prices for standalone residential landline telephone services were above the competitive level, thereby causing consumer detriment. In February 2017, Ofcom provisionally concluded that a three-year retail price control was necessary to reduce the prices charged by BT for those landline services. Subsequently, in October 2017, Ofcom accepted a set of voluntary commitments from BT which involved, amongst other things, a forward-looking price reduction for a certain segment of customers who buy certain standalone residential landline services and do not buy broadband at all, from

BT or any other provider.<sup>1</sup> As set out below, Ofcom recently launched a consultation to review and consider the renewal of the existing commitments.

5. The Proposed Collective Proceedings are brought on an opt out basis on behalf of a class consisting predominantly of consumers (“**the Proposed Class**”), which it is proposed to divide into two sub-classes (“**the Proposed Sub-classes**”), and seek an aggregate award of damages for the Proposed Class.
6. The Proposed Class and the Proposed Sub-classes are described in detail at §§75 – 101 below. In overview, the Proposed Class comprises consumers who have bought certain residential landline services from BT, on a standalone basis, rather than as part of a bundle, during the Claim Period (as defined below). Those consumers are divided into two Proposed Sub-classes depending on whether or not they also bought broadband (not as part of a bundle but separately).
7. The remainder of this Claim Form is split into the following parts in order to address the requirements in Part 5 of the Rules and Section 6 of the Tribunal’s Guide to Proceedings (“**the Guide**”):<sup>2</sup>
  - (a) **Part I** sets out the information and statements to comply with Rule 75(2);
  - (b) **Part II** sets out the factual background to the 2017 Review and Ofcom’s findings;
  - (c) **Part III** sets out the information and statements concerning the Proposed Class to comply with Rule 75(3)(a)-(c));
  - (d) **Part IV** sets out the information and statements concerning the alleged infringement and the basis of the claims to comply with Rule 75(3)(f)-(h) and (j));
  - (e) **Part V** sets out the summary of the basis upon which it is contended that the criteria for certification and approval in Rule 79 are satisfied to comply with Rule 75(3)(e);

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<sup>1</sup> As explained later, these are known as “Voice Only Customers”.

<sup>2</sup> §6.11 of the Guide suggests that the Claim Form should be set out in three parts; however, in order to avoid duplication and excessive cross-referencing, the basis of the Claims is set out first, before addressing their suitability for inclusion in collective proceedings and the Proposed Class Representative’s ability to represent the class.

- (f) **Part VI** sets out the summary of the basis on which the Proposed Class Representative seeks to be authorised to comply with Rules 75(3)(d) and 78; and
- (g) **Part VII** sets out the relief sought to comply with Rule 75(3)(i).
8. Accompanying this Claim Form are the following documents in support of the application for a CPO and the Claims:
- (a) Glossary of definitions used in this Claim Form [**Annex 1**] [**CF Bundle/2/82-86**];
- (b) Expert economic report by David Parker (Frontier Economics), dated 13 January 2021 (“**the Parker Report**”), which addresses the Infringements, quantification and the class definition and size [**Annex 2**] [**CF Bundle/3/87-255**];
- (c) Evidence in support of the Claims, which is publicly available, namely: (i) Ofcom’s “Review of the market for standalone landline telephone services; Statement” (26 October 2017) (“**the Statement**”) (non-confidential) [**Annex 3**] [**CF Bundle/4/256-306**]; (ii) Ofcom’s Evidence, “Evidence supporting this statement: Review of the market for standalone landline telephone services”, 26 October 2017 (non-confidential) [**Annex 4**] [**CF Bundle/5/307-368**]; (iii) Ofcom’s Provisional Conclusions, “Review of the market for standalone landline telephone services”, 28 February 2017 (non-confidential) (“**the Provisional Conclusions**”) [**Annex 5**] [**CF Bundle/6/369-486**]; and (iv) Ofcom’s Provisional Conclusions Annexes, 28 February 2017 (non-confidential) [**Annex 6**] [**CF Bundle/7/487-607**];
- (d) Draft Collective Proceedings Order, as required by Rules 75(5)(b) and 80 [**Annex 7**] [**CF Bundle/8/608-611**];
- (e) Draft Notice to Proposed Class Members of the CPO, as required by Rules 75(5)(c) and 81 [**Annex 8**] [**CF Bundle/9/612-624**];
- (f) Witness Statement of Justin Le Patourel (Proposed Class Representative), [**JLP Bundle/1/3-32**], addressing the requirements of Rule 78 and including (i) a litigation plan for the Proposed Collective Proceedings as per Rule 78(3)(c) (“**Litigation Plan**”) [**JLP Bundle/2/33-160**]; (ii) a Notice and Administration Plan (“**Notice and Administration Plan**”) [**JLP Bundle/2/60-149**] and (iii) a litigation

funding agreement to demonstrate an ability to pay the proposed Defendants' reasonable costs in accordance with Rule 78(2)(d) ("**Litigation Funding Agreement**") [**JLP Bundle/22/901-933**]; and

- (g) Witness Statement of the Proposed Class Representative's legal representative, Rob Murray (Partner, Mishcon de Reya LLP), addressing the pre-action correspondence and suitability of the legal team [**RPM Bundle/1/3-12**].

## **PART I: THE REQUIRED INFORMATION AND STATEMENTS UNDER RULE 75(2)**

9. This part sets out the information and statements to comply with Rule 75(2).

### **The Proposed Class Representative (Rule 75(2)(a)-(c))**

10. The Proposed Class Representative is Mr Justin Le Patourel of a private residential address in East Sussex, United Kingdom.<sup>3</sup> Further biographical information concerning the Proposed Class Representative is set out in his Witness Statement [**JLP Bundle/1/3-32**].
11. The Proposed Class Representative's legal representatives and address for service in the United Kingdom are: Mishcon de Reya LLP, Africa House, 70 Kingsway, London, WC2B 6AH (Attention: Rob Murray/Natasha Pearman). The Proposed Class Representative's counsel are: Ronit Kreisberger Q.C., Alison Berridge and Jack Williams (all of Monckton Chambers). Further information about the Proposed Class Representative's legal representatives and counsel is set out in the Witness Statement of Rob Murray [**RPM Bundle/1/3-12**] at §§44 – 46.

### **The Proposed Defendants (Rule 75(2)(d) and 75(7))**

12. The Proposed Defendants, BT Group PLC and British Telecommunications PLC ("**BT**"), ~~is a~~ are public limited companies~~y~~ with registration numbers 04190816 and 01800000

<sup>3</sup> The address for the Proposed Class Representative will be provided to the Tribunal and to the Proposed Defendants, if required. The Applicant requests, in accordance with Rule 101 of the Rules, for the confidential treatment of his private address in any documents filed or served in the proceedings to be treated as confidential by any party to whom it has been or shall be disclosed. The Proposed Class Representative can otherwise be contacted via his legal representatives.



respectively and the same registered office of 81 Newgate Street, London, EC1A 7AJ. BT ~~is a~~are communications providers within the meaning of section 32(4) of the Communications Act 2003 (“CP”).

12A. As for the relationship between the Proposed Defendants and their joint and several liability for the Infringements (as defined below):

- (a) British Telecommunications is a wholly owned subsidiary of BT Group Plc and has been for the entirety of the Claim Period.
  - (b) British Telecommunications PLC is the principal operating subsidiary of BT Group Plc.
  - (c) The BT Group plc Board has ultimate responsibility for the management of the group and until on or around 2 October 2017, the Operating Committee of BT Group plc was the key management committee, which monitored the group’s financial, operational and customer service performance and had cross-business oversight of BT’s lines of business; and reviewed the group’s key risks and considered the potential threats and opportunities to the business. From on or around 2 October 2017, the Operating Committee was replaced by the Executive Committee (the "ExCo").
  - (d) Correspondence between Ofcom and BT relating to the BT Commitments (as defined below) was addressed to Marc Allera of BT Group. Mr Allera is CEO of BT Consumer. As CEO of BT Consumer, he was/is on the ExCo Board of BT Group Plc.
  - (e) In the premises, BT Group Plc had the ability to exercise and/or did in fact exercise decisive influence over the conduct of BT Telecommunications PLC during the Claim Period.
13. The legal representatives of the Proposed Class Representative have been informed that Simmons & Simmons represents the Proposed Defendants and is instructed to accept service of these proceedings on behalf of the Proposed Defendants.

**Application for a Collective Proceedings Order (Rule 75(2)(e)-(f))**

14. The Proposed Class Representative is making, via this Claim Form, an application for a CPO. The application relates to opt-out proceedings on behalf of consumers.<sup>4</sup>

**Alternative Dispute Resolution (Rule 75(2)(g))**

15. At the date of filing this Claim Form, the parties have not yet used an alternative dispute resolution procedure. In his letter before action of 14 November 2020 [**RPM Bundle/3/25-30**] and further letters of 27 November 2020 [**RPM Bundle/5/35-39**] and 8 January 2021 [**RPM Bundle/8/46-48**], the Proposed Class Representative made it clear that he is willing to engage in or explore alternative dispute settlement discussions (in accordance with the Rules on Collective Settlements); but he also explained to BT that, in order to do so meaningfully, on an informed basis, and to secure a fair settlement for all Members of the Proposed Class, the Proposed Class Representative must be satisfied that he has received sufficient disclosure from BT concerning the true extent and level of excessive pricing, rather than basing it on estimates from non-confidential versions of the Provisional Conclusions and Statement. See, further, the Witness Statement of the Proposed Class Representative’s legal representative, Rob Murray (Partner, Mishcon de Reya LLP) [**RPM Bundle/1/3-12**].

**Real prospect of success (Rule 75(2)(h))**

16. The Proposed Class Representative believes that the claims which he has sought to combine in the collective proceedings have a real prospect of success (see §§60 - 61 of his Witness Statement [**JLP Bundle/1/19**]).
17. In particular, whilst the Claims are of a standalone nature, they rely heavily on the facts and findings set out in the 2017 Review.
18. Ofcom provisionally found that BT had significant market power, was a price-leader, and charged prices which were above the competitive level so as to give rise to serious

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<sup>4</sup> As discussed further below, while the services concerned are aimed at residential customers i.e end consumers, a small proportion of customers buying those residential services may in fact have been small businesses. Where the term “consumer” is used in this Claim Form, it is intended to covers both categories of customer unless otherwise stated.

consumer detriment. See the Provisional Conclusions [**Annex 5**] [**CF Bundle/6/369-486**], at §1.16 and §1.17:

“...BT has significant market power (i.e. has a dominant position) in the market for standalone landline telephone services. This allows it to act in setting the terms and conditions of sales in this market without facing significant competitive constraint from other providers. This is particularly true when it comes to setting prices.

BT benefits from a very high market share; over 70%, in a market where many customers are not actively engaged. This in turn has allowed BT to act as a price leader, steadily increasing the price of standalone landline services. Further, given the difficulty in winning new customers from BT, the range of choice from competing providers has declined as prices have increased.”<sup>5</sup>

19. As Ofcom stated that “customers purchasing voice-only services – often elderly people who have remained with the same provider for many years – are getting poor value for money” whereas customers “who buy bundled services are getting more for their money than ever before” (Statement, §1.2) [**CF Bundle/4/260**]. Ofcom stated that the customers affected “have less choice of suppliers and are not benefiting from strong price competition or promotional offers. Their loyalty to their provider is not being rewarded but is instead leading to ever higher prices” (ibid.).<sup>6</sup>
20. Ofcom intended to impose direct price control to reduce monthly line rental prices by £5-7 for both sets of customers (i.e. broadly, the two Proposed Sub-classes): see Provisional Conclusions [**Annex 5**] at §§1.21 – 1.23 and 8.32 – 8.34 [**CF Bundle/6/377**] and [**CF Bundle/6/470**].
21. Ultimately, (and presumably in order to avoid direct price control by Ofcom) BT offered voluntary commitments involving, amongst other things, a 3-year commitment to reduce line rental prices by £7 per month to around a million residential BT Voice Only Customers (i.e. broadly only one of the Proposed Sub-classes), and offered certain engagement remedies for BT Split Purchase Customers (i.e. the other Proposed Sub-

<sup>5</sup> See, also, the Statement [**Annex 3**] at §§1.12 (“BT currently holds a dominant position in the market for voice-only customers and the lack of competition enables it to maintain prices above the competitive level”); 2.12, 3.6, 3.34 – 3.48, 3.53 (“BT also accounts for a very high market share, 97% of split-purchase lines”) and 3.54 (“BT’s position in the markets for voice-only access and calls is consistent with the position we set out in the February Consultation for standalone fixed voice services more generally.”)

<sup>6</sup> See also Statement §§3.5 and 4.24 in relation to a category of customers known as Split Purchase Customers, addressed below.

class). The BT Commitments [**Annex 3**] [**CF Bundle/4/284-300**] are described in detail at §§58 - 62 below.

22. On the basis of his own analysis of the publicly available data arising out of the 2017 Review, the Parker Report has concluded that, during the applicable Claim Period, BT holds/held a dominant position on relevant markets for standalone residential landline services, and that it abused its position in those markets by charging excessive prices, thereby infringing the Chapter II Prohibition.
23. The Proposed Class Representative therefore believes that (i) the prices for standalone residential landline services which form the subject-matter of the Claims infringe the Chapter II Prohibition and (ii) the infringing prices caused Members of the Proposed Class to sustain losses. Whilst the precise magnitude and effects of the unlawful overcharges will be the subject of detailed disclosure, expert reports and factual evidence (and will be tested at trial, including by cross-examination), the Proposed Class Representative believes on the basis of Ofcom's findings and the Parker Report that the Members of the Proposed Class have a real prospect of recovering damages in the Claims.

## **PART II: FACTUAL BACKGROUND TO THE 2017 REVIEW AND OFCOM'S FINDINGS**

### **Regulatory framework**

24. Ofcom is the independent regulator responsible for regulating communication services in the UK. Under the Communications Act 2003, Ofcom is responsible for implementing the market review process established under European law. The following is a summary of the regulatory framework under which Ofcom's 2009 and 2017 reviews (discussed below) were conducted.
25. Directive 2002/21/EC on a common regulatory framework for electronic communications networks and services requires national regulatory authorities to carry out reviews of competition in communications markets to ensure that regulation remains appropriate and proportionate in the light of changing market conditions.
26. Each market review normally has three stages, namely:

- (a) identification and definition of the relevant markets (Communications Act 2003, s.79);
  - (b) assessment of competition within in each relevant market, in particular whether any undertakings have significant market power (“SMP”) (Communications Act 2003, s.79). SMP is defined as a position which amounts to or is equivalent to dominance of the market (Communications Act 2003, s.78); and
  - (c) where there is a finding of SMP, imposition of appropriate regulatory obligations (Communications Act 2003, ss.87-93).
27. In doing so, Ofcom is required to take utmost account of the Commission’s 2002 guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications networks and services.<sup>7</sup>

### **Regulatory action by Ofcom pre-2017**

28. BT has been subject to a variety of regulation since privatisation in 1984. In 2003, Oftel (the predecessor regulator to Ofcom) carried out the first review of *retail* landline services (i.e. services provided to end customers), including residential and business services, under the above regulatory framework and imposed certain *ex ante* regulation including (i) no undue discrimination requirements; (ii) certain price publication and notification requirements and (iii) cost accounting and accounting separation requirements.<sup>8</sup> At the stage, Ofcom also confirmed the regime of direct retail price controls which had been in place since 2002,<sup>9</sup> but they were not renewed on their expiry in 2006.<sup>10</sup>

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<sup>7</sup> Commission guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications networks and services (2002/C 165/03). Framework Directive 2002/21/EC Recital 28, Arts 15(3) and 16(1).

<sup>8</sup> Ofcom, “Fixed Narrowband Retail Services Markets: Identification and analysis of markets, making of market power determinations and setting of SMP conditions, Final Explanatory Statement and Notification”, 28 November 2003.

<sup>9</sup> Oftel, “Protecting consumers by promoting competition: Oftel’s conclusions”, 20 June 2002.

<sup>10</sup> Ofcom, “Retail Price Controls: Explanatory Statement”, 19 July 2006.

29. In 2009, Ofcom conducted a review of “Fixed Narrowband Retail Services Markets”<sup>11</sup> under s.79 Communications Act 2003 (“**the 2009 Review**”) [Annex 11] [CF Bundle/12/664-767]. As part of that review, Ofcom concluded that, following the adoption of various measures which Ofcom had taken to enhance competition in retail markets,<sup>12</sup> BT no longer had SMP in landline telephone services. See §§66-70 of the Parker Report [Annex 2] [CF Bundle/3/113-114].

### Ofcom’s 2017 Review

30. On 1 December 2016, Ofcom announced<sup>13</sup> a review under s.79 of the Communications Act 2003 of “the market for standalone landline telephone services” (“**the 2017 Review**”<sup>14</sup>). In the announcement, Ofcom explained that the review was prompted by a concern that people who bought landline services on a standalone basis were not being served well by the market. Ofcom published its Provisional Conclusions on 28 February 2017, and sought responses by 9 May 2017.
31. The 2017 Review concerned the provision of **Standalone Fixed Voice Services (“SFV Services”)** which, Ofcom explains, comprise residential landline telephone services which are not sold as part of a bundle with non-voice services,<sup>15</sup> as addressed in more detail below.
32. The Proposed Class Representative reserves his right to rely on all Ofcom documents pertaining to the 2017 Review at trial for their full meaning and effects. The following paragraphs contain a summary of the main facts and findings made by Ofcom in the 2017 Review from the public, non-confidential versions of the documents.

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<sup>11</sup> Ofcom, “Fixed Narrowband Retail Services Markets: Identification of markets and determination of market power”, 15 September 2009. This covered analogue and digital (ISDN) telephone lines, and calls for consumers and businesses.

<sup>12</sup> See Ofcom’s 2009 Review, §1.7 [CF Bundle/12/668].

<sup>13</sup> [Annex 9] [CF Bundle/10/625-631].

<sup>14</sup> Ofcom’s 2017 Review encompasses the Provisional Conclusions [Annex 5] [CF Bundle/6/369/486] and the Statement [Annex 3] [CF Bundle/4/256-306], which are key documents in relation to the Claims.

<sup>15</sup> Provisional Conclusions, §1.15 [Annex 5] [CF Bundle/6/376-377] and see Glossary [Annex 6] [CF Bundle/7/603-695].

## Provisional Conclusions

### *Relevant markets: products, geography and customer groups*

33. Ofcom defined two distinct product markets in relation to the provision of SFV Services:
- (a) the market for the provision of access *i.e.* line rental (“**the SFV access market**”);  
and
  - (b) the market for the provision of calls (“**the SFV calls market**”).<sup>16</sup>
34. In defining the material scope of each of the SFV access market and SFV calls market, Ofcom excluded “landline telephone services when they are provided as part of a bundle (landline telephone and broadband or landline telephone, broadband and pay-TV)”.<sup>17</sup>
35. Ofcom refers to three types of bundles: multi-play, triple play and dual play, as follows:
- “CPs offer fixed voice services bundled with other communications services e.g. broadband, pay TV or mobile. These multi-play bundles are usually sold at a discount compared to the price of purchasing the individual components separately from different providers (or the same provider). ... dual-play (voice and broadband) and triple-play (voice, broadband and pay TV) bundles are particularly common. ...”<sup>18</sup>
36. This Claim Form uses the term “Dual Play” to refer to a bundle comprising voice and broadband services.
37. Further, as regards the material scope of each of the SFV access market and SFV calls market, Ofcom provisionally excluded:
- (a) BT Basic, a product available only to customers on specific low income government benefits;<sup>19</sup>

<sup>16</sup> Provisional Conclusions, §§1.15 and 3.3 [Annex 5] [CF Bundle/6/376-377] and [CF Bundle/6/386].

<sup>17</sup> Provisional Conclusions, §1.15 [Annex 5] [CF Bundle/6/376-377]

<sup>18</sup> Provisional Conclusions, §3.30 [Annex 5] [CF Bundle/6/392]

<sup>19</sup> Provisional Conclusions, §§3.50 to 3.53 [Annex 5] [CF Bundle/6/398]. See §88 below for an explanation of BT Basic.

- (b) services available only to businesses;<sup>20</sup> and
  - (c) mobile services on the basis that they “remain at most a complementary service for most consumers.”<sup>21</sup>
38. Ofcom defined the relevant geographic area as the UK excluding the Hull area.
39. Ofcom went on to identify the following two distinct groups of customers taking SFV Services as follows:
- (a) **“Voice Only Customers”**: SFV Customers who do not also buy a fixed broadband service (whether from the same provider or different providers); and
  - (b) **“Split Purchase Customers”**: SFV Customers who buy fixed broadband but not as part of a bundle with SFV services. As set out above, customers buying dual play, triple play or multi play bundles are excluded from the scope of each of the SFV access market and SFV calls market.
40. Ofcom further distinguished between two groups of Split Purchase Customers<sup>22</sup> as follows:
- (a) Split Service Customers: SFV Customers “who buy fixed broadband from the same provider as their SFV service (but not as part of a bundle)” (emphasis added); and
  - (b) Split Supplier Customers: SFV Customers “who buy fixed broadband from a different provider than their SFV service” (emphasis added).
41. The various customers groups are represented in Ofcom’s Figure 3.1 which, for convenience, is reproduced below.

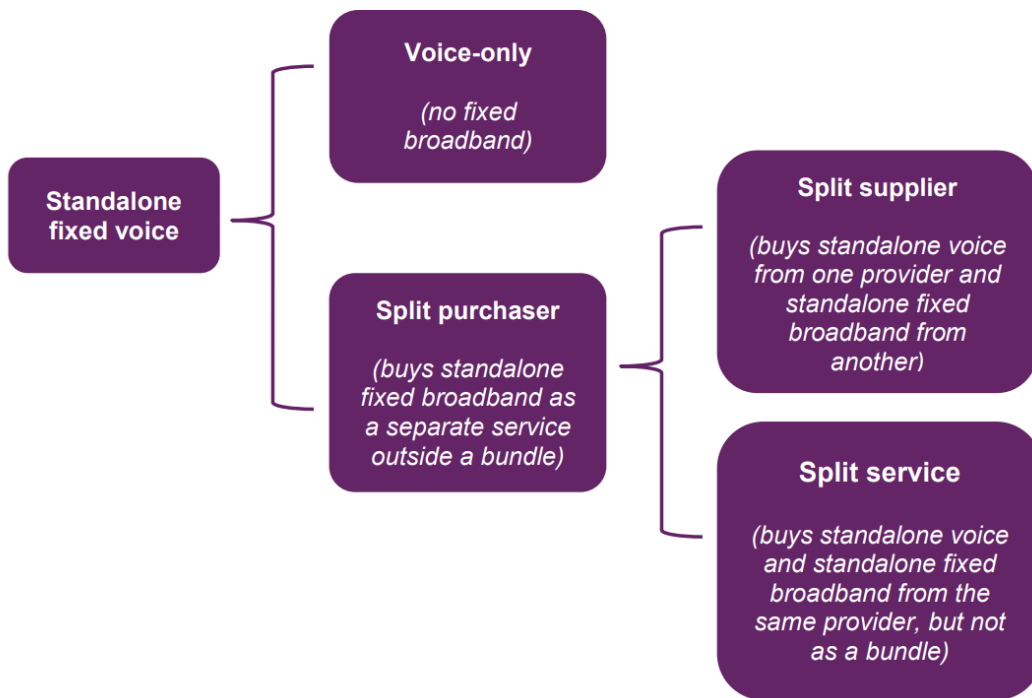
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<sup>20</sup> Provisional Conclusions, §§3.54 to 3.56 and 3.106 [Annex 5] [CF Bundle/6/398-399] and [CF Bundle/6/407].

<sup>21</sup> Provisional Conclusions, §§3.57-3.62, 3.86-3.100 [Annex 5] [CF Bundle/6/399-400] and [CF Bundle/6/404-406].

<sup>22</sup> Provisional Conclusions, §3.21.2. [Annex 5] [CF Bundle/6/389].



**Figure 3.1: Customer groups within SFV<sup>30,31</sup>**

42. Ofcom estimated that, at the time of the Provisional Conclusions, there were around 2.9 million SFV Customers, which accounted for 11% of total residential landline customers. Of those, around 1.7 million were Voice Only Customers and 1.2 million were Split Purchase Customers.<sup>23</sup>
43. Ofcom provisionally concluded that it was not necessary to distinguish between Voice Only and Split Purchase Customers for the purposes of defining the SFV access market, given that the two customer groups “purchase identical products under identical terms.”<sup>24</sup> Ofcom went on to consider whether there was scope for BT and other CPs to price discriminate between the two customer groups, which might suggest that they are in different markets. At that stage, Ofcom treated both groups as in the same market as they had so far been charged the same prices for SFV Services.
44. In relation to the nature and characteristics of Voice Only and Split Purchase Customers (together, SFV customers or standalone landline customers), Ofcom provisionally found:

<sup>23</sup> Provisional Conclusions, §1.12 [Annex 5] [CF Bundle/6/376].

<sup>24</sup> Provisional Conclusions, §§3.44 to 3.49 [Annex 5] [CF Bundle/397].

- (a) “Standalone landline customers generally do not engage with the market: 70% of standalone landline customers have never switched provider or considered doing so”: §1.13, Provisional Conclusions [**Annex 5**] [**CF Bundle/6/376**];
- (b) “SFV customers have lower levels of engagement (9%) and lower annual switching rates (3%), compared to dual-play customers (20% and 12%, respectively). Further, a higher proportion of SFV customers reported that they have never switched their landline supplier (70%) compared to dual-play customers (45%)”: A8.147 in Ofcom’s Provisional Conclusions Annexes, 28 February 2017 (non-confidential) [**Annex 6**] [**CF Bundle/7/576**];
- (c) “BT SFV and BT voice-only customers are less engaged compared to customers of other CPs. Only 5% of BT SFV customers are classified as engaged, compared to 19% of other CP SFV customers.”: A8.156 in Ofcom’s Provisional Conclusions Annexes, 28 February 2017 (non-confidential) [**Annex 6**] [**CF Bundle/7/578**];
- (d) Standalone landline customers “tend to be older and less likely to shop around for a better deal. Approximately 43% of standalone landline customers are at least 75 years old, and 35% live in DE socio-economic group households (for comparison, 4% of dual-play customers are 75 or over, and 20% are in DE group households)”: §1.13, Provisional Conclusions [**Annex 5**] [**CF Bundle/6/376**]. See also §A8.143 in Ofcom’s Provisional Conclusions Annexes, 28 February 2017 (non-confidential) [**Annex 6**] [**CF Bundle/7/572-573**];<sup>25</sup>
- (e) “35% of SFV customers live in DE socioeconomic group households, which is substantially higher than the equivalent proportion for dual-play customers (20%). In terms of customer segments, the proportion of voice-only customers who live in DE socioeconomic group households (41%) is materially higher than the

<sup>25</sup> “S135 responses indicate that 43% of SFV customers are aged 75 years old or over (12% are aged between 75 and 79, 15% are aged between 80 and 84, and 16% are aged 85 or over). This is substantially higher than the equivalent proportion for dual-play customers (4% according to the Ofcom Technology Tracker, 2016 H2) and for the UK population over 15 years old (10% according to the ONS)”; and “The Ofcom Technology Tracker (2016 H2) study suggests that: 34% of SFV customers are aged 75 years old or over. This is lower than the 43% figure based on S135 responses. We rely on the 43% figure as it is based on actual customer information held by CPs, rather than on survey responses. The Technology Tracker also suggests that voice-only customers tend to be older (47% are aged 75 or over) than split-supplier customers (4% are aged 75 or over, as is the case for dual-play customers)”.

equivalent proportion of split-supplier customers (21%). The high proportion of DE is partially explained by the fact that pensioners are automatically classified as living in E socioeconomic group households under the National Readership Survey’s classification system.” §A8.143 in Ofcom’s Provisional Conclusions Annexes, 28 February 2017 (non-confidential) [**Annex 6**] [**CF Bundle/7/572-573**]; and

- (f) “71% of SFV customers indicated they are not working, which is materially higher than the equivalent proportion for dual-play customers (35%). In terms of customer segments, 81% of voice-only customers indicated they are not working which is markedly higher than the equivalent proportion for split supplier customers (45%).” §A8.143 in Ofcom’s Provisional Conclusions Annexes, 28 February 2017 (non-confidential) [**Annex 6**] [**CF Bundle/7/572-573**].

*Provisional findings on SMP*

45. Ofcom provisionally concluded that:

- (a) BT had SMP in the SFV access market in the UK (excluding the Hull Area) based amongst other things on: BT’s market share of at or above 79% (Provisional Conclusions, §4.27); the high cost of acquiring customers; evidence that BT acted as a price leader; BT’s profitability; and the lack of countervailing buyer power (section 4) [**CF Bundle/6/413-430**].
- (b) BT had SMP in the SFV calls market in the UK (excluding the Hull Area) based amongst other things on: BT’s market share; the high cost of acquiring customers; and BT’s profitability (section 5) [**CF Bundle/6/431-437**].

*Provisional findings on consumer detriment*

46. While Ofcom considered that consumers buying bundled products had benefitted from competition, it was concerned that:

“... competition is not benefiting standalone voice customers (i.e. those that do not purchase bundled products) to the same extent. There are currently 2.9 million households which take voice services outside a bundle,

representing 11% of all residential landline users (i.e. including those that purchase landline services in a bundle). Whilst the number of such customers is declining over time, it is nevertheless likely to remain significant for the foreseeable future.

... these customers have been progressively exposed to increasing line rental prices since 2010. This has been occurring despite wholesale charges for products used to provide line rental falling by up to 26% in real terms...

While some of the price increases may be due to rebalancing prices as fixed voice call revenue falls, declining wholesale costs suggest that CPs serving this market have been increasing their profitability.

We are particularly concerned that this trend affects a significant number of consumers who are elderly... over half of these consumers are over 70... Moreover, this group of consumers is generally more disengaged; Ofcom research has shown that 71% of consumers who use standalone landline services have never switched providers or considered doing so. We are concerned that these customers are receiving poor value for money given the rising line rental charges which they face.”<sup>26</sup>

47. Ofcom identified two types of consumer detriment: (i) direct effects and (ii) indirect effects.
48. In relation to direct effects, Ofcom considered the extent to which BT’s SFV services were above the competitive level, taking into account its assessment of BT’s profitability in the SFV access and calls markets and the profit margins which it identified. The relevant data on BT’s profitability is redacted and the Proposed Class Representative reserves his right to amend this section of the Claim Form following disclosure of the redacted material. In the light of that assessment, Ofcom provisionally concluded that BT’s prices were approximately £8-10 per line per month above the level of its costs and £5 to £7 per line per month above a level defined using competitive benchmarks.<sup>27</sup>
49. In relation to indirect effects, Ofcom stated:

“Competition can deliver a number of consumer benefits such as lower prices, more choice, better quality and innovation. Competition in the provision of SFV services could, for example, deliver benefits in the form of

<sup>26</sup> See §§2.2 – 2.7 in the Provisional Conclusions [Annex 5] [CF Bundle/6/379-380]. The Proposed Class Representative relies on those passages in full.

<sup>27</sup> Provisional Conclusions, §6.4 [Annex 5] [CF Bundle/6/438], referencing the analysis at Section 8 and Annex 5.

product differentiation by reference to service features (e.g. reliability of the connection), customer and add-on services. Consumers could also benefit from competition in the provision of different call packages and inclusive call allowances. As a result of the lack of competition in the market, reflected in BT's SMP, consumers are deprived of the benefits that such competition would bring.<sup>28</sup>

*Ofcom's proposed remedy*

50. Ofcom provisionally decided to impose a price control remedy in the form of a price reduction to BT's charges for SFV Services "in order to protect consumers from prices which are above the competitive level".<sup>29</sup> Ofcom proposed "that both sets of consumers purchasing SFV services [i.e. broadly, the two Proposed Sub-classes] would be included in a price control": Provisional Conclusions, §8.34. Specifically, Ofcom (provisionally) considered that a reduction to the prices paid by customers to BT each month for line rental was necessary.
51. Ofcom considered a number of options in order to determine the size of the monthly line reduction. One such option was to reduce BT's line rental prices to a cost-based level, which would result in a reduction of between £8 and £10 (including VAT) per line per month (§8.17). But Ofcom considered that such a reduction would be highly likely to make it uneconomic for other providers to compete in offering SFV Services, due to the substantial customer acquisition costs that they face (§8.18).
52. Accordingly, in order to understand how much it could reduce prices by and still expect competition to emerge, Ofcom took account of a number of different measures in order to estimate a competitive benchmark (§8.19) set out below:
  - (a) BT's 2009 profitability for its SFV Services (§§8.20 to 8.28);
  - (b) BT's profitability, at the time of the Provisional Conclusions, in the dual play market (§§8.22 to 8.23);

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<sup>28</sup> Provisional Conclusions §6.7 [Annex 5] [CF Bundle/6/439].

<sup>29</sup> Provisional Conclusions, §8.30 [Annex 5] [CF Bundle/6/469].

- (c) The profitability of other CPs offering retail voice services (although Ofcom had some concerns about the robustness of its estimates and therefore treated the results of its analysis with caution (§§8.24 and 8.25); and
- (d) A discounted cash flow analysis designed to establish what level of price cut could be imposed but retain the incentive for rivals to compete for providers (§§8.26 to 8.28).<sup>30</sup>
53. Ofcom provisionally concluded that a price cut of between £5 and £7 (including VAT) per line per month would allow profitability at a level that would be consistent with competition developing (§8.30); and would significantly reduce the direct customer detriment attributable to BT’s pricing behaviour (§9.6).
54. Ofcom proposed a three-year term for the price control which would give consumers and CPs “certainty over BT’s charges over the medium term” (§8.31).
55. Ofcom considered whether there was any reason to exclude Split Purchase Customers from the proposed price control (notwithstanding its finding on market definition at §43 above), as follows:

“Both sets of consumers purchase the same SFV products and therefore, as we noted in Section 3, they both face the same detriment from the prices of SFV services being above the competitive level. Our provisional conclusion in Section 3 is that both of these sets of consumers are included in the same SFV markets. These provide reasons to include both sets of consumers in any price control.

Nevertheless, we have also considered whether there is a reason to exclude split purchasers from any price control. One possible reason is the potential for engagement remedies to be more effective in promoting competition for split purchasers than for voice-only consumers. Compared to voice-only customers, split purchasers have the added benefit of using the internet to compare and switch between products and CPs. In addition, there are many CPs offering competitive dual-play packages which split purchasers could adopt. However, even if, assisted by these circumstances, engagement remedies proved to be effective, in the absence of a price control, consumers who remain split purchasers are likely to continue to suffer detriment from

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<sup>30</sup> Ofcom also noted that BT used its Home Phone Saver product as a retention tool where it may lose customers to competitors. The product therefore provided an indication of the price cut which BT was willing to offer commercially where it perceived the threat of competition (§8.29).

BT’s prices for SFV services being above cost in the significant period of time before the implementation of such remedies. Therefore, we propose that both sets of consumers purchasing SFV services would be included in a price control.” (§§8.33 – 8.34)

56. In the light of the above, Ofcom proposed a price control in the following terms:<sup>31</sup>

“Specifically, we propose to set a three-year retail price control on BT’s standalone fixed voice services of the following form:

An initial one-off price reduction of the line rental by between £5 and £7 per month and controls on line rental in years 2 and 3 of between CPI-0 and CPI+2.5%;

A CPI-0 basket control on all other core existent standalone fixed voice services available to residential customers’ charges in each year (the basket will also include the line rental in years 2 and 3 though subject to a sub-cap to avoid significant rebalancing between call charges and the line rental, which might harm consumers who make fewer calls).”

57. Ofcom also proposed to impose obligations on BT: (i) to cooperate with Ofcom in the testing or trialling of different measures to provide information to its customers, and - if justified in the light of that evidence - (ii) to implement measures in the manner and form as Ofcom may direct.<sup>32</sup>

#### BT’s proposed Commitments

58. On 24 October 2017, BT put forward a voluntary proposal in relation to the 2017 Review, presumably in order to avoid *ex ante* regulation involving mandatory price control by Ofcom (“**the BT Commitments**”).<sup>33</sup> The BT Commitments were submitted following “discussions between BT and Ofcom”: see BT letter to Ofcom of 24 October 2017 [Annex A to the Statement] [Annex 3] [CF Bundle/4/285]. The Proposed Class Representative has not had access to records of those discussions and reserves the right to amend this Claim Form following their disclosure.

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<sup>31</sup> §9.3.

<sup>32</sup> Provisional Conclusions, §9.5 [Annex 5] [CF Bundle/6/479].

<sup>33</sup> Published as part of the Statement [Annex 3] [CF Bundle/4/284-300].

59. The BT Commitments are at [**Annex 3**] [**CF Bundle/4/284-300**]. The Proposed Class Representative will rely on them at trial for their full meaning and effects. A summary of the key provisions is set out below.
60. BT offered a set of price commitments (referred to below as “**the Price Commitments**”) [**Annex 3**] [**CF Bundle/4/287-288**] comprising:
- (a) a forward-looking price reduction from 1 April 2018 of £7 (including VAT) per line per month on “Line Rental Services” for only its “Fixed Voice-Only Customers” where:
    - (i) Line Rental Services was defined as standard line rental and line rental plus.; and<sup>34</sup>
    - (ii) Fixed Voice-Only Customers was defined as “residential customers who purchase a Line Rental service under the BT brand and who do not also have a fixed broadband service provided to them, whether by BT or another Communications Provider”;
  - (b) an analogous reduction to prices for Line Rental Saver; and
  - (c) a commitment to cap increases across a basket of access and calls charges in line with the Consumer Prices Index for three years (i.e. until 31 March 2021).
61. The following categories of BT’s customers were excluded from the Price Commitments:
- (a) BT Basic and Home Phone Saver customers;<sup>35</sup>
  - (b) Split Purchase Customers;<sup>36</sup>

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<sup>34</sup> See §87 below for a description of line rental products offered by BT.

<sup>35</sup> See §88 below for a description of these products.

<sup>36</sup> BT Commitments, §2.2.2 [**Annex 3**] [**CF Bundle/4/288**]: BT undertook to exclude customers it believed to be Split Purchase Customers from the price reduction but to give such customers an opportunity to opt back in if BT’s information is incorrect.



- (c) Business customers;<sup>37</sup> and
- (d) Customers not supplied by BT’s “Consumer Business Unit”. This category includes, for example, customers of Plusnet plc and EE Limited.<sup>38</sup>

62. BT also offered:

- (a) “**Reporting Commitments**” according to which BT would, amongst other things, provide annual compliance statements to Ofcom until the end of BT’s financial year in 2021; and
- (b) “**Commitments to increase engagement**” whereby BT offered:
  - (i) to work with Ofcom to identify the form of communication with the best prospect of success in increasing engagement for BT Voice Only Customers; and
  - (ii) to send an annual statement to BT Split Purchase Customers detailing, amongst other things their total spend, potential cost savings and information on switching to another CP. No other commitments were offered in relation to BT Split Purchase Customers.

### The Statement

63. On 26 October 2017, Ofcom published the Statement [**Annex 3**] [**CF Bundle/4/256-306**]. The Proposed Class Representative relies on the Statement for its full meaning and effects. The key facts and findings are summarised below.
64. Ofcom reiterated its concerns regarding the detriment suffered by SFV Services customers including that:

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<sup>37</sup> BT Commitments, §2.2.3 [**Annex 3**] [**CF Bundle/4/288**]: BT undertook to “exclude any standalone voice customers from the price reduction that it has reason to believe are business customers. Such customers will be provided with an opportunity to opt back in if BT’s information is incorrect.”

<sup>38</sup> See BT Commitments, Recital C, footnote 2 and Annex A, §§ 2.5, 2.8 and 2.9 [**Annex 3**] [**CF Bundle/4/287-290**].

- (a) Customers purchasing voice-only services – often elderly people who have remained with the same provider for many years – are getting poor value for money (§1.2).
- (b) Line rental prices have increased significantly since 2009 (§1.3).
- (c) Competition is not benefiting customers purchasing landline telephone services on a standalone basis to the same extent as those purchasing in a bundle (2.5). In particular:
  - (i) “these customers have been progressively exposed to increasing line rental prices since 2009. This has been occurring despite wholesale charges for products used to provide line rental falling by up to 27% in real terms.” (§2.6)
  - (ii) Those increases have “a particular impact on elderly customers... over 40% of voice-only customers are over 75. Moreover, this group of consumers is generally more disengaged. Ofcom research has shown that 77% of voice only customers have never switched providers or considered doing so. These customers are receiving poor value for money given the rising line rental charges which they face” (§2.8)
  - (iii) “Split-purchase customers pay materially more...than they would pay for functionally equivalent dual-play services ...” (§3.51).
  - (iv) “Voice-only customers... have a very limited set of competitive choices, are highly disengaged from the market and have a more limited range of tools, in any event, through which to compare service options (as they generally have less access to the internet” (§4.6); and “low consumer engagement is one of the factors that has contributed to cementing BT’s position in the market” (§4.18).<sup>39</sup> See also §1.11 and §2.8 of the Statement on lack of

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<sup>39</sup> The Statement cites Ofcom, 2016, The Consumer Experience 2015, Research Annex, which states at 3.4.2: “The proportion of consumers purchasing a fixed line as a stand-alone product was unchanged in 2015 (31%, the same as in 2014), following a continued decline over several years as consumers moved to bundled offers. At an overall level, the proportion of consumers classified as ‘engaged’ in the fixed-line market is also unchanged since 2014, at 14%. However, half as many consumers in the standalone fixed-line market remain ‘engaged’ (8%) compared to those who bundle this service (17%). Lower engagement among stand-alone purchasers may be linked to the older age profile of this group of fixed-line customers;

customer engagement [**Annex 3**] [**CF Bundle/4/262**] and [**CF Bundle/4/267**].<sup>40</sup>

- (v) Only 8% of SFV Services customers are classified as “engaged” according to Ofcom’s Switching Tracker 2017 (see Figure 9 of Ofcom’s Consultation on end-of-contract and out-of-contract notifications dated 31 July 2018 [**Annex 12**] [**CF Bundle/13/802**]).

65. Ofcom’s detailed findings on market definition are addressed in the Parker Report [**Annex 2**] at §§85-88 [**CF Bundle/3/117-119**]. In summary:

- (a) Ofcom found, contrary to its original approach in the Provisional Conclusions, that Voice Only Customers and Split Purchase Customers are in separate markets for the purchase of SFV Services (§§1.10, 3.13 – 3.22 of the Statement [**Annex 3**] [**CF Bundle/4/262**] and [**CF Bundle/4/271-273**]) given, in particular, that:

- (i) “providers of standalone telephone services on Openreach’s network are in fact able to distinguish which of their customers take voice-only and which are split purchasers”;
- (ii) therefore, providers could in theory price discriminate between the two groups even though they had not done so in the past; and
- (iii) by offering the Price Commitments, BT had shown that in future it could and was willing to identify Voice Only Customers and charge them different prices from Split Purchase Customers.

- (b) As regards the supply of SFV Services to Voice Only Customers, Ofcom found that:

- (i) SFV access and SFV calls comprise different markets, even though consumers typically buy SFV access and SFV calls together. But whether or

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four in ten (40%) are aged 65+, and consumers in this age group are more likely than other age groups to be classified as inactive.”

<sup>40</sup> Voice Only Customers “generally do not engage with the market”, “tend to be older” and are “less likely to shop around for a better deal”.

not access and calls were treated as part of the same market did not fundamentally affect Ofcom’s competition assessment (§3.30-3.32 of the Statement);

- (ii) Dual play services are not in the same market as SFV access services bought by Voice Only Customers. In particular, Ofcom found that “BT did not provide any evidence to contradict our assessment that the presence of dual-play offers had not constrained standalone fixed voice prices to competitive levels. We have updated our analysis of price trends for standalone fixed voice and ADSL<sup>41</sup> services and the updated figures continue to support our position.” (§§3.23 to 3.29 of the Statement);
- (iii) the geographic scope of the relevant market was the UK excluding the Hull Area (§3.33 of the Statement); and
- (iv) the following products were not within the relevant market:
  - (i) BT Basic;
  - (ii) Business SFV access services; and
  - (iii) Mobile services.<sup>42</sup>

66. Ofcom found that BT had SMP in each of the markets for SFV access and SFV calls by Voice Only Customers (§3.34 to 3.48 of the Statement), concluding as follows:

“Overall, BT enjoys a significant market share within the markets for voice-only access and calls which have persisted over time. While competition was more intense in the early part of the century[, w]ith the movement of the focus of the market to bundles the market has become significantly more static. Competitors face significant barriers to expansion within the market and BT has been able to increase prices above the competitive level. In these circumstances, we do not consider that BT faces any significant constraints

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<sup>41</sup> ASDL stands for Asymmetric Digital Subscriber Line and is the most commonly available type of broadband, delivered through BT’s copper network.

<sup>42</sup> Statement, §3.5 [Annex 3] [CF Bundle/4/270].

on its ability to act independently within the markets for the purchase of voice-only access and calls.”<sup>43</sup>

67. Ofcom concluded that “BT currently holds a dominant position in the market for voice-only customers and the lack of competition enables it to maintain prices above the competitive level. We therefore consider that a significant price cut is important to alleviate the detriment suffered by voice-only customers... Like voice-only customers, split purchasers have suffered increases in line rental charges in recent years without significant offsetting benefits”.<sup>44</sup>
68. In relation to Split Purchase Customers, Ofcom:
- (a) reiterated its concerns that “Split-purchase customers pay materially more, for standalone voice and standalone broadband services, than they would pay for functionally equivalent dual-play services” (§3.51. See also §1.11,
  - (b) did not consider it necessary to proceed with a more formal market definition (or market assessment) exercise (§3.49);
  - (c) noted its findings in the Provisional Conclusions that SFV Services bought by Split Purchase Customers were not in the same market as Dual Play services, and that consultation responses had not provided evidence or arguments to lead it to change its view (§§3.50-3.52);
  - (d) noted that BT had a very high market share at 97% of Split Purchase lines, and that the declining and relatively small size of the market could make it difficult for providers of SFV Services to target Split Purchase Customers to encourage them to switch provider (§3.53);
  - (e) carried out some qualitative research, based on “a small and non-representative sample”, which suggested that “a more effective trigger for split purchase customers to increase their engagement could be through their broadband and/or TV package, rather than the landline” (§4.25); and

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<sup>43</sup> Statement, §3.48 [Annex 3] [CF Bundle/4/277].

<sup>44</sup> Statement, §§1.12 – 1.14 [Annex 3] [CF Bundle/4/262-263].

- (f) decided on balance that it was “more appropriate to allow time for Split Purchasers to become more engaged, and potentially to switch to dual play where that is a better option for them, rather than including them in a price control at this stage” (§4.26).

69. Ofcom accordingly accepted the BT Commitments [**Annex 3**] [**CF Bundle/4/284-300**] would monitor their impact and consider further intervention if the consumer detriment on the part of Voice Only Customers remained unaddressed (§4.23 of the Statement).

### **Ofcom’s 2020 Review**

70. On 10 December 2020, Ofcom announced a consultation entitled “Protecting voice-only landline telephone customers” regarding the BT Commitments (due to expire on 31 March 2021) and BT’s offer of further voluntary commitments (“**the 2020 Review**”) [**Annex 10**] [**CF Bundle/11/632-663**]. The 2020 Review contains the following relevant statements:

- (a) in 2019, there were still 1.2 million Voice Only Customers, representing approximately 5% of total residential customers and the “overwhelming majority of voice-only landline customers take their service from BT, which has a share of over 75% of such customers” (§2.1), which share had increased from 69% in 2017;<sup>45</sup>
- (b) the providers reported that “the largest source of ceased voice-only services relates to the death of the bill payer” (§3.3);
- (c) “concerns arising from the 2017 review...remain relevant” (§2.3) and Ofcom “continue[s] to believe that price protection for voice-only customers remains necessary to address [its] previous concerns from our last review in 2017, which included lack of competition in the market and poor value for money for this group of customers” (pg. 2, and see also §§2.27 – 2.30);
- (d) levels of switching among Voice Only Customers “are low, particularly for BT customers. Voice-only customers also tend to be older, from lower socio-economic

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<sup>45</sup> 2020 Review, §3.4.

grades, not working, and more financially vulnerable” (pg. 2 and see also §§3.9 – 3.13);

- (e) BT did not meet its voluntary commitments in 2018/19 as a result of a “modelling error” and BT made a charitable donation of £142k to recognise the impact of this error (§2.20); and
  - (f) while the majority of Voice Only Customers benefited from the implementation of the line rental price reduction, there is little competition in the market for this group of consumers (§3.6).
71. Ofcom proposed to accept BT’s offer of new voluntary commitments for a period of five years in respect of all products and services for Voice Only Customers (including any new products or services for Voice Only Customers introduced during the 5-year period) made up of:
- (i) an inflation-based control (CPI+0%) on the basket of line rental and call charges for voice-only products (excluding EE, Plusnet and BT’s business products and/or services);
  - (ii) an annual CPI+0% limit on prices for its Home Phone Saver product and a safeguard cap of CPI+2.5% for its line rental product; and
  - (iii) a commitment to provide information to Ofcom on its compliance with the new commitments on an annual basis.
72. Ofcom also found that “an indicative range for the estimated benefit for customers [of the new voluntary commitments by BT] would be around £6m to £14m in the first year and benefits would increase each year of the commitment period. On average over the five year period [of the new commitments], customer benefits in these scenarios could be between £17m to £34m on an annualised basis” (§4.8).
73. The 2020 Review does not address or contain any assessment of SFV prices charged to Split Purchase Customers.

**PART III: THE PROPOSED CLASS (RULE 75(3)(A)-(C))**

74. This part sets out the information and statements required to comply with Rule 75(3)(a)-(c), providing a description of the Proposed Class and Proposed Sub-classes and an estimate of their sizes.

**Description of the Proposed Class and Proposed Sub-classes (Rule 75(3)(a) and 75(3)(b))**Overview of the Proposed Class and Proposed Sub-classes

75. The Proposed Class is defined as:

“all persons domiciled in the United Kingdom (except in the **Hull Area**) who, during the **Claim Period**, bought a **BT Standalone Fixed Voice Service** except for the **Excluded Services**” (referred to below as “**the Proposed Class**” or “**Proposed Class Members**” as appropriate).<sup>46</sup>

76. For these purposes:

- (a) **BT Standalone Fixed Voice Service** (referred to below as a “**BT SFV Service**”) means any residential landline calling plan service provided by BT, except for the Excluded Services, which (i) includes landline line rental and (ii) has not been sold as part of a bundle with broadband. For these purposes, a bundle refers to a contract, or two or more closely related, linked or interdependent contracts which, individually or together, include and require the purchase of broadband as well as the landline calling plan service.
- (b) **Excluded Services** means BT Basic and BT Home Phone Saver.
- (c) **Hull Area** means the area defined as the Licence Area in the licence granted on 30 November 1987 by the Secretary of State under Section 7 of the Telecommunications Act 1984 to Kingston upon Hull City Council and Kingston Communications (Hull) plc.

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<sup>46</sup> For the avoidance of doubt, all defined terms used in the remainder of this Claim Form are the defined terms set out in the Class Definition and explanation of those terms herein, unless otherwise stated.



77. The Proposed Class is split into two Proposed Sub-classes, namely:
- (a) **BT Voice Only Customers:** Members of the Proposed Class who, during the applicable Claim Period as defined below, bought a BT SFV Service but did not, at the same time, buy a broadband service, either from BT or any other provider.
  - (b) **BT Split Purchase Customers:** Members of the Proposed Class who, during the applicable Claim Period as defined below, have bought at the same time both (i) a BT SFV Service; and (ii) a broadband service, either from BT or any other provider.
78. The **Claim Period** means:
- (a) for residential BT Voice Only Customers, between 1 October 2015 and 1 April 2018 inclusive;
  - (b) for business BT Voice Only Customers, between 1 October 2015 and the date of the Tribunal's final determination of the Claims made by the Proposed Sub-class of BT Voice Only Customers or their earlier settlement (or settlement of any part thereof); and
  - (c) for BT Split Purchase Customers, between 1 October 2015 and the date of the Tribunal's final determination of the Claims made by the Proposed Sub-class of BT Split Purchase Customers or their earlier settlement (or settlement of any part thereof).
79. Defined terms used in the definition of the Proposed Class and the Proposed Sub-classes (i.e. those in bold font above) are set out in the Glossary to this Claim Form [**Annex 1**] [**CF Bundle/2/82-85**], and further explanation of relevant terms is given below. All definitions are the same as or consistent with those used by Ofcom<sup>47</sup> and BT.<sup>48</sup>

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<sup>47</sup> See, for example, §1.12 and Figure 3.1 of the Provisional Conclusions [**Annex 5**] [**CF Bundle/6/376**] and [**CF Bundle/6/390**] and Annex A3 to the Statement [**Annex 3**] [**CF Bundle/4/303-305**].

<sup>48</sup> see, for example, §2.2 and Annex A to the BT Commitments [**Annex 3**] [**CF Bundle/4/288**] and [**CF Bundle/4/290-291**]

Nature of the Proposed Class

80. Members of the Proposed Class have characteristics which suggest that many of them are in groups that are considered to be vulnerable.<sup>49</sup> As Ofcom noted, SFV Customers tended to be:
- (a) **elderly / older**: see §§44(d), 64(a) and (c), and 70(b) and (d) above. See also the Litigation Plan at §§3.10 – 3.15 [**JLP Bundle/2/42-43**], and the Notice and Administration Plan at §§27 – 29 [**JLP Bundle/2/69**];
  - (b) **in lower socio-economic groups**: see §§44(e) and (f), and §70(d) above. See also the Litigation Plan at §§3.16 – 3.19 [**JLP Bundle/2/43-44**] and the Notice and Administration Plan at §§24– 25 [**JLP Bundle/2/68**]; and
  - (c) **disengaged**: see §§44(a) – (c), 64(c) and 70(d) and above. See also the Litigation Plan at §3.9 [**JLP Bundle/2/42**].
81. Based on Ofcom’s estimates (see Annex 8 to the Provisional Conclusions at §A8.2 [**Annex 6**] [**CF Bundle/7/530**]), 60% of SFV Customers are Voice Only Customers, with the remaining 40% being Split Purchase Customers.

Explanation of the Proposed Class

82. The following paragraphs explain the parameters of the Proposed Class and Proposed Sub-classes.<sup>50</sup> In defining their scope, the Proposed Class Representative has considered the guidance on class definition contained in §6.37 of the Guide, as follows:
- (a) “[T]he class should be defined as narrowly as possible without arbitrarily excluding some people entitled to claim”

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<sup>49</sup> Ofcom considers customers’ age, disability, income and geographical location to be factors that impact their vulnerability. See <https://www.ofcom.org.uk/about-ofcom/what-is-ofcom/consumer-vulnerability> [**JLP Bundle/4/166-171**].

<sup>50</sup> For the avoidance of doubt, the defined terms are consistent with, if not identical to, those used by Ofcom (see, for example, §1.12 and Figure 3.1 of the Provisional Conclusions [**Annex 5**] [**CF Bundle/6/376**] and [**CF Bundle/6/390**] and Annex A3 to the Statement [**Annex 3**] [**CF Bundle/4/303-305**]), and by BT (see, for example, §2.2 and Annex A to the BT Commitments [**Annex 3**] [**CF Bundle/4/288**] and [**CF Bundle/4/290-291**])

(b) “If the class is too broad, the proposed collective proceedings may raise too few common issues and accordingly not be worthwhile.”

83. For the reasons given below, the Proposed Class has been defined in such a way to ensure that all consumers<sup>51</sup> harmed by BT’s excessive prices for SFV Services are within its scope, and that any exclusions are based on an objective and clear rationale. In particular, and as explained below, the Proposed Class encompasses the different categories of customer which bought SFV Services from BT and which, Ofcom found, had suffered detriment as a result of BT’s pricing.

*Services within the Proposed Class*

84. The Proposed Class is made up of BT customers who bought a (standalone) BT SFV Service. As explained above, the term “standalone” connotes an SFV service which is not sold as part of a bundle with non-voice services such as broadband (and therefore excludes dual play and other multi play bundles).

85. A SFV Service is comprised of two distinct components:

(a) The access component (“**SFV access**”) is the provision of a fixed telephone line connection (*i.e.* a landline) with the ability, once the call component is added, to make calls. The access component is a pre-requisite for the purchase of outgoing calls and the vast majority of customers will make some calls. The access component is usually paid for by a periodic fixed line rental charge for access to the network.

(b) The calls component (“**SFV calls**”) allows the consumer to make outgoing call over the telephone line. This is often paid for by a variable payment for calls made under a calling plan.

86. Access services are typically offered by providers as part of a “calling plan package” which encompasses both line rental and a call allowance; indeed BT does not offer “standalone” line-rental services (*i.e.* line rental without a call allowance): see

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<sup>51</sup> Though please see further detail in relation to Home Phone Saver customers below.

Provisional Conclusions, §§3.23 – 3.24 [**Annex 5**] [**CF Bundle/6/390-391**]. BT SFV Services therefore encompass all BT’s calling plan packages (except BT Basic and Home Phone Saver, as explained below), which include landline rental.<sup>52</sup>

87. At all material times during the Claim Period, BT offered three line rental products and three calling plan services, each of which are within the scope of BT SFV Services, as set out below:

(a) The relevant line rental services are:<sup>53</sup>

- (i) **Standard Line Rental**, the standard product available to those paying on direct debit;
- (ii) **Line Rental Saver**, offering a discount for up-front payment by credit or debit card at the start of the year; and
- (iii) **Line Rental Plus**, a product allowing for payment by means such as cash or cheque.

(b) The relevant calling plans are:

- (i) **Unlimited Weekend Calls** which covers weekend calls to fixed numbers only, and was offered free of charge with all line rental services until October 2019.<sup>54</sup>
- (ii) **Unlimited Evening and Weekend Calls** which is charged as an addition to line rental.
- (iii) **Unlimited Anytime Calls** which is charged as an addition to line rental and covers daytime, evening, and weekend calls.<sup>55</sup>

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<sup>52</sup> Such as Standard Line Rental, Line Rental Saver and Line Rental Plus.

<sup>53</sup> For more detail on these products please see the Parker Report [**Annex 2**], §§60 – 61 [**CF Bundle/3/109**].

<sup>54</sup> See the Parker Report [**Annex 2**], §59 [**CF Bundle/3/109**].

<sup>55</sup> See Provisional Conclusions, §3.24 [**Annex 5**] [**CF Bundle/6/390-391**] and Annex 9, page 113 [**Annex 6**] [**CF Bundle/7/601**].

*Excluded Services*

88. The following services provided by BT have been excluded for the reasons given below:

(a) **BT Basic**, which:

- (i) is a service provided to customers who are recipients of specific means-tested Government benefits. To qualify for BT Basic a customer has and had to receive one of the following benefits: income support, income-based job seekers allowance, pension credit (guarantee credit), employment and support allowance (income related), and universal credit (and are on zero earnings);
- (ii) was excluded from the scope of the relevant affected market(s) as provisionally defined by Ofcom and (consequently) Ofcom’s proposed price control and the BT Commitments;<sup>56</sup> and
- (iii) is offered at prices well below prices for other line rental products: see Parker Report at §64.<sup>57</sup>

(b) **BT Home Phone Saver**, which:<sup>58</sup>

- (i) is a tariff which packages together line rental, calls and a number of additional features;<sup>59</sup>

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<sup>56</sup> Provisional Conclusions, §§3.26, 3.50 – 3.53 [Annex 5] [CF Bundle/6/391] and [CF Bundle/6/398] and at Annex 8 at §A8.111-A8.113 [Annex 6] [CF Bundle/7/563-564].

<sup>57</sup> And Provisional Conclusions, Annex 8 §A8.112 [Annex 6] [CF Bundle/7/564].

<sup>58</sup> The term “BT Home Phone Saver” covers each and any year’s version in the Claim Period e.g. BT Home Phone Saver 2019 for the year 2019.

<sup>59</sup> Provisional Conclusions, Annex 8, Figure A8.38 [Annex 6] [CF Bundle/7/565].

- (ii) provides a substantial discount compared with purchasing all of the individual features separately, but is more expensive than buying a line rental product with weekend calls;<sup>60</sup>
  - (iii) was excluded from the scope of Ofcom’s proposed price control;<sup>61</sup> and
  - (iv) in respect of which there is insufficient publicly available evidence to determine whether prices were excessive (see the Parker Report, §§308-311 [Annex 2] [CF Bundle/3/180]).
- (c) **Business services offered by BT**, which were excluded from Ofcom’s proposed price control and the BT Commitments. In particular, Ofcom found that business services are in a separate market from residential SFV Services. As Ofcom noted, “there is limited scope for demand-side substitution from residential to business services because in order to purchase a business access line from BT a customer is required to submit a company registration number, which would prevent a residential user from acquiring a business line”.<sup>62</sup> See also Parker Report, §§107-118 [Annex 2] [CF Bundle/3/123-128].
89. For the avoidance of doubt, as set out in the Draft Collective Proceedings Order [Annex 7] [CF Bundle/8/608-611], various categories of individuals (such as lawyers and Tribunal panel members) are also excluded on the conventional approach in collective proceedings.

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<sup>60</sup> Provisional Conclusions, Annex 8 §§8.116 and Figure A8.38 [Annex 6] [CF Bundle/7/564-565]. See also Parker Report, §64 [Annex 2] [CF Bundle/3/111-112].

<sup>61</sup> Provisional Conclusions Annex 9, Schedule, §2.8(vi)(c) [Annex 6] [CF Bundle/7/599-600].

<sup>62</sup> Provisional Conclusions, §3.55: “there is limited scope for demand-side substitution from residential to business services because in order to purchase a business access line from BT a customer is required to submit a company registration number, which would prevent a residential user from acquiring a business line” [Annex 5] [CF Bundle/6/399]. Note this is not to be confused with residential SFV services bought by business customers.

90. As regards the geographic market, the Hull Area is excluded because BT does not offer SFV Services in that area; the incumbent network provider in Hull is KCOM (formerly Kingston Communications).<sup>63</sup>

*The Claim Period*

91. The Claim Period differs between the Proposed Sub-classes for the sole reason that the price control aspects of the BT Commitments did not cover either BT Split Purchase Customers or BT Voice Only Customers who, despite buying residential services, were business users.

*Reasons for defining a single class*

92. The Proposed Class Representative seeks the Tribunal’s permission to bring collective proceedings on behalf of a single class of persons comprising customers of BT (the majority of which were/are consumers purchasing in a personal capacity)<sup>64</sup> who paid excessive prices to BT for SFV Services during the Claim Period. For the reasons given above, that class of persons is made up of two broad customer groups: BT Voice Only Customers and BT Split Purchase Customers.
93. The BT SFV Services purchased by BT Voice Only and BT Split Purchase Customers are identical; as the Parker Report explains, from a “functional characteristics’ perspective” there is no reason to separate the two customer groups.<sup>65</sup> The distinguishing feature is that, in addition to the excessively priced service, BT Split Purchase Customers separately buy an additional service, namely, broadband, whereas BT Voice Only Customers do not.
94. For the reasons given at §§152 - 155 below and as explained by the Parker Report,<sup>66</sup> the economic methodology for determining: (i) the level of the unlawful overcharge paid by

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<sup>63</sup> Ofcom estimated that around 17% of SFV Customers were small and medium sized enterprises (Provisional Conclusions, §3.11) [Annex 5] [CF Bundle/6/387-388].

<sup>64</sup> Ofcom estimated that around 17% of SFV Customers were small and medium sized enterprises (Provisional Conclusions, §3.11) [Annex 5] [CF Bundle/6/387-388].

<sup>65</sup> Parker Report, §133 [Annex 2] [CF Bundle/3/132].

<sup>66</sup> Parker Report, §132 and subsequent sections [Annex 2] [CF Bundle/3/131-255].

consumers to BT for SFV Services and (ii) the losses thereby suffered by those consumers, is common to the two customer groups.

95. In the premises, it is appropriate to define a single class in respect of both customer groups.

Explanation of the Proposed Sub-classes and how it is proposed that their interests will be represented

96. Although a single class is proposed, the Proposed Class Representative suggests defining each customer group as comprising a discrete sub-class, in the interests of clarity, given that:

- (a) each customer group comprises a discrete economic market: see the Parker Report, §§131-141 [**Annex 2**] [**CF Bundle/3/131-134**].
- (b) the BT Commitments reduced prices solely to the Voice Only Customer group (save that businesses buying residential SFV services were carved out and so denied the price reduction: see §§61 and 80(c) above and §101 below.) As such, the claim period for Voice Only Customers ends on 1 April 2018, the date on which the BT Commitments became effective (save for Voice Only Customers who are businesses for whom the claim period is the same as that applicable to Split Purchase Customers).<sup>67</sup>

97. For the avoidance of doubt, there is no conflict of interest between the Proposed Sub-classes, and accordingly the Class Representative can properly represent the interests of all Proposed Class Members. The two Proposed Sub-classes only differ in respect of whether they purchased a fixed broadband service (separately) or not. BT Voice Only Customers bought only a telephone service and not broadband, whereas BT Split Purchase Customers bought a telephone service and a broadband service (but, crucially, not as a bundle).

98. Nor does the Proposed Class Representative anticipate that the Proposed Sub-classes will require separate case management. As described in more detail below at §§152 - 155, the

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<sup>67</sup> See §§2.2 and 2.2.2 of the BT Commitments [**Annex 3**] [**CF Bundle/4/288**].



analysis of the relevant market and dominance for each Proposed Sub-class are similar and draw on related evidence. The methodology for assessing overcharge and calculating damages do not differ between the Proposed Sub-classes, save to reflect the different time periods for which excessive prices were charged.

#### Other potential sub-classes

99. Other sub-classes (or sub-sub-classes) are unnecessary.
100. First, Split Purchase Customers are divided by Ofcom into two further sub-categories: Split Service and Split Supplier Customers. See §§39 - 43 above. However, whether a BT Split Purchase Customer buys their separate broadband service from BT (a Split Service Customer) or from another provider (a Split Supplier Customer) does not affect the services provided or the prices paid to BT for SFV Services.<sup>68</sup> As such, it is not a material distinction for the purposes of the assessment of infringement or quantum.<sup>69</sup>
101. Second, there is no need for business purchasers of BT SFV Services to be defined as a separate sub-class. The Proposed Class Representative does not currently know the size of this group although Ofcom gives a very broad-brush estimate of around 17% of SFV Customers.<sup>70</sup> Although the assessment of damages in respect of such purchasers may raise issues such as amounts of VAT which have been reclaimed and/or pass on if raised by BT, all other aspects of the assessment of liability and quantum are common with other Proposed Class Members: see §§152 - 155 below. In the premises, there is no need to define this group as a separate sub-class or sub-sub class. The Proposed Class Representative will also, of course, keep such matters under review, but it is anticipated

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<sup>68</sup> See also Ofcom’s finding that “survey evidence from split-supplier customers is a reasonable proxy for Split Purchasers as it estimates that split-supplier customers account for around 80% of Split Purchasers, with the remaining 20% being split-service customers”: Ofcom’s Evidence at §§1.103 – 1.107) [**Annex 4**] **CF Bundle/5/342**].

<sup>69</sup> The distinction between split-supplier and split-service sub-groups of Split Purchase Customers only appears in some evidence relied upon by Ofcom where it relies on some data from only Split Supplier customers. In any event, Ofcom states “survey evidence from split-supplier customers is reasonable proxy for Split Purchasers as it estimates that split-supplier customers account for around 80% of Split Purchasers, with the remaining 20% being split-service customers”: Ofcom’s Evidence at §§1.103 – 1.107) [**Annex 4**] [**CF Bundle/5/342**].

<sup>70</sup> Ofcom stated that: “In total, 9% of SMEs purchase a (residential) SFV service. With 5.4 million SMEs in the UK, this would suggest around 490,000 out of 2.9 million SFV customers are SMEs – around 17%.” Provisional Conclusions, §.3.11 [**Annex 5**] [**CF Bundle/6/387-388**].

that it will be possible to manage these additional steps, if necessary, in the context of the wider Proposed Class and after liability is established.

**Estimate of the size of the Proposed Class and Proposed Sub-classes (Rule 75(3)(c))**

102. Rule 75(3)(c) of the Rules requires the provision of “an estimate of the number of class and sub-class members and the basis for that estimate”. The Guide at §6.37 states that “although the claim form must give an evidence based estimate of the size of the class, it is not necessary to identify each class member (in an opt-out claim) or specify exactly how many persons are within the class”.
103. It is estimated that the size of the Proposed Class (i.e. those who purchased BT SFV Services in the Claim Period) is around 2.31 million individuals (Parker Report, §418); with the BT Voice Only Customer Sub-class estimated at around 1.23 million and the BT Split Purchase Customer Sub-class is estimated at around 1.08 million members (Parker Report, §418). For the avoidance of doubt, these estimates reflect the total number of individual Members of the Proposed Class across the Claim Period, rather than the number of Members of the Proposed Class purchasing BT’s SFV Services at any given time.<sup>71</sup>
104. The above Class size estimate is based on publicly available information and calculated by estimating the number of BT SFV Customers at the beginning of the Claim Period (by, for example, removing customers who had the Excluded Services) and adjusting that number to reflect the estimated number of consumers who joined the Class over the Claim Period by applying an average monthly switching rate (Parker Report, §§420-426 [Annex 2] [CF Bundle/3/214-216]).
105. In the light of the BT Commitments - according to which BT undertook to grant the discount to BT Voice Only Customers and to send annual statements to BT Split Purchase Customers - BT assumedly has records of the precise number of customers that belong to the Proposed Class and Proposed Sub-classes. As such, the Proposed Class

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<sup>71</sup> In 2017, for example, Ofcom stated that there were 2.9 million SFV Customers, which accounted for 11% of total residential landline customers (Provisional Conclusions, §1.12). Of these, approximately 1.7 million were Voice Only Customers and 1.2 million were Split Purchasers. (These numbers include Home Phone Saver customers, which are excluded from the Class and hence Parker’s Class size estimates.)

Representative anticipates that this estimate will be replaced with an exact Class size following disclosure by BT.

**PART IV: THE INFRINGEMENT AND BASIS OF THE CLAIMS (RULE 75(3)(F)-(H) AND (J))**

106. This part sets out the information and statements required by Rule 75(3)(f)-(h) and (j), in particular a concise statement of the relevant facts; a concise statement of the contentions of law which are relied on; and the Proposed Class Representative’s observations on which part of the UK the proceedings are to be treated as taking place under Rule 18.

**Contentions of law**

107. In accordance with Rule 75(3)(h), the following section contains a concise statement of contentions of law relied on by the Proposed Class Representative. The contentions of law set out below will be elaborated upon in written and/or oral submissions in due course.

108. Section 18 of the Competition Act 1998 (the “**Chapter II Prohibition**”) prohibits “any conduct on the part of one or more undertakings which amounts to the abuse of a dominant position in a market if it may affect trade within the United Kingdom”.

Market definition

109. According to the Tribunal: “In order to determine whether, in any given case, an undertaking has the necessary degree of economic strength or, to use the more modern term, market power, so as to give rise to dominance, it is self-evidently necessary to define the market in which that market power is said to exist”. (*Aberdeen Journals v Director General of Fair Trading* [2002] CAT 4, §88).

110. As to market definition, it is well established that:

“The concept of the relevant market in fact implies that there can be effective competition between the products or services which form part of it and this presupposes that there is a sufficient degree of interchangeability between all the products or services forming part of the same market in so far as a specific use of such products or services is concerned. The interchangeability or substitutability is not assessed solely in relation to the objective

characteristics of the products and services at issue, but the competitive conditions and the structure of supply and demand on the market must also be taken into consideration". (Case T-699/14 *Topps Europe v Commission* EU:T:2017:2, §81).

### Dominance

111. A dominant position means: “a position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained on the relevant market by affording it the power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers” (*United Brands v Commission*, Case 27/76 EU:C:1978:22 (“*United Brands*”), §65).
112. A market share in excess of 50% gives rise to a presumption of dominance (*AKZO v Commission*, Case C-62/86 EU:C:1991:286, §60).

### Abuse: excessive pricing

113. Excessive pricing is an established head of abuse: see the Chapter II Prohibition which prohibits “*directly or indirectly imposing unfair purchase or selling prices.*”
114. The seminal EU judgment on excessive pricing is *United Brands*, in which the CJEU confirmed that the imposition of unfair selling prices is an abuse, and held that:
- (a) It is advisable to ascertain whether the dominant undertaking has used its dominant position to reap trading benefits which could not have been obtained in normal and sufficiently competitive conditions.<sup>72</sup>
  - (b) A price that bears no reasonable relation to the economic value of the product supplied is excessive.<sup>73</sup>
  - (c) While noting that other ways could be devised, one approach for identifying excessive prices involves addressing the questions in the following two-stage analysis:

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<sup>72</sup> *United Brands*, §249. See also the Chancellor in *Flynn CA*, §249 which described this element as “the overarching exercise”.

<sup>73</sup> *Ibid.* §235.

- (i) Is the difference between the costs actually incurred and the price actually charged excessive?
- (ii) If so, is the price (i) unfair in itself or (ii) when compared to competing products?<sup>74</sup>

115. In the subsequent case of *AKKA LAA Case C-177/16 ECLI:EU:C:2017:689*, the CJEU confirmed that the difference between the disputed price and the relevant competitive benchmark must be “significant and persistent”.<sup>75</sup>

116. The Proposed Class Representative will refer in written and oral submissions, insofar as relevant, to the various EU and domestic cases, decided in the wake of *United Brands*, concerning the applicable legal and economic principles for determining whether a price is excessive. The most recent such judgment is that of the Court of Appeal in *CMA v Flynn* [2020] EWCA Civ 339 (“*Flynn CoA*”), which sets out the following (non-exhaustive) principles:<sup>76</sup>

- (a) The basic test for abuse is whether the price is unfair. In broad terms, a price will be unfair when the dominant undertaking has reaped trading benefits which it could not have obtained in conditions of normal and sufficiently effective competition i.e. workable competition.
- (b) One example of an unfair price is a price that is “excessive” because it bears no reasonable relation to the economic value of the good or service.
- (c) There is no single method or “way” in which abuse might be established and competition authorities have a margin of manoeuvre or appreciation in deciding which methodology to use and which evidence to rely on.

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<sup>74</sup> Ibid., §252.

<sup>75</sup> §§55-56, 61.

<sup>76</sup> *Flynn CoA*, §97.

- (d) A competition authority might use one or more of the alternative economic tests which are available but there is no rule of law requiring them to use more than one test or method in all cases.
  - (e) In analysing whether the end price is unfair, a competition authority may look at a range of relevant factors including but not limited to evidence and data relating to the dominant undertaking and / or evidence of comparables drawn from competing products and/or any other relevant comparable, or all of these. There is no fixed list of categories of relevant evidence.
117. For the avoidance of doubt, the Proposed Class Representative will say that the principles summarised at §§116(d) and (e) above apply equally to private claimants seeking redress in respect of unlawful excessive prices.
118. Green LJ also observed that the above propositions are supported by the economic literature and, amongst other things, that: all cases are highly fact and context specific; there are many different tests for determining if a price is excessive and unfair and that it is economically rational that competition authorities should have a margin of appreciation as to the choice of method and evidence that they seek to rely on.<sup>77</sup>
119. The Court of Appeal also emphasised that:
- (a) There is no discrete component of the test which assesses economic value: the reference to “economic value in *United Brands* is part of the overall descriptor of the abuse; it is not the test”.<sup>78</sup>
  - (b) When the *United Brands* test is properly applied, it is capable of assessing economic value so that if a price is excessive it bears “no reasonable relationship to economic value”.<sup>79</sup>

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<sup>77</sup> *Flynn CoA*, §107.

<sup>78</sup> *Green LJ*, §172; *Vos LJ*, §282.

<sup>79</sup> §172.

- (c) The simple fact that a consumer will or must pay the price that a dominant undertaking demands is not an indication that it reflects a reasonable relationship with economic value. Dependency of the user on the impugned product is relevant.<sup>80</sup> A proxy might be what consumers are prepared to pay for the good or service in an effectively competitive market.<sup>81</sup>
- (d) Equally, if there is evidence of the prices being charged in relevant, comparator, markets which were effectively competitive then those prices could be capable of acting as proxy evidence of the economic value of the product in question.

### **The Infringement**

120. The Claims are for loss and damage caused by BT's breach of statutory duty on account of its infringement of the Chapter II Prohibition by virtue of its excessive charges for BT SFV Services (or alternatively BT SFV access<sup>82</sup>) during the Claim Period.
121. Whilst the Claims are of a standalone nature, because they are not in respect of a final infringement decision within the meaning of section 58A of the Competition Act 1998 (see Rule 75(3)(f)), they rely in large part on the facts and findings by Ofcom set out in the documents pertaining to the 2017 Review, which are summarised at in Part II above.
122. The Proposed Class Representative has, thus far, seen non-confidential copies of those documents only. Accordingly, whilst this Claim Form is particularised as far as possible, the Proposed Class Representative reserves his right to amend this Claim Form and/or to provide further particulars following disclosure and/or the preparation of expert reports and/or factual evidence.
123. The best particulars of infringement which the Proposed Class Representative can presently provide, based on publicly available material, are set out below. Despite the gap in information currently available to the Proposed Class Representative, the

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<sup>80</sup> §167. See also Case 395/87 *Ministere Public v Tournier*.

<sup>81</sup> *Flynn CoA*, §155.

<sup>82</sup> For the avoidance of doubt, (i) BT SFV access is a component of BT SFV Services and (ii) any reference to the BT SFV access is a reference to any individual, or all, of the access component options available from BT in the Claim Period, namely BT Standard Line Rental, BT Line Rental Plus and/or BT Line Rental Saver.

threshold of a “triable issue” (*Merricks v Mastercard* [2020] UKSC 51 at §46) as to the excessive and unfair nature of BT’s prices is clearly satisfied.

### Market definition

124. While the precise delineation of the affected markets will be a matter for factual and expert evidence at trial, the Proposed Class Representative avers that the relevant product and geographic markets (“**the Relevant Markets**”) are:<sup>83</sup>

- (a) the market for SFV access and SFV calls (together “**SFV Services**”) supplied in the United Kingdom (excluding the Hull Area) to Voice Only Customers, referred to below as “**the market for the supply of SFV Services to UK Voice Only Customers**”; and
- (b) the market for SFV access and SFV calls supplied in the United Kingdom (excluding the Hull Area) to Split Purchase Customers, referred to below as “**the market for the supply of SFV Services to UK Split Purchase Customers**”.

125. Alternatively, if (contrary to the Parker Report):

- (a) there are separate product markets for SFV access and SFV calls, then the Relevant Markets are each or any of the following:
  - (i) the market for SFV access in the United Kingdom (excluding the Hull Area) supplied to Voice Only Customers;
  - (ii) the market for SFV calls in the United Kingdom (excluding the Hull Area) supplied to Voice Only Customers;
  - (iii) the market for SFV access in the United Kingdom (excluding the Hull Area) supplied to Split Purchase Customers; and/or
  - (iv) the market for SFV calls in the United Kingdom (excluding the Hull Area) supplied to Split Purchase Customers.

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<sup>83</sup> Parker Report, §§30 and 32 [**Annex 2**] [**CF Bundle/3/101-102**].



- (b) Further or alternatively, if, notwithstanding BT’s ability to price discriminate between Voice Only and Split Purchase customers, those customers groups form part of the same market, then the Relevant Markets defined at (a)(i) and (a)(iii) above form a single market for SFV access (not segmented by customer group); and the markets at (a)(ii) and (a)(iv) form a single market for SFV calls (not segmented by customer group).

126. For the avoidance of doubt, the Relevant Markets, exclude each of the following services:

- (a) Dual Play services, as they do not sufficiently constrain the prices charged to Voice Only and/or Split Purchase Customers of SFV Services, for the reasons given above §§65, 68 and 84 and by the Parker Report at §§142-170 [**Annex 2**] [**CF Bundle/3/134-143**].
- (b) Business services, because they are not materially substitutable with residential SFV Services, for the reasons given above at §§37, 61, 65 and 88 and/or by the Parker Report at §§107-118 [**Annex 2**] [**CF Bundle/3/123-128**].
- (c) Mobile services because they are not materially substitutable with SFV Services and/or the prices charged for mobile services do not sufficiently constrain SFV prices for the reasons given above at §§35, 37 and 65 and/or by the Parker Report at §§171-179 [**Annex 2**] [**CF Bundle/3/143-144**].
- (d) BT Basic for the reasons given above at §§37, 61, 65 and 88 and/or by the Parker Report at §180 [**Annex 2**] [**CF Bundle/3/144-145**].

### Dominance

127. BT held a dominant position, within the meaning of the Chapter II Prohibition, on each or any of the Relevant Markets during the Claim Period.

### *SFV Services supplied to Voice Only Customers*

128. At all material times within the Claim Period, BT has held and/or holds a dominant position within the meaning of the Chapter II Prohibition in the market(s) for the supply of SFV Services to UK Voice Only Customers and/or the market for SFV access supplied

to UK Voice Only Customers. In particular, and without prejudice to the generality of the foregoing:

- (a) Ofcom provisionally concluded that BT enjoyed a position of SMP in respect of both SFV access and SFV calls (see §§45, 49 and 66 above and Provisional Conclusions, §§4.80 and 5.36 [**Annex 5**] [**CF Bundle/6/429**] and [**CF Bundle/6/437**]).
- (b) BT sustained a share of SFV access to Voice Only Customers, as measured by the number of lines, considerably above 50% (and no less than 68%) over the period 2013 to Q1 2017. It is averred that BT's share is likely to have remained above 61% for the remainder of the Claim Period (Parker Report, §§202-209 [**Annex 2**] [**CF Bundle/3/150-152**]);
- (c) BT's share across both SFV access and SFV calls to Voice Only Customers, on both a volume and revenue basis, is likely to have been materially in excess of 50% throughout the Claim Period (Parker Report, §§210-219) [**Annex 2**] [**CF Bundle/3/152-154**];
- (d) There are significant barriers to entry and expansion resulting from the limited level of customer switching, creating significant challenges for new entrants or existing operators seeking to expand (Parker Report, §§220-224 [**Annex 2**] [**CF Bundle/3/155-156**]);
- (e) The gap between BT's prices for SFV access and its costs (as measured by the charges for key wholesale inputs) increased significantly over time (Parker Report, §§226-227 [**Annex 2**] [**CF Bundle/3/156**]);
- (f) BT acted as a price leader in relation to SFV access, with other CPs following its increases in line rental in terms of both timing and magnitude (Parker Report, §§228-231 [**Annex 2**] [**CF Bundle/3/157-158**]);
- (g) In relation to SFV calls, BT's prices have on average increased since 2009, while prices charged by its competitors have decreased (Parker Report, §§232-239 [**Annex 2**] [**CF Bundle/3/158-160**]);

- (h) While much of the relevant evidence on profitability is redacted from the Provisional Conclusions and Statement, the available evidence suggests that BT's profitability per fixed voice line has been high and increasing over time. For example, Ofcom found that BT's EBIT margins had been increasing and were at 34-42% in 2015/6, and that BT was making higher profits on fixed voice customers than its rivals (Parker Report, §§240-245 [**Annex 2**] [**CF Bundle/3/160-161**]); and/or
- (i) Customers do not have countervailing buyer power (Parker Report, §§246-247 [**Annex 2**] [**CF Bundle/3/161**] and Provisional Conclusions, §4.80 [**Annex 5**] [**CF Bundle/6/429**]).

*SFV Services supplied to Split Purchase Customers*

129. At all material times during the Claim Period, BT has held and/or holds a dominant position within the meaning of the Chapter II Prohibition in the market(s) for SFV Services supplied to UK Split Purchase Customers or, alternatively, the market for SFV access supplied to UK Split Purchase Customers. In particular (and without prejudice to the generality of the foregoing):

- (a) §§128(a), (e), (f), (g), (h) and (i) above are repeated (as they apply equally to UK Split Purchase Customers).
- (b) Although Ofcom did not consider it necessary to make a formal market assessment in respect of Split Purchase Customers in the Statement, it noted that BT had a very high market share at 97%, and that the declining and relatively small size of the market could make it difficult for providers of SFV Services to target Split Purchase Customers to encourage them to switch provider (see §68 above);
- (c) Ofcom estimated that, measured by number of lines, BT's share of SFV access to Split Purchase Customers was close to 100% over the period 2013 to Q1 2017. It is likely to have remained above 97% for the remainder of the Claim Period (Parker Report, §§250-253 [**Annex 2**] [**CF Bundle/3/162-163**]);

- (d) The Parker Report notes that while relevant data is redacted from Ofcom's Provisional Conclusions, based on the information currently available to him, BT's volume and revenue market shares for SFV services to Split Purchase Customers appear to have been persistently above 50%, whether the market is defined to include both the access and calls components, or the access component only (Parker Report, §§254-260) [Annex 2] [CF Bundle/3/163-165]; and
- (e) There are barriers to entry and expansion resulting from the limited level of customer switching, making it difficult for a new entrant of existing operator to attract new customers (Parker Report, §§261-264) [Annex 2] [CF Bundle/165-166].

130. Alternatively, to the extent that Voice Only and Split Purchase Customers are in the same market, contrary to the Parker Report, it is averred that BT is dominant in the relevant market(s) for the supply of SFV Services and/or SFV access for those customers combined, for the reasons set out above.

Abuse: excessive pricing

131. In the light of the matters pleaded above and, in particular, the evidence set out in the Parker Report, at all material times during the Claim Period (or, alternatively, any part thereof), BT has imposed excessive prices (on each or any of the Relevant Markets), in breach of the Chapter II Prohibition, for the provision of BT SFV Services, or alternatively for the provision of BT SFV access, to BT Voice Only and/or BT Split Purchase Customers in the UK (excluding Hull).

Particulars of breach

132. The prices for BT SFV Services, or alternatively BT SFV access, to BT Voice Only and/or BT Split Purchase Customers in the UK (excluding Hull) during the Claim Period:
- (a) enabled BT to reap trading benefits which could not have been obtained in normal and sufficiently effective conditions; and/or
  - (b) are excessive because they bear no reasonable relation to either (i) the economic value of the BT SFV Services and/or the BT SFV access supplied and/or (ii) the

costs of providing BT SFV Services and/or the BT SFV access (for the purposes of the ‘first limb’ of the *United Brands* test at §114(c)(i) above); and/or

- (c) are unfair in themselves and/or when compared to comparable services and/or other relevant proxy/proxies for the prices for BT SFV Services which would obtain in conditions of normal and sufficiently effective competition (for the purposes of the ‘second limb’ of the *United Brands* test at §§114(c)(ii) above).

133. Without prejudice to the generality of the foregoing, the impugned access prices are significantly and persistently above:

- (i) residential landline rental prices charged by BT in 2009, adjusted to reflect changes in the key cost input, which as the Parker Report explains at §§289-322 of his Report, provides a good proxy for the competitive price level for SFV access throughout the Claim Period, and is the best available and most robust competitive benchmark for these purposes (Parker Report, §§323-338 [Annex 2] [CF Bundle/3/184-190]). As Mr Parker explains this benchmark also encapsulates a ‘cost plus’ approach for the purposes of the first limb of the *United Brands* test (Parker Report §315);
- (ii) further or alternatively, each or both of the further potential proxies relied on by the Parker Report, as “sensitivities” only, which are: residential landline rental prices charged by BT in 2009 without any adjustment to reflect changes in costs; and the prices which BT undertook to charge BT Voice Only Customers under the Commitments (Parker Report, §§323-338)

while there is not evidence of any offsetting effect from calls prices (Parker Report, §§339-361).

**(“the Infringement”).**

134. For example, as the Parker Report explains at §326 [Annex 2] [CF Bundle/3/185-186], the price of BT Standard Line Rental exceeded the competitive level by 51% above the competitive level in October 2015 for both BT Voice Only Customers and BT Split Purchase Customers; by 63% above the competitive level in April 2018 for BT Split

Purchase Customers; and by 65% above the competitive level in the latest available period, August 2020 for BT Split Purchase Customers, using Mr Parker's preferred benchmark.

135. It is further averred that the prices for Line Rental Plus and Line Rental Saver were excessive to the same or similar degree as BT Standard Line Rental, on the basis that differences in price between each of those services and BT Standard Line Rental reflect (wholly or in part) cost differences between each of those services and BT Standard Line Rental: the Parker Report, §§327-331 [**Annex 2**] [**CF Bundle/3/186-188**]. This conclusion is further supported by Ofcom's Provisional conclusions [**Annex 5**] [**CF Bundle/6/487-607**]:

- (a) that BT's prices were approximately £5 to £7 per line per month above a level defined using competitive benchmarks;<sup>84</sup> and
- (b) that a price cut of between £5 and £7 (including VAT) per line per month would allow profitability at a level that would be consistent with competition developing and would significantly reduce the direct customer detriment attributable to BT's pricing behaviour.<sup>85</sup>

136. For the avoidance of doubt, the above averments are supported by Ofcom's findings in the 2017 Review and supporting evidence (and the 2020 Review) and the BT Commitments: see, in particular, §§46 – 49; 50 – 57; 58 – 62; 64; and 70 – 71 above. Whilst the Proposed Class Representative reserves the right to plead further particulars of Infringement following disclosure and/or evidence, the threshold of a triable issue as to the excessive charges imposed by BT is clearly met. BT has a case to answer.

### **Causation / Loss and damage**

137. The Proposed Defendant's breach(es) of statutory duty, arising out of the Infringement, has/have caused loss and damage to Proposed Class Members during the Claim Period, consisting in the difference between the prices which they, in fact, paid for the BT SFV

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<sup>84</sup> See §§20, 48, 54 and 56 above and Provisional Conclusions, §6.4, referencing the analysis at Section 8 and Annex 5 [**Annex 5**] [**CF Bundle/6/438**].

<sup>85</sup> Ibid. and Provisional Conclusions, §§8.30 and 9.6 [**Annex 5**] [**CF Bundle/6/469**] and [**CF Bundle/6/479-480**].

Services (or alternatively BT SFV access services) and the prices which they would have paid for those services in the absence of the unlawful Infringement. But for the Infringement, the Members of the Proposed Class would not have suffered this loss and/or damage.

Particulars of loss and damage

138. The Members of the Proposed Class are entitled to the difference between the prices which they, in fact, paid for the BT SFV Services (or alternatively BT SFV access) and the prices which they would have paid for those services but for the unlawful Infringement.
139. Without prejudice to the Proposed Class Representative's right to provide further particulars of loss and damage following disclosure, expert reports and/or factual evidence, the current best estimate of the loss and damage incurred by the Proposed Class, inclusive of VAT but before interest, is £469 million (Parker Report, §§365-414) **[Annex 2] [CF Bundle/3/198-213]**. This comprises:
- (a) £182 million for the BT Voice Only Customer Sub-class; and
  - (b) £287 million for the BT Split Purchase Customer Sub-class.
140. This estimate is based on the following steps as set out in the Parker Report (§§365-414) **[Annex 2] [CF Bundle/3/198-213]**:
- (a) identifying the Claim Period set out above;
  - (b) an estimate, on a monthly basis, of the number of BT Voice Only and BT Split Purchase Customers of BT SFV Services during the Claim Period, based on data published by Ofcom as part of or with the Provisional Conclusions and/or the Statement;

- (c) an adjustment to those customer numbers to reflect the exclusion of Home Phone Saver services (noting that purchasers of BT Basic services were already excluded in the Ofcom data);
- (d) an estimate of the level of overcharge in each month, based on comparing the BT Standard Line Rental price over time with the competitive benchmark/level.

141. The Proposed Class Representative also claims interest on the above amounts, either in the form of:

- (a) Compound interest, by way of damages:
  - (i) The Members of the Proposed Class are entitled to full compensation for the loss and damage caused to them by BT's breach of statutory duty. All Members of the Proposed Class have been deprived of money to which they were entitled, and therefore lost the opportunity to earn compound interest and/or they paid compound interest on loans, in respect of those amounts.
  - (ii) The nature of the Claim and the numbers of the Members of the Proposed Class involved means that it is not possible or proportionate to particularise the detail of each such loss on an individual basis. Instead, the Proposed Class Representative will adduce evidence (both expert and factual) in respect of such losses on an aggregate average basis, i.e. compound interest will be treated as any other head of loss in the proposed Claim (as per *Sempra Metals Ltd v Commissioners of Inland Revenue* [2008] 1 AC 561, §94). The Proposed Class Representative reserves the right to provide further particulars on compound interest in due course.

142. In the alternative, simple interest pursuant to s.35A of the Senior Courts Act 1981 and/or Rule 105 of the CAT Rules, on such sums and at such a rate as the Tribunal thinks fit.

143. For illustrative purposes only:

- (a) adding compound interest at 8% gives a best estimate of the loss and damage incurred by the Proposed Class, inclusive of VAT, of £608 million (Parker Report §412 [**Annex 2**] [**CF Bundle/3/212**], comprising:



- (i) £248 million for the BT Voice Only Customer Sub-class; and
  - (ii) £360 million for the BT Split Purchase Customer Sub-class; and
- (b) adding simple interest at 8% gives a best estimate of the loss and damage incurred by the Proposed Class, inclusive of VAT, of £589 million (Parker Report §411[**Annex 2**] [**CF Bundle/3/212**]), comprising:
- (i) £238 million for the BT Voice Only Customer Sub-class; and
  - (ii) £351 million for the BT Split Purchase Customer Sub-class.

144. The relief sought is also set out in part VII below.

**Observations on which part of the UK the proceedings are to be treated as taking place under Rule 18 (Rule 75(3)(j))**

145. Pursuant Rules 18 and 75(3)(j), the proceedings should be treated as proceedings in England and Wales:
- (a) the majority of the Members of the Proposed Class are located in England and Wales (see Parker Report, §§432-434);
  - (b) the majority of loss and damage suffered by the Members of the Proposed Class in consequence of the Defendant's conduct is being sustained in England and Wales (see Parker Report, §§432-434); and
  - (c) the Proposed Defendants is are incorporated under the law of England and Wales and has its head office and principal places of business in England and Wales (see §12 above).

**PART V: SUMMARY OF THE BASIS UPON WHICH IT IS CONTENDED THAT THE CRITERIA FOR CERTIFICATION AND APPROVAL IN RULE 79 ARE SATISFIED (RULES 75(3)(E) AND 79)**

146. This part provides a summary of the basis upon which it is contended that the criteria for certification and approval in Rule 79 are satisfied, as required by Rule 75(3)(e). Rule 79

sets out three criteria (together, “**the Eligibility Criteria**”) which must be satisfied in order for claims to be certified as eligible for inclusion in collective proceedings, namely:

- (a) the Claims must be brought on behalf of an identifiable class of persons (Rule 79(1)(a));
- (b) the Claims must raise common issues (Rule 79(1)(b)); and
- (c) the Claims must be suitable to be brought in collective proceedings (Rule 79(1)(c)).

147. Moreover, Rule 79(3) sets out matters that the Tribunal may take into account in addition to the Eligibility Criteria in determining whether the Proposed Collective Proceedings should be certified as opt-in or out-out proceedings.

148. Each criterion is met in the instant application for the reasons addressed in turn below.

**The Claims are brought on behalf of an identifiable class of persons (Rule 79(1)(a))**

149. The Claims are brought on behalf of an objectively identifiable class of persons (see the definition of the Proposed Class above and the Witness Statement of the Proposed Class Representative at §§21 - 24 [**JLP Bundle/1/7-8**]). In accordance with §6.37 of the Guide, it is possible to identify, using the class definition set out above, whether any person falls within the Proposed Class (and Proposed Sub-classes) based on objective and straightforward factual enquiries, as set out below.

150. First, BT should itself be able readily to identify its current and historic customers which make up the Members of the Proposed Class and those falling in the Proposed Sub-classes based on its billing records. In terms of distinguishing BT Voice Only and BT Split Purchase Customers, the Statement [**Annex 3**] [**CF Bundle/4/256-306**] records at §1.10: “providers of standalone telephony services are in fact able to identify which of their customers are voice-only and which are split purchasers” and “BT has told us that it can seek information from Openreach on a monthly basis to confirm which of their lines are voice-only”. Further, BT itself undertook to identify and distinguish between BT Voice Only and BT Split Purchase Customers in the BT Commitments given that the

prospective price reduction applied to certain Voice Only Customers only: §61 above is repeated.<sup>86</sup>

151. Second, Members of the Proposed Class should be able easily to tell or work out if they fall within its scope. First, all Members of the Proposed Class are UK consumers who have bought or are buying landline telephone services from BT; a matter which will be known or, if not, can be readily ascertained by the individual consumer. The customer will then need to consider whether they also bought broadband (but not as part of a bundle) from BT or another CP during the Claim Period. The Proposed Class Representative considers that BT customers will either already know the answers to these questions or can easily ascertain them, if necessary, by checking their billing history or bank statements.

### **The Claims raise common issues (Rule 79(1)(b))**

152. Rule 79(1)(b) stipulates that the Tribunal may certify the Claims as eligible for inclusion in collective proceedings where the Claims “raise common issues”. Pursuant to s. 47B(6) of the Act and Rule 73(2), “common issues” are defined as “the same, similar or related issues of fact or law”.<sup>87</sup> Moreover, §6.37 of the Guide states:

“Although the claims must raise common issues to satisfy the criteria for approval, the final resolution of the claims will often require the assessment of individual issues. The existence of such individual issues is not fatal to an application for a CPO. For example, the determination of liability for an infringement may raise common issues of fact and law which justify a CPO, while causation and the quantification of any damages may not be common to the class.

...

Where only certain issues in the claims constitute common issues, there is no requirement that those must predominate over the remaining individual issues in order for it to be suitable for the part of the claims covering the common issues to be brought in collective proceedings. However, the

<sup>86</sup> See, for example, 2.1 and 2.2 of the BT Commitments [**Annex 3**] [**CF Bundle/4/287-288**]. Moreover, BT’s privacy policy (available at: <https://www.bt.com/privacy-policy/>) states that BT will keep a summary copy of its customers’ bills, contact details and details relating to any dispute for six years.

<sup>87</sup> This mirrors section 47B (6) of the Competition Act 1998.

common issues must be significant such that resolution of those issues will significantly advance the claims of the members of the class.”

153. Ultimately, the Claims manifestly raise common issues because each and every individual claim under s47A, which the Proposed Class Representative seeks to combine in these collective proceedings, concerns: the same service namely, BT SFV Services; supplied by the same undertaking, BT, to UK customers (who are predominantly consumers).
154. Specifically, the Claims raise the following common issues (the “**Common Issues**”):
- (a) Whether BT’s prices for BT SFV services and/or SFV access charged to BT Voice Only Customers and BT Split Purchase Customers are excessive in breach of the Chapter II Prohibition. This in turn requires consideration of:
    - (i) How the markets on which the SFV services are provided to BT customers should be defined, in terms of product, customer group and geographic scope, as pleaded above.
    - (ii) Whether BT occupies a dominant position in the Relevant Markets, as defined, as pleaded above.
    - (iii) What competitive benchmark(s)/level(s) should be selected for the purposes of ascertaining whether BT’s prices for providing BT SFV Services (or BT SFV access) to Members of the Proposed Class were/are excessive.
    - (iv) Whether BT’s prices for providing BT SFV Services (or BT SFV access) were/are excessive when compared to the chosen competitive benchmark(s)/level(s) and what the magnitude of the unlawful overcharge is.
  - (b) The amount of damages which should be awarded to compensate Members of the Proposed Class for the unlawful overcharge paid by them to BT.
  - (c) The rate of interest to be awarded to Members of the Proposed Class.
  - (d) Whether interest should be awarded on a simple basis, or as damages on a compound basis.

155. Each of these issues is capable of being resolved on a common basis, as explained below (and see §25 of the Witness Statement of the Proposed Class Representative [**JLP Bundle/1/8-9**]):

(a) **Market definition:**

- (i) Each claim is in respect of BT SFV Services supplied in the UK excluding the Hull Area. As pleaded above, SFV Services may comprise a single relevant economic market, or be divided into two or more relevant economic markets by reference to material scope (calls / access) and/or customer groups.
- (ii) As is clear from the Parker Report Section 6, whichever approach to market definition is adopted, certain core issues arise relating in particular to the lack of substitutability of SFV Services with: Dual Play services; business services; and mobile services. Further, the approach to geographic scope is common to all relevant markets, however defined.
- (iii) Even if separate economic markets are defined, according to the Parker Report (or otherwise), the Parker Report (Section 6) makes clear that the exercise for defining each respective market raises similar questions and is based on similar principles.

(b) **Dominance:** Whilst dominance is assessed separately on each Relevant Market, the Parker Report makes clear that the *approach* to assessing whether BT is dominant is the same or similar as regards each Relevant Market: see Parker Report, Section 7.

(c) **Competitive benchmark:** As set out in the Parker Report Section 8, the proposed approach to establishing a competitive benchmark is identical for each of the Claims. This approach will lead to individual benchmarks for each of the three line rental products, in each month of the Claim Period, but the methodology is identical in each case.

- (d) **Excessive pricing:** As set out in the Parker Report Section 8, the amount of the monthly overcharge per line which is abusive and therefore unlawful, will be established by a comparison of the prices actually paid for each BT SFV access service in each month of the Claim Period, with the competitive benchmark for that product for that month. This approach is identical across each and every Claim.
- (e) **Damages:** As set out in the Parker Report Section 9, in order to establish the damages payable, it is necessary to apply the overcharge established in the above step to the circumstances of the Proposed Class Members. The Parker Report [Annex 2] has explained the steps that will be taken in order to calculate the amount of aggregate damages to which the Proposed Class Members is entitled at Section 9 [CF Bundle/3/198-212] (see also below). Had the Claims had been pursued separately, the same methodology would apply to the calculation of individual loss, as follows:
- (i) identifying the relevant overcharge for each individual Proposed Class Member's specific subscription (which BT SFV access service they purchased and for which months). While this calculation would be tailored to the individual, it would follow a methodology identical for each and every Proposed Class Member.
  - (ii) establishing an appropriate basis for awarding interest for each Proposed Class Member. This step would follow common legal principles and a common methodology.
  - (iii) for any Proposed Class Members who were businesses customers during the Claim Period, considering potential deductions for any VAT which has been reclaimed and any arguments relating pass on,<sup>88</sup> but their assessment would depend on a common methodology.

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<sup>88</sup> It is for BT in the first place to plead and prove that pass-on of a sufficiently specific nature would have occurred (see *Sainsbury's v MasterCard* [2018] EWCA Civ 1536),

**The Claims are suitable to be brought in collective proceedings (Rule 79(1)(c) and 79(2))**

156. In determining whether the claims are suitable to be brought in collective proceedings, Rule 79(2) states that the Tribunal shall take into account all matters that it thinks fit, including seven expressly identified considerations (together, the “**Suitability Considerations**”).

157. In *Merricks v Mastercard* [2020] UKSC 51, the Supreme Court held that:

- (a) “the certification process is not about, and does not involve, a merits test... There is no requirement at the certification stage for the CAT to assess whether the collective claim form, or the underlying claims, would pass any other merits test, or survive a strike out or summary judgment application”: see also rule 89(4) and (§59);
- (b) “The listed factors [in Rule 79(2)] are not separate suitability hurdles, each of which the applicant for a CPO must surmount. The hurdles (ie preconditions to eligibility under section 47B(5)(b) and (6)) are only that the claims are brought on behalf of an identifiable class, that they raise common issues and that they are suitable to be brought in collective proceedings”: see also rule 79(1) and (§61); and
- (c) the phrase “suitable” in section 47B of the Competition Act and under rule 79(2)(f) means “suitable in a relative sense: ie suitable to be brought in collective proceedings rather than individual proceedings” (§56).

158. Each consideration is met in the instant application for the reasons addressed in turn below (and see §§30 - 32 of the Witness Statement of the Proposed Class Representative [**JLP Bundle/1/10-12**]).

Collective proceedings are an appropriate means for the fair and efficient resolution of the Common Issues (Rule 79(2)(a))

159. The proposed collective proceedings for the Claims are an appropriate means for the fair and efficient resolution of the Common Issues (see also, the Witness Statement of the Proposed Class Representative [**JLP Bundle/1/3-32**] at §25 and the Litigation Plan generally [**JLP Bundle/2/33-160**]).

160. The principal reason why the Proposed Class Representative considers that the Claims can only be brought by way of collective proceedings is that they are individually low in value: the Parker Report estimates individual loss as between £148 and £333 per person (Parker Report, §413 [**Annex 2**] [**CF Bundle/3/213**]). It would therefore be unviable for individual consumers to pursue such claims separately considering their relative complexity and the corresponding costs and time which would be required to bring such a claim (especially bearing in mind the characteristics of the Members of the Proposed Class, as addressed above at §80 and references therein). Indeed, this is borne out by the total absence of such individual claims to date despite the Statement in 2017. The low value of each s47A claim is therefore a complete bar to bringing individual claims and the Infringements by BT will go unredressed unless the Claims are made collectively.

161. Other relevant considerations are that:

- (a) The particular characteristics of the Members of the Proposed Class means that they would in practice be unable or unlikely to bring their own claims: §80 above is repeated. See, also, the Witness Statement of the Proposed Class Representative [**JLP Bundle/1/3-32**] at §§49 – 59 and 89, and the Litigation Plan [**JLP Bundle/2/33-160**] at §§3.8 – 3.19.
- (b) The Common Issues are ones of mixed law, fact and expert evidence, which would be extremely difficult and likely costly exercises for individual Members of the Proposed Class (and the Tribunal) to undertake on an individual basis. It would be inefficient and unfair to expect individual Members of the Proposed Class to each bring a claim, which would in any event have to be case managed together. This would introduce a significant burden on the Tribunal's (or County Court's) time if individual claims were pursued.
- (c) There is unlikely to be any need for Members of the Proposed Class to produce any evidence in order to establish the Infringement or quantum. For example, issues relating to dominance and infringement are highly technical ones requiring expert legal argument and economic evidence, thus avoiding duplication of costs for Members of the Proposed Class.



- (d) The principal issues are Common Issues and each is ideal for determination in collective proceedings: this is “a potential plus factor in the balance” (*Merricks*, §62). The resolution of these Common Issues will significantly advance the claims of the Members of the Proposed Class.

162. For these reasons, collective proceedings are not only an “*appropriate*” means for the fair and efficient resolution of the Common Issues, but the only viable means for the individual Members of the Proposed Class to vindicate their rights and obtain redress for the loss and damage caused by the Infringement.

The benefits of continuing the collective proceedings outweigh any costs (Rule 79(2)(b))

163. In the light of the factors set out above, the benefits of continuing the collective proceedings outweigh any costs for the Members of the Proposed Class, the Proposed Defendants and the Tribunal. Whilst there are inevitably costs associated with bringing the collective proceedings (as set out in the costs budget in the Litigation Plan, section 8 and at Annex 2 to that Plan [**JLP Bundle/2/150**]), these costs are fair and proportionate in light of: (i) the loss suffered as a result of the Infringement which would otherwise go un-redressed; (ii) the size of the Class; and (iii) the aggregate value of the Claims.

164. Moreover, as explained in in Part VI below and §§96 – 115 in the Witness Statement of the Proposed Class Representative [**JLP Bundle/1/27-31**]), to the extent that the Proposed Class Representative is unsuccessful, the costs of this litigation will be covered by the Proposed Class Representative’s Litigation Funding Agreement [**JLP Bundle/22/901-933**].

There are no separate proceedings making claims of the same or similar nature which have already been commenced by members of the class (Rule 79(2)(c))

165. The Proposed Class Representative is not aware of any separate proceedings making claims of the same or a similar nature having been commenced whether by the Members of the Proposed Class or an alternative proposed class representative (whether on an opt-in or opt-out basis).

The size and nature of the Proposed Class (Rule 79(2)(d))

166. Both the size and nature of the Proposed Class mean that the Claims are suitable to be brought by way of (opt-out) collective proceedings. As to the size of the Proposed Class, §§102 - 105 above are repeated and relied upon. As to the nature of the Proposed Class, §80 above is repeated. The Guide at §6.37 states that “it may be where the class is small, but each individual member’s loss is significant, redress would be more effectively obtained by an ordinary individual action”. Neither is the case here. The Class is estimated to be 2.31 million unique individuals, each having suffered relatively small individual amounts (Parker Report, §§418 and 413 [**Annex 2**] [**CF Bundle/3/214**] and [**CF Bundle/3/213**]). Moreover, as explained fully at §80 (and references therein) above, the characteristics of the Members of the Proposed Class (in particular, age, socio-economic group and lack of engagement) means that, by their very nature, their Claims are well-suited to being advanced on their behalf in collective proceedings.

It is possible to determine in respect of any person whether that person is or is not a member of the Proposed Class (Rule 79(2)(e))

167. For the reasons given at §§75 – 79 and 149 – 151 above, it is possible to determine in respect of any person whether that person is or is not a Member of the Proposed Class (and which Proposed Sub-class they fall within).

The Claims are suitable for an aggregate award of damages (Rule 79(2)(f))

168. The Guide at §6.78 states that:

“In awarding damages in collective proceedings, the Tribunal is not required to assess how much each represented person may recover in respect of their claim. Rather the Tribunal may make an “aggregate” award of damages as defined in Rule 73(2). An aggregate award determines the amount the class as a whole is entitled to and is designed to be a practical and proportionate method of assessing damages in collective proceedings. For example, the Tribunal may calculate the damages on a class-wide basis; this could be way of a lump sum award against the defendant, or by using a formula to determine each represented person’s claim without requiring individual proof. This type of award is likely to be more suitable where its calculation can be made without information from the class members, such as where the defendant’s records are sufficient, or where there is a large class with largely identical individual claims.”

169. In relation to aggregate damages, in *Merricks v Mastercard* [2020] UKSC 51, the Supreme Court held that:

- (a) “it is not a condition that the claims are suitable for an award of aggregate damages. That is only one of many relevant factors in the suitability assessment under rule 79(2)” (§§61 and 64(b)) and “[s]uitability of a case for aggregate damages is plainly not a hurdle. It is just one of many factors relevant to suitability of the claims for collective proceedings under rule 79(2)” (§68);
- (b) “in sharp contrast with the principle that justice requires the court to do what it can with the evidence when quantifying damages, which is unaffected by the new structure, the compensatory principle is expressly, and radically, modified. Where aggregate damages are to be awarded, section 47C of the Act removes the ordinary requirement for the separate assessment of each claimant’s loss in the plainest terms.” (§58);
- (c) [i]n the context of suitability for collective proceedings or aggregate damages, it is no answer to say that members of the class can bring individual claims. They would face the same forensic difficulties in establishing merchant pass-on, and insuperable funding obstacles on their own, litigating for small sums for which the cost of recovery would be disproportionately large.” (§73)
- (d) aggregate damages “provides just compensation for the loss suffered by the claimant class as a whole, but the amount need not be computed by reference to an assessment of the amount of damages recoverable by each member of the class individually” (§3);

170. In relation to the distribution of any damages, the Supreme Court added that “generally” any consideration of distribution proposals “at, and for the purposes of the certification stage” is “premature...not least because issues about distribution mainly engage the interests of the represented class *inter se*, rather than those of the proposed defendant... [Any] inappropriate element in the distribution proposals would normally be better dealt with at a later stage” (§80 and see, also, §§58, 64(g) and 77 of that case);

171. The individual claims of the Proposed Class Members are suitable for an award of aggregate damages including for the following reasons:

- (a) There is a large number of individual Claims (estimated by the Parker Report at 2.31 million: see above and Parker Report, §418), each of relatively small value (Parker Report, §413 [**Annex 2**] [**CF Bundle/3/213**]);
- (b) Each of the Claims is very similar, arising out of the pricing of a single service (available in three variants) by a single provider (BT) over a defined period (the Claim Period) and so the Claims are largely, if not entirely, identical (see §§152 – 155 above);
- (c) The Proposed Class Representative anticipates that the total damages are capable of being calculated without information from the Proposed Class Members (see the Litigation Plan at section 6 [**JLP Bundle/2/50-54**]);
- (d) Certain aspects of the calculation of damages, namely the appropriate rates for compound interest calculation, and any pass-on, cannot practicably be undertaken on an individual basis;
- (e) The Parker Report [**Annex 2**] sets out a simple methodology for calculating aggregate damages at §§368 – 387) [**CF Bundle/3/198-203**], namely, in summary, on a monthly basis, based on (i) the duration of the period over which damages arise for BT Voice Only Customers and BT Split Purchase Customers; (ii) the number of BT Voice Only Customers and BT Split Purchase Customers purchasing BT SFV Services; and (iii) a comparison of the price for each BT SFV Service against its competitive benchmark; and
- (f) BT is likely to retain sufficient evidence and data in order to make these calculations and the unredacted, confidential versions of the Ofcom materials are likely to greatly assist (see Annex E to the Parker Report for the disclosure Mr Parker deems appropriate [**Annex 2**] [**CF Bundle/3/247-254**]).

172. In the premises, an award of aggregate damages is a practical and proportionate method of assessing damage on behalf of the Proposed Class.

173. The Proposed Class Representative however notes that it will in theory be possible to calculate the precise unlawful overcharge borne by each individual consumer (subject to any adjustments which may need to be made for business customers) which may be relevant at the distribution stage. See the Litigation Plan (section 8) [**JLP Bundle/2/54-56**] and the Parker Report (§388) [**Annex 2**] [**CF Bundle/3/203-204**], which set out a provisional and initial methodology for achieving an individually-tailored (and compensatory) distribution (Parker Report, §§375 – 384) [**Annex 2**] [**CF Bundle/3/200-202**]. The Proposed Class Representative will keep this matter under review and will, in due course, provide a detailed methodology and process for how individual Proposed Class Members can claim their share of any award of damages and how their claims will be processed.
174. The Proposed Class Representative has made appropriate plans for notifying Proposed Class Members (see the Notice and Administration Plan (sections 7 – 9) [**JLP Bundle/2/89-95**] and Litigation Plan [**JLP Bundle/2/33-160**]).

The availability of alternative dispute resolution (Rule 79(2)(g))

175. Section 49C of the Act on voluntary redress schemes does not apply in the instant case (there being no relevant decision). Nevertheless, as set out above at §15, and in correspondence on his behalf with BT (see the Witness Statement of Rob Murray [**RPM Bundle/1/3-12**]), the Proposed Class Representative is prepared to enter into constructive discussions with BT to explore a timely resolution of the Claims so that Members of the Proposed Class are fairly compensated as soon as possible. In order to fulfil his functions as a Proposed Class Representative and meet the criteria set out in the Rules for the approval of any Collective Settlement, this must, however, be done on an informed and fair basis.

**The collective proceedings should be opt-out proceedings (Rule 79(3))**

176. The Proposed Class Representative seeks permission to bring the Claims by way of opt-out proceedings. The Guidance indicates that the Tribunal can consider whether the Claims should be brought on an opt-in or an opt-out basis, taking into account all matters

it thinks fit, including (i) the strength of the Claims<sup>89</sup> and (ii) whether it is practicable for the proceedings to be brought as opt-in proceedings. Each of these considerations, dealt with in turn below, support the Proposed Class Representative’s application for a CPO on an opt-out basis.

### Background to the introduction of the opt-out regime

177. One of the principal reasons for introducing a wider regime for collective proceedings, and the ability for representatives to bring opt-out proceedings, was the ineffectiveness of the previous scheme of representative proceedings brought by a specified body in securing redress for consumers. The travaux documents for the 2015 Act observed that the previous regime had resulted in only a single case being brought in over 10 years (a claim by The Consumers’ Association (more commonly referred to as Which?) against JJB in respect of replica football shirts) and that the claim only recovered a “small fraction of the consumer losses involved due to the low level of participation” (estimated to be approximately £20 on average per consumer who opted-in).<sup>90</sup> Following this sole outing, Which? had stated that it would not bring another action under the existing procedure, identifying the “greatest barrier” as being “reaching consumers who have suffered detriment”.<sup>91</sup>
178. The primary justification for enabling opt-out actions was therefore to protect the interests of consumers, particularly in cases where “the amount of damages per claimant is very low”, in which case “only an opt-out action is likely to succeed in delivering redress”.<sup>92</sup> As stated by Baroness Neville-Rolfe during a debate on the Bill, “a key feature of the revised regime is the introduction of an opt-out regime, where consumers are automatically part of a court action unless they opt out”.<sup>93</sup>

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<sup>89</sup> §6.39 of the Guide states: “the reference to the “strength of the claims” does not require the Tribunal to conduct a full merits assessment, and the Tribunal does not expect the parties to make detailed submissions as if that were the case. Rather, the Tribunal will form a high level view of the strength of the claims based on the collective proceedings claim form.”

<sup>90</sup> Private Actions in competition law: a consultation on options for reform (April 2012), §§5.4 and 5.6.

<sup>91</sup> Business, Innovation and Skills Committee – Sixth Report (Consumer Rights Bill) (23 December 2013), §272.

<sup>92</sup> Private Actions in competition law: a consultation on options for reform (April 2012), §5.27.

<sup>93</sup> Hansard (HL Grand Committee (7th sitting)) 3 Nov 2014, vol.756, col. GC580, emphasis added.

179. The government was particularly concerned about the possibility of cases where it is not “economically worthwhile to bring a claim” because the sums sought are likely to be small, “e.g. the sum due for an over-priced washing machine or an excessively high coach ticket price”.<sup>94</sup>
180. See also the Tribunal’s observations in *Gibson v Pride Mobility Products* [2017] CAT 9 at §22 (emphasis added):
- “One of the main purposes of the introduction of collective proceedings for competition law claims was to provide an effective mechanism for consumers and smaller enterprises to recover compensation for loss which, although significant for the victim, is individually not of such an amount as could justify bringing such a claim but which, taken together, constitute an appreciable sum.”
181. In that case, the Tribunal went on to hold that, were it not for (unrelated) issues as to the way in which the proposed class representative had defined the alleged infringement, an opt-out proceeding would have been suitable given “the size of the class” (being some 27,000-32,000 people), “the fact that the class members are individual consumers” and the “estimated amount that each represented class member could recover” (being £40 or £195 per consumer, depending on the model purchased) (§§5, 22 and 124).

#### The strength of the Claims (Rule 79(3)(a))

182. The Claims are strong.<sup>95</sup> Whilst the Claims are technically of a standalone nature, they rely heavily on the facts and findings set out in the Provisional Conclusions, the Statement and the effect of the BT Commitments. As pleaded above, Ofcom considered that BT’s prices were so high as to warrant direct price control which was avoided only by virtue of the BT Commitments. Whilst Ofcom’s intervention has resulted in lower prices for Voice Only Customers from 1 April 2018, there was no provision for BT customers to obtain redress for unlawful overcharges already paid to BT (and it is noted that Ofcom still, in 2021, considers these consumers do need protection from detriment). The Proposed Class Representative therefore seeks permission to bring these collective

<sup>94</sup> House of Commons Consumer Rights Bill Research Paper (27 January 2014), p.43.

<sup>95</sup> This requirement is to be understood in light of the dicta in *Merricks*: “claimants with a real prospect of (some) success should [not] be denied a trial by the only procedure available to them in practice”, and “such a merits threshold should not be applied, beyond the strike out or summary judgment levels” (§75).

proceedings in order to obtain such redress on behalf of Members of the Proposed Class in respect of BT’s past and ongoing infringement.

183. Moreover, this Claim Form is also supported by the Parker Report, which constitutes strong evidence of the significant unlawful overcharges to Members of the Proposed Class and of consequent interest foregone.

Opt-in collective proceedings are not practicable (Rule 79(3)(b))

184. Given the individual sums at stake, the complexity and costs involved and the characteristics of the Members of the Proposed Class, it would not be feasible to bring this consumer claim on an opt-in basis. This is an exemplar of precisely the sort of claims for which the opt-out procedure was introduced:

- (a) as explained above, the sums in question are relatively small on an individual Class Member basis; and
- (b) as explained in §80 above, many of the Proposed Class Members are generally unengaged, elderly, in lower socio-economic households and/or (in the case of Voice Only Customers) by definition do not have access to the internet. As the Statement noted, it is exactly this low level of consumer engagement “*that has contributed to cementing BT’s position in the market*”, leading to the abuse in the first place (§4.18). ) For these reasons, it is impracticable to expect these consumers to take the proactive steps required to opt into the proposed collective proceedings.

185. In short, the characteristics described at §80 (and references therein) above which led many of the Members of the Proposed Class to buy a BT SFV Service and suffer detriment from BT’s action (for example, lack of engagement) are precisely the characteristics which render the Class inapt for an opt-in claim. Consequently, the Proposed Class Representative considers, based on his experience, that an opt-in claim is very unlikely to serve as an effective means of seeking redress for at least a large part of the Class, and their interests will be most effectively advanced by bringing an opt-out claim (see §§30 – 32 and 89 of the Witness Statement of the Proposed Class Representative [**JLP Bundle/1/10-12**] and [**JLP Bundle/1/26**]).

186. As the Proposed Class Representative states (at §32 [**JLP Bundle/1/12**]):



“Even with the most intensive efforts to notify claimants, and even if they were offered every conceivable way to register their claim, forcing members of such a disengaged and technically unconfident group to opt-in to a little-known process concerning a claim about technologies they don't really understand would inevitably lead to a huge drop-out rate even among those who were aware they might be due damages”

187. Although it may be possible to identify and contact Proposed Class Members (or at least many of them<sup>96</sup>) by reference to BT's customer records, which the Guide notes in general terms might favour an opt-in, the major obstacle would arise after Members of the Proposed Class have been identified and contacted. Individual Members of the Proposed Class are very unlikely to take the proactive steps required to opt *into* a class action; nor is it likely to be feasible for most Members of the Proposed Class to conduct their own assessment of the merits of the claim, as the Tribunal presumes to be the case for opt-in Members of the Proposed Class (1<sup>st</sup> indent, §6.39 of the Guide).

#### **PART VI: SUMMARY OF THE BASIS ON WHICH THE PROPOSED CLASS REPRESENTATIVE SEEKS TO BE AUTHORISED (RULES 75(3)(D) AND 78)**

188. This part provides a summary of the basis on which the Proposed Class Representative seeks to be authorised to act in that capacity on the basis that such authorisation is just and reasonable in accordance with Rules 75(3)(d) and 78(1)(b). See, also, the Witness Statement of the Proposed Class Representative [**JLP Bundle/1/3-32**].
189. Pursuant to Rule 78(2), in determining whether it is just and reasonable for the Proposed Class Representative to act as the class representative the Tribunal shall consider five matters (together, “**the Just and Reasonable Considerations**”). Each consideration is met in the instant application for the reasons addressed in turn below.<sup>97</sup>

#### **The Proposed Class Representative would fairly and adequately act in the interests of the Class Members (Rule 78(2)(a))**

190. Rule 78(1)(a) provides that the Tribunal may authorise a person to act as the representative in collective proceedings “*whether or not*” the Proposed Class

<sup>96</sup> It is unknown how many ex-customers of BT may have moved address and so be uncontactable.

<sup>97</sup> This Application is also accompanied by a Witness Statement [**JLP Bundle/1/3-32**] in which the Proposed Class Representative addresses the considerations raised by Rule 78, as envisaged by §6.13 of the Guide. Further reference is to be made to that statement.

Representative is a Class Member. As explained in his Witness Statement at §77 and §80, Mr Le Patourel is not a Class Member [**JLP Bundle/1/23**].

191. The Proposed Class Representative would act fairly and adequately in the interests of the Members of the Proposed Class for the following reasons:

- (a) He has considerable experience in the telecoms industry with a specific focus on matters which stop consumers from switching from one service provider to another in order to get a better deal, including the conduct of the CPs themselves. As a result, he has an in-depth understanding of the motivations, behaviours and difficulties faced by telecoms consumers, particularly those who are vulnerable, elderly or less comfortable with technology. He believes that this is directly relevant to the experience of SFV Customers during and prior to the Claim Period, and enables him to understand the Members of the Proposed Class, and act fairly and adequately in their interests (Witness Statement of the Proposed Class Representative, §§62 - 84 [**JLP Bundle/1/19-24**]). He is also well-placed as a result of his previous experience and knowledge to manage the proceedings.
- (b) He wishes to represent the Proposed Class in order to secure justice for them (Witness Statement of the Proposed Class Representative, §§33 – 59 [**JLP Bundle/1/12-18**]).
- (c) He has the benefit of the expertise of the advisory panel, which he has started to assemble to assist. The Proposed Class Representative has identified certain individuals with specific expertise and experience in consumer rights, particularly in the context of vulnerable consumer matters, to assist him. This has led to the appointment of Jane Vass OBE – former Director of Policy and Research at Age UK. See §§82 - 84 of the Witness Statement of the Proposed Class Representative [**JLP Bundle/1/24**]).

192. The Proposed Class Representative has prepared a plan for the Proposed Collective Proceedings (the Litigation Plan [**JLP Bundle/2/33-160**] and Notice and Administration Plan [**JLP Bundle/2/60-149**]) which includes:

- (a) a method for bringing the proceedings on behalf of represented persons and for notifying represented persons of the progress of the proceedings (see section 4). Both the Litigation Plan and the Notice and Administration Plan place emphasis on the fair treatment of older, lower income, and vulnerable consumers, and are designed not only to target Members of the Proposed Class, but also their friends, family and carers who may assist them with their decision-making process, and draw to their attention issues such as this, which may affect them (Witness Statement of the Proposed Class Representative, §§85 – 95 [**JLP Bundle/1/25-27**]), Notice and Administration Plan (see section 3) [**JLP Bundle/2/67-71**]);
- (b) notification proposals at pre-CPO, CPO and distribution stages (see Notice and Administration Plan [**JLP Bundle/2/72-91**] at sections 4 - 7)
- (c) a procedure for governance and consultation which takes into account the size and nature of the class, including the appointment of an advisory panel (Litigation Plan, section 4 [**JLP Bundle/2/44-45**], and the Panel terms of reference [**JLP Bundle/18/842-850**]);
- (d) consideration of matters in relation to disclosure, evidence and witnesses (Litigation Plan, section 6);
- (e) consideration of the litigation timetable (Litigation Plan, section 7);
- (f) a procedure for distributing any award of aggregate damages (Litigation Plan, section 8); and
- (g) a cost budget for the Proposed Collective Proceedings (Litigation Plan, section 8 [**JLP Bundle/2/54**] and Annex 2 to that Plan [**JLP Bundle/2/150**] as well as a litigation timetable [**JLP Bundle/2/151**]).

193. The Proposed Class Representative has instructed Case Pilots (a claims administration company) and Media Zoo (a PR agency) in order to assist with the administering and notifying the Proposed Collective Proceedings. Background to the Litigation Plan and the Notice and Administration Plan (including biographical information for Case Pilots

and Media Zoo) is set out at §§85 - 95] of the Witness Statement of the Proposed Class Representative [**JLP Bundle/1/25-27**]).

**The Proposed Class Representative does not have a material interest that is in conflict with the interests of Class Members (Rule 78(2)(b))**

194. As set out in the Witness Statement of the Proposed Class Representative (§§77, 109 and 112),<sup>98</sup> there is no conflict of interest which prevents him from acting as Class Representative for the Proposed Class [**JLP Bundle/1/27-30**].

**There is not more than one applicant seeking approval (Rule 78(2)(c))**

195. §165 above is repeated and relied upon.

**The Proposed Class Representative will be able to pay the proposed defendant's costs if ordered to do so (Rule 78(2)(d))**

196. As set out in the Witness Statement of the Proposed Class Representative (§§96 - 115) [**JLP Bundle/1/27**], he has made arrangements to ensure that he will be able to pay the Proposed Defendant's costs if ordered to do so (or if he agrees to do so). The Proposed Class Representative's costs budget can be found as Annex 2 to the Litigation Plan [**JLP Bundle/2/150**].

197. The Proposed Class Representative has arranged appropriate funding for the Proposed Collective Proceedings (as explained in the Witness Statement of the Proposed Class Representative, §§96 - 115 [**JLP Bundle/1/3-32**], and Litigation Plan, section 8 [**JLP Bundle/2/54**]).

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<sup>98</sup> See also §§97 and 188 - 193 above.

198. Specifically, as part of the funding arrangements<sup>99</sup> for the Proposed Collective Proceedings, Harbour Fund V, L.P. have agreed to pay any adverse costs award on favour of BT (or any adverse costs that the Proposed Class Representative agrees to pay) BT in relation to the Proposed Collective Proceedings. In line with this obligation, Harbour Fund V, L.P. has purchased adverse costs insurance in relation to the Proposed Collective Proceedings. See further details set out in the Witness Statement of the Proposed Class Representative (§§96 - 15) [**JLP Bundle/1/27-30**].
199. The costs of BT should not exceed those of the Proposed Class Representative<sup>100</sup>: BT will already have substantial knowledge of the factual and legal issues that will arise for determination in the proposed proceedings on account of the 2017 Review, the BT Commitments (and their on-going obligations), and the 2020 Review (including BT’s new proposed voluntary commitments), the adverse costs cover obtained by the Proposed Class Representative is more than adequate.

**No interim injunction is sought (Rule 78(2)(e))**

200. The Proposed Class Representative does not seek an interim injunction so Rule 78(2)(e) is inapplicable.

**PART VII: RELIEF SOUGHT (RULE 75(3)(I))**

201. For the reasons given above, in summary, the relief sought in the Proposed Collective Proceedings is:

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<sup>99</sup> The Proposed Class Representative seeks confidentiality protection over these agreements under Rule 101 of the Rules. The Proposed Class Representative is nonetheless willing to agree to the terms of an appropriate confidentiality order and confidentiality ring with BT, with a view to making an application to the Tribunal, by consent, for the creation of a confidentiality ring pursuant to Rule 53(1) and 53(2)(h) so that BT can understand the funding terms. Moreover, in order to act transparently vis-à-vis Proposed Class Members, the Proposed Class Representative will, in due course, make non-confidential versions of the funding agreements available to the Proposed Class Members upon request via a designated website which has been established to assist with providing notice to the Proposed Class Members.

<sup>100</sup> See *Gibson v Pride Mobility Products* [2017] CAT 9 §143: “it is not evident why the costs of Pride [the respondent] should exceed those of the Applicant, particularly when Pride’s lawyers have already done a great deal of work in gathering documentation and responding to the inquiries made in the course of the OFT’s investigation”

- (a) Damages to be assessed on an aggregate basis pursuant to section 47C(2) of the Act;
- (b) interest, calculated from the date each individual claim arose on either a compound, or alternatively simple, basis as pleaded above;
- (c) the Proposed Class Representative’s costs; and/or
- (d) any such further or other relief as the Tribunal may see fit.

202. As to the estimate of the amount claimed in damages, aggregate damages are currently estimated at £589 million (on the illustrative basis of 8% simple interest, and comprised of £238 million for BT Voice Only Customers and £351 million for BT Split Purchase Customers) on the basis set out in §§139 - 144 above. As explained therein, this is a preliminary estimate only and may require further revision once disclosure of appropriate data has been provided by the Proposed Defendants.

**Ronit Kreisberger Q.C.**  
**Alison Berridge**  
**Jack Williams**  
**MONCKTON CHAMBERS**  
**15 January 2021**  
**Amendments: 4 March 2021**

**Statement of Truth**

I believe that the facts stated in this Claim Form are true.

Full name: JUSTIN LE PATOUREL

Signed: 

.....  
 (Applicant / Proposed Class Representative)

Dated: 15 January 2021

**Statement of Truth**

I believe that the facts stated in this Amended Claim Form are true.

Full name: JUSTIN LE PATOUREL

Signed:

A handwritten signature in black ink, appearing to read 'Justin Le Patourel', written over a horizontal dotted red line.

(Applicant / Proposed Class Representative)

Dated: 4 March 2021

## LIST OF ANNEXES

1. Glossary
2. Expert economic report by David Parker (Parker Economics), dated 13 January 2021
3. Ofcom’s Statement, “Review of the market for standalone landline telephone services”, 26 October 2017 (non-confidential)
4. Ofcom’s Evidence, “Evidence supporting this statement: Review of the market for standalone landline telephone services”, 26 October 2017 (non-confidential)
5. Ofcom’s Provisional Conclusions, “Review of the market for standalone landline telephone services”, 28 February 2017 (non-confidential)
6. Ofcom’s Provisional Conclusions Annexes, 28 February 2017 (non-confidential)
7. Draft Collective Proceedings Order
8. Draft Notice to Members of the Proposed Class of the CPO
9. Ofcom Press Release of 2017 Review
10. Ofcom 2020 Review
11. Ofcom's Statement "Fixed Narrowband Retail Services Markets", 15 September 2009
12. Ofcom's Consultation on end-of-contract and out-of-contract notifications, 31 July 2018 (non-confidential)

The Application for a CPO is also supported by a Witness Statement of Justin Le Patourel (the Proposed Class Representative) [**JLP Bundle/1/3-32**] and Rob Murray (of Mishcon de Reya LLP) [**RPM Bundle/1/3-12**], which are provided in separate bundles (with accompanying exhibits, including the Litigation Plan [**JLP Bundle/2/33-160**] and Notice and Administration Plan [**JLP Bundle/2/60-149**]).





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**ANNEX1**

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## ANNEX 1: GLOSSARY

1. **BT** means BT Group PLC, a public limited company with registration number 04190816 and registered office of 81 Newgate Street, London, EC1A 7AJ
2. **BT Basic** is a landline telephone service sold by BT to customers who are recipients of specific means-tested Government benefits. To qualify for BT Basic a customer has and had to receive one of the following benefits: income support, income-based job seekers allowance, pension credit (guarantee credit), employment and support allowance (income related), and universal credit (and are on zero earnings).
3. **BT Home Phone Saver** is a BT landline telephone service, which provides in one package line rental and a number of additional services such as calls within the same price. The service could not and cannot be taken in a bundle with other services from BT such as broadband. The term “BT Home Phone Saver” covers each and any year’s version in the Claim Period e.g. BT Home Phone Saver 2019 for the year 2019.
4. **BT Line Rental Saver** is a BT product offering customers a discount when paying the entire sum up front. Line Rental Saver is and was not compatible with BT Home Phone Saver.
5. **BT SFV access** means: means an **SFV access** component of a **BT SFV Service** offered by BT.
6. **BT SFV calls** means: means an **SFV calls** component of a **BT SFV Service** offered by BT.
7. **BT SFV Service** means any residential landline calling plan service provided by BT, except for the Excluded Services, which (i) includes landline line rental and (ii) has not been sold as part of a bundle with broadband. For these purposes, a bundle refers to a contract, or two or more closely related, linked or interdependent contracts which, individually or together, include and require the purchase of broadband as well as the landline calling plan service.

8. **BT Split Purchase Customers** means Members of the Proposed Class who, at any time during the applicable Claim Period as defined, have bought at the same time both (i) a BT SFV Service; and (ii) a broadband service, either from BT or any other provider. BT Split Purchase Customers are either **BT Split Supplier Customers** or **BT Split Service Customers**.
9. **BT Split Service Customers** means Members of the Proposed Class who, at the same time, buy: (i) a BT SFV Service; and (ii) a broadband service from BT.
10. **BT Split Supplier Customers** means Members of the Proposed Class who, at the same time, buy: (i) a BT SFV Service; and (ii) a broadband service from a provider other than BT.
11. **BT Voice Only Customers:** Members of the Proposed Class who, at any time during the applicable Claim Period as defined, bought a BT SFV Service but did not, at the same time, buy a broadband service, either from BT or any other provider.
12. The **Claims** means the claims which it is proposed to combine in these collective proceedings i.e. the Members of the Proposed Class' individual claims for, *inter alia*, damages caused by the Proposed Defendant's breaches of statutory duty in infringing the Chapter II Prohibition in the Competition Act 1998.
13. **Claim Period** means:
  - (a) for residential BT Voice Only Customers, between 1 October 2015 and 1 April 2018 inclusive;
  - (b) for business BT Voice Only Customers, between 1 October 2015 and the date of the Tribunal's final determination of the Claims made by the Sub-class of BT Voice Only Customers or their earlier settlement (or settlement of any part thereof); and
  - (c) for BT Split Purchase Customers, between 1 October 2015 and the date of the Tribunal's final determination of the Claims made by the Sub-class of BT Split Purchase Customers or their earlier settlement (or settlement of any part thereof).

14. **Communications Provider (CP)** means a person who (within the meaning of section 32(4) of the Communications Act 2003) provides an electronic communication network or an electronic communications service.
15. **Dual Play** means: a bundle comprising voice and broadband services.
16. **Excluded Services** means BT Basic and BT Home Phone Saver services.
17. **Parker Report** means: the expert economic report by David Parker (Frontier Economics), dated 7 January 2021.
18. **Hull Area** means the area defined as the Licence Area in the licence granted on 30 November 1987 by the Secretary of State under Section 7 of the Telecommunications Act 1984 to Kingston upon Hull City Council and Kingston Communications (Hull) plc.
19. **Provisional Conclusions** means: Ofcom’s Provisional Conclusions, “Review of the market for standalone landline telephone services”, 28 February 2017 (non-confidential)
20. **SFV access** means: the access component of a SFV Service, which is the provision of a fixed telephone line connection (i.e. a landline) with the ability, once the call component is added, to make calls. The access component is a pre-requisite for the purchase of outgoing calls and the vast majority of customers will make some calls. The access component is usually paid for by a periodic fixed line rental charge for access to the network.
21. **SFV access market** means: the market for the provision of **SFV access** i.e. line rental.
22. **SFV calls market** means: the market for the provision of **SFV calls**.
23. **SFV calls** means: the calls component of a **SFV Service**, which allows the consumer to make outgoing call over the telephone line. This is often paid for by a variable payment for calls made under a calling plan.
24. **SFV Customers** means: purchasers of a **SFV Service**.
25. **SFV Service** means: any residential landline calling plan service provided by any communications provider, except for BT Basic, which (i) includes landline line rental

and (ii) has not been sold as part of a bundle with broadband. For these purposes, a bundle refers to a contract, or two or more closely related, linked or interdependent contracts which, individually or together, include and require the purchase of broadband as well as the landline calling plan service.

26. **Split Purchase Customers** means: SFV Customers who bought at the same time both (i) a SFV Service; and (ii) a broadband service, either from the same provider or from different providers.
27. **Statement** means: Ofcom’s “Review of the market for standalone landline telephone services; Statement” (26 October 2017)
28. **Voice Only Customers** means: SFV Customers who bought a SFV Service but did not, at the same time, buy a broadband service, either from the same provider or any other provider.
29. **2009 Review** means: Ofcom’s 2009 review entitled, “Fixed Narrowband Retail Services Markets: Identification of markets and determination of market power”, 15 September 2009.
30. **2017 Review** means: Ofcom’s 2017 review of “the market for standalone landline telephone services”, leading to, and encompassing, the **Provisional Conclusions** and the **Statement**.
31. **2020 Review** means: Ofcom’s consultation entitled “Protecting voice-only landline telephone customers” regarding the BT Commitments (due to expire on 31 March 2021) and BT’s offer of new, further voluntary commitments.

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**ANNEX 2**

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# EXPERT REPORT OF DAVID PARKER

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## Justin Le Patourel (Proposed Class Representative) VS BT Group plc

13 January 2021





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## **1 INTRODUCTION**

1. I am instructed by Mishcon de Reya LLP ("**Mishcon**") on behalf of Justin Le Patourel ("**the Proposed Class Representative**") to provide expert evidence in connection with an application by the Proposed Class Representative to the Competition Appeal Tribunal ("**CAT**") to bring opt-out collective proceedings against BT Group Plc ("**BT**"), as described below.

## 2 QUALIFICATIONS

2. I am David Parker of Frontier Economics Limited (“**Frontier**”), 71 High Holborn, London, WC1V 6DA, a consultancy specialising in microeconomic analysis. I am a Director in Frontier’s Competition practice with over 20 years of experience as a professional economist. I specialise in the use of economics – both economic theory and empirical analysis – in competition law cases.
3. I am regularly employed as an expert in litigation and arbitration cases, including class action cases. I was the economic expert for Pride Mobility Products in *Dorothy Gibson vs Pride Mobility Products Ltd.*, which was the first case for which an application for a Collective Proceedings Order under the Consumer Rights Act 2015 was brought in the UK.
4. I have given evidence in several Courts and Tribunals, including the England and Wales High Court, the Competition Appeal Tribunal, the Northern Ireland High Court, the Ireland High Court, the First Tier Tax Tribunal, the London Court of International Arbitration and the Milan Court of Appeal.
5. My CV is attached as Annex D.

## 3 BACKGROUND AND MY INSTRUCTIONS

### 3.1 Overview of the Claims

6. Mishcon has explained to me that the Proposed Class Representative is applying to the CAT for a collective proceedings order (“**CPO**”) against BT to recover damages for losses suffered by certain customers of BT who have been unlawfully overcharged for landline telephone services in breach of s.18 of the Competition Act 1998 (the “**Chapter II Prohibition**”) (the “**Claims**”). The period in respect of which losses are claimed begins on 1 October 2015.
7. There is no pre-existing finding by a competition authority that the charges imposed by BT, which form the subject matter of the Claims, are in breach of Chapter II. However, Mishcon has drawn my attention to (i) a consultation and provisional conclusions by Ofcom called the “*Review of the market for standalone landline telephone services: Provisional Conclusions*”, dated 28 February 2017 (“**the Provisional Conclusions**”); and (ii) a Statement by Ofcom dated 26 October 2017 (“**the Statement**”) which concluded the consultation.
8. In summary, in the Provisional Conclusions, Ofcom examined the amounts that BT’s customers were paying for residential landline telephone services where those services were bought on a standalone basis by the customer, rather than as a part of a bundle which also included non-voice services such as broadband. These are known as “**Standalone Fixed Voice Services**” (or “**SFV services**”).<sup>1</sup> Ofcom provisionally concluded that SFV services were subject to “*ever higher prices*”<sup>2</sup>, that “*line rental prices have increased significantly*”,<sup>3</sup> and that Ofcom would need to act directly in the retail market by regulating the price of BT’s SFV services.<sup>4</sup>
9. In the Statement, Ofcom found that BT had significant market power, was a price-leader, and was overcharging its customers for the line rental component of BT SFV Services. Rather than imposing price regulation, Ofcom decided to accept voluntary commitments offered by BT and appended to the Statement (“**the BT Commitments**”). The BT Commitments set out that BT would, amongst

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<sup>1</sup> For the avoidance of doubt, where I use “SFV services” in this report I refer to residential services unless I make clear otherwise. I refer to SFV services offered by BT as “**BT SFV Services**” as defined in the Class Definition.

<sup>2</sup> Provisional Conclusions, (para. 1.6)

<sup>3</sup> Provisional Conclusions, (para. 1.9)

<sup>4</sup> Provisional Conclusions, (paras. 1.7 – 1.8)

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other things, introduce a forward-looking line rental price reduction of £7 per month for customers who only bought residential landline telephone services from BT, and did not also buy broadband, either from BT or any other provider (a category known as 'Voice Only Customers').<sup>5</sup> Customers who did buy broadband, from any provider, as well as residential landline telephone services from BT, did not benefit from the BT Commitments.

### 3.2 The Proposed Class

10. I am told that the Proposed Class is defined as:

10.1. "all persons domiciled in the United Kingdom (except in the **Hull Area**) who, during the **Claim Period**, bought a **BT Standalone Fixed Voice Service** except for the **Excluded Services**" (referred to below as "the **Proposed Class**" or "**Proposed Class Members**" as appropriate).

11. I understand that for these purposes:

11.1. **BT Standalone Fixed Voice service** (referred to below as a "**BT SFV Service**") means any residential landline calling plan service provided by BT, except for the Excluded Services, which (i) includes landline line rental and (ii) has not been sold as part of a bundle with broadband. For these purposes, a bundle refers to a contract, or two or more closely related, linked or interdependent contracts which, individually or together, include and require the purchase of broadband as well as the landline calling plan service.

11.2. **Excluded Services** means BT Basic and BT Home Phone Saver.

11.3. **Hull Area** means the area defined as the Licence Area in the licence granted on 30 November 1987 by the Secretary of State under Section 7 of the Telecommunications Act 1984 to Kingston upon Hull City Council and Kingston Communications (Hull) plc.

12. The Proposed Class is split into two Proposed Sub-classes, namely:

12.1. **BT Voice Only Customers:** Members of the Proposed Class who, during the applicable Claim Period as defined below, bought a BT SFV Service but did not, at the same time, buy a broadband service, either from BT or any other provider.

12.2. **BT Split Purchase Customers:** Members of the Proposed Class who, during the applicable Claim Period as defined below, have bought at

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<sup>5</sup> With some exceptions, as explained in Section 3.2 below.

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the same time both (i) a BT SFV Service; and (ii) a broadband service, either from BT or any other provider.

13. The **Claim Period** means:

- 13.1. for residential BT Voice Only Customers, between 1 October 2015 and 1 April 2018 inclusive;
- 13.2. for business BT Voice Only Customers, between 1 October 2015 and the date of the Tribunal's final determination of the Claims made by the Sub-class of BT Voice Only Customers or their earlier settlement (or settlement of any part thereof); and
- 13.3. for BT Split Purchase Customers, between 1 October 2015 and the date of the Tribunal's final determination of the Claims by the Sub-class of BT Split Purchase Customers or their earlier settlement (or settlement of any part thereof).

### 3.3 Instructions

14. Mishcon (on behalf of the Proposed Class Representative) has asked me to give a preliminary view, based on information and data currently available to me, on whether the charges imposed by BT for BT SFV Services to Proposed Class Members during the Claim Period are excessive in breach of the Chapter II prohibition.

15. In particular, I am asked to consider:

- 15.1. How the relevant market(s) should be defined;
- 15.2. Whether BT is dominant in those markets;
- 15.3. Whether BT's charges for BT SFV Services are excessive and therefore abusive within the meaning of the Chapter II prohibition.

16. If my preliminary view is that BT has engaged in an abuse of dominance, Mishcon has also asked me to set out what is, in my view, the appropriate methodology for calculating the aggregate amount of damages for Proposed Class Members to compensate them for losses caused by BT's charges for BT SFV Services and to explain whether there is likely to be sufficient data available to implement that methodology.

17. I am also asked, if my preliminary view is that BT has engaged in an abuse of dominance, to give preliminary estimates of:

- 17.1. The total number of members within the Proposed Class and each Proposed Sub-class;



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- 17.2. The proportion of Proposed Class Members resident in England and Wales; and
- 17.3. The total aggregate loss suffered by Proposed Class Members as a result of the infringement.
18. I have read the Judgment of the Supreme Court in *Merricks vs Mastercard*.
19. I have taken the guidance given by the Supreme Court into account in giving my preliminary view on both the expert methodology and the data which will be required for the purposes of undertaking the assessment of aggregate damages according to that methodology.
20. In the light of the above, I set out my preliminary views on the impact of BT's charges for BT SFV Services on Proposed Class Members. I understand that I will have an opportunity to develop these views further in subsequent reports that may be produced at a later stage of these proceedings if a CPO is granted. It should be noted that the opinions I express in this report are based on the documents and information available to me at the time of writing.
- 20.1. Where I need further information to improve my estimates or to confirm my findings at a later stage if a CPO is granted, I set out the data which I will need as well as the methodology I propose to adopt. I anticipate that the data which I will need is likely in most and perhaps all cases to be held by entities within the BT Group, as follows:
- 20.1.1. BT Retail because it relates either:
- 20.1.1.1. to BT Retail customers, or to market or competitor research undertaken by BT Retail; or
- 20.1.1.2. to document and data submissions made by BT to Ofcom in relation to the Provisional Conclusions and Statement, as well as the confidential versions of those documents; and
- 20.1.2. Openreach, which holds data on the usage of the network.
- 20.2. Given that BT serves the vast majority of this market, at present, I expect that data disclosed by BT will be sufficient to refine my analysis in my evidence for trial.
21. My instructions are set out in full in Annex C.

### 3.4 Materials on which I have relied

22. I have been provided with the following materials:

- 22.1. “The review of the market for standalone landline telephone services, Provisional conclusions”, Consultation, Ofcom, February 2017 (non-confidential version) (“**the Provisional Conclusions**”);
- 22.2. “The review of the market for standalone landline telephone services – Annexes Provisional conclusions”, Consultation, Ofcom, February 2017 (non-confidential version) (“**the Provisional Conclusions, Annexes**”);
- 22.3. “Review of the market for standalone landline telephone services”, Statement, Ofcom, October 2017 (non-confidential version) (“**the Statement**”); and
- 22.4. “Review of the market for standalone landline telephone services, Evidence supporting the Statement”, Ofcom, October 2017 (non-confidential version) (“**Ofcom’s Evidence**”).
- 22.5. “Consultation: Protecting voice-only landline telephone customers”, Ofcom, December 2020 (“**the 2020 Review**”).

23. I have also relied on further documents in the public domain, as follows:

- 23.1. BT’s Consumer Price Guides;
- 23.2. a price series for BT’s Wholesale Line Rental (“**WLR**”) service;
- 23.3. Ofcom’s quarterly telecommunications market data updates;
- 23.4. Ofcom, Fixed Narrowband Retail Services Market Review, Statement, September 2009;
- 23.5. Ofcom, Fixed Narrowband Retail Services Market Review, Consultation, March 2009;
- 23.6. Ofcom Communications Market Reports, published annually;
- 23.7. Ofcom, Promoting competition and investment in fibre networks: Wholesale Fixed Telecoms Market Review 2021-26;
- 23.8. Oftel, Carrier Pre-Selection in the UK Consultative Document July 1998;
- 23.9. Communications Act, 2003;
- 23.10. information from the Office of National Statistics on age distribution;
- 23.11. Directive 2002/21/EC on a common regulatory framework for electronic communications networks and services;

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- 23.12. Commission Notice on the definition of relevant market for the purposes of Community competition law;
  - 23.13. Consolidated version of the Treaty on the Functioning of the European Union – Part three: Union Policies and Internal Actions – Title VII: Common Rules on Competition, Taxation and Approximation of Laws – Chapter 1: Rules on competition - Section 1: Rules applying to undertakings - Article 102 (ex Article 82 TEC);
  - 23.14. Guidance on Commission’s Enforcement Priorities in applying Article 102 TFEU, February 2009;
  - 23.15. The Competition Act 1998, s.18 (the “Chapter II Prohibition”)
  - 23.16. Judgment of 14 February 1978, United Brands and United Brands Continentaal v Commission, 27/76, EU:C:1978:22;
  - 23.17. Case C-62/86 AKZO Chemie BV v Commission ECLI:EU:C:1991:286
  - 23.18. Pfizer and Flynn v CMA [2020] EWCA Civ 339 (“Flynn CoA”); and
  - 23.19. utortiesību un komunicēšanās konsultāciju aģentūra / Latvijas Autoru apvienība vs Konkurences padome, Case 177/16, 14 September 2017 (“Latvian Copyright Society”);
24. Precise references to the specific pieces of evidence drawn from the above are provided where these are referred to within this report, alongside references to particular websites, news articles, etc. where these are the relevant sources.
25. The analysis and evidence presented in this report contain my preliminary views on the basis of the information and evidence that is presently available to me. If more information and/or evidence becomes available, for example through disclosure, I may need to revise my opinions.

### 3.5 Structure of this report

26. This report is structured as follows.
- 26.1. **Section 4** provides a summary of my preliminary conclusions;
  - 26.2. **Section 5** sets out the key factual background;
  - 26.3. **Section 6** provides my assessment of the relevant market definition.
  - 26.4. **Section 7** provides an initial economic assessment of dominance.
  - 26.5. **Section 8** sets out an initial economic assessment of abuse.
  - 26.6. **Section 9** provides my methodology for assessing quantum of damage as well as an interim assessment of damage;
  - 26.7. **Section 10** explores the size of the Proposed Classes and Sub-classes; and

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26.8. **Section 11** sets out a statement of truth.

27. Annexes A and B contain more detail on certain aspects of my methodology. Annex C contains my instructions. Annex D contains my CV. Annex E, for convenience, consolidates the additional data I would need to refine and confirm the conclusions in this report.

## 4 SUMMARY OF PRELIMINARY CONCLUSIONS

28. In this section, I provide an overview of my preliminary conclusions in relation to:

- 28.1. Market definition;
- 28.2. Dominance;
- 28.3. Abuse; and
- 28.4. Class size and damage assessment.

### 4.1 Market definition

29. I use residential SFV access as the focal product for the purposes of market definition as the BT Commitments focus on this product. I note that Ofcom also used this focal point as its starting point for market definition.<sup>6</sup>

30. My analysis is set out in detail in Section 6. I conclude the following:

- 30.1. Access and calls services for residential SFV customers are in the same market.
- 30.2. Separate markets should be defined for SFV services for Voice Only Customers and Split Purchase Customers.
- 30.3. Dual Play products (i.e. products where fixed voice services and broadband are provided together in a bundle) do not fall within either market.
- 30.4. Business-focused SFV services are outside the relevant market.
- 30.5. Mobile services are outside the relevant market.
- 30.6. The geographic scope of the market is UK-wide, but excludes the Hull Area where KCom is the incumbent.

31. In most cases, these market definitions are identical to those employed by Ofcom in the Statement. The exception is in relation to access and calls, where Ofcom has defined separate markets. I consider that it is sensible to define a single market for access and calls given that on the demand side these are usually purchased together, and on the supply side these can be supplied together. However, I have assessed whether my conclusions on dominance and

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<sup>6</sup> Provisional Conclusions, (para. 3.9)

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abuse would change were I to take the same view as Ofcom, and I find that they would not.

### 4.2 Dominance

32. As set out above, I have identified separate relevant markets for:

32.1. SFV services for Voice Only Customers; and

32.2. SFV services for Split Purchase Customers.<sup>7</sup>

33. As set out in Section 7, my preliminary conclusion is that BT is dominant in each of the two markets defined above throughout the Claim Period.<sup>8</sup> This is because:

33.1. BT's market share has remained high, at well over 50% throughout the period in each market. BT's share has been stable, with gradual reductions for Voice Only Customers and virtually no reduction for Split Purchase Customers.

33.2. Rivals to BT face significant barriers to entry and expansion due to customer inertia.

33.3. BT has been able profitably to raise line rental prices to both customer groups substantially over time, despite the main input cost (WLR) falling.

33.4. Individual customers do not have any countervailing buyer power.

34. This assessment is consistent with Ofcom's conclusion that BT had Significant Market Power (SMP) in each of the relevant markets, as SMP is a closely related concept to dominance.<sup>9</sup>

### 4.3 Abuse

35. Since I find that BT had or has a dominant position in the relevant services, I then assess whether BT has abused its dominant position. In this case, the concern relates to whether the prices charged were excessively high. I understand that – at a broad level – the relevant legal test, as set out in the recent Court of Appeal Judgment in *Pfizer and Flynn v CMA* ("**Flynn CoA**")<sup>10</sup>, is

<sup>7</sup> Strictly speaking, I refer to customers on residential tariffs, as distinguished from business customers taking business tariffs. I take account of whether there are business customers taking residential tariffs in my assessment of quantum.

<sup>8</sup> As mentioned earlier, this conclusion holds irrespective of whether I define a market for access alone, or also include calls.

<sup>9</sup> See Footnote 33 for further details.

<sup>10</sup> *Pfizer and Flynn v CMA* [2020] EWCA Civ 339 ("**Flynn CoA**")

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that a price is excessive if it is significantly and persistently above the competitive level.

36. To carry out this assessment, I first explore whether the price for the access component of the SFV service has been or is significantly and persistently above the competitive level (and my preliminary conclusion is that this is the case). I then consider whether the price of the calls component has been or is below the competitive level, in a way that would offset the finding of excess pricing on access.
37. I have explored several benchmarks as proxies for the competitive price level for the access component. My preferred benchmark starts from the price for Standard Line Rental in 2009, as at that time Ofcom did not consider BT to have a position of SMP in the relevant markets. As a result, on a forward looking basis, Ofcom did not expect BT to have market power in those markets (and so did not expect BT to be able to raise prices above the competitive level). I then adjust this starting point for changes in the price of WLR, which is the most important cost input for access, as economic theory predicts that in competitive markets the price level will adjust for changes in variable costs.
38. I consider this approach provides a good proxy for the competitive price level for access throughout the Claim Period.
39. I explore several other potential benchmarks. I consider some to be reasonable potential benchmarks, but are less appropriate than my preferred benchmark. I include these as sensitivities to my analysis. I consider others not to be good benchmarks as they do not represent a good proxy for the competitive price level. I do not consider these further.
40. Comparing actual prices to the competitive benchmark, I find that:
  - 40.1. Access prices for BT's residential SFV products for Voice Only Customers and Split Purchase Customers have been significantly and persistently above the competitive benchmark throughout the Claim Period, by between 51% and 65%.
  - 40.2. There is no evidence that calls prices were below the competitive level so as to offset the excessive prices on the access element, throughout the Claim Period. Indeed, there is some evidence to suggest that BT's SFV calls prices may be/may have been excessive over the Claim Period, but I do not have access to the information which I would need to reach a preliminary view on whether calls were/are also excessively priced.

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40.3. There is no evidence to suggest that BT faced a breakeven constraint, such that it was imperative for BT to increase access prices to offset a decline in profits on calls services or face exit (i.e. the change in prices was not the result of ‘competitive rebalancing’).

41. I therefore conclude that the Proposed Class Members faced excessively high prices for the SFV services to Voice Only Customers and Split Purchase Customers throughout the Claim Period. This is consistent with Ofcom’s concerns that prices for the relevant services had risen substantially over the relevant period, and with the BT Commitments being offered in response to Ofcom’s concern.

### 4.4 Class size and quantum of damage

42. I estimate that the class size is 2.31 million BT customers of SFV services, of which:

42.1. 1.23 million members are in the Voice Only Sub-Class; and

42.2. 1.08 million members are in the Split Purchase Sub-Class.<sup>11,12</sup>

43. The substantial majority of the class is located in England and Wales.

44. My preliminary estimate of aggregate damages for the Class, inclusive of VAT but before interest, is **£469 million**.<sup>13</sup> This comprises the following damage for the Proposed Sub-classes:

44.1. £182 million for the BT Voice Only Sub-class; and

44.2. £287 million for the BT Split Purchase Sub-class.

45. My preliminary estimate of aggregate damages for the Class, inclusive of VAT and *simple* interest at 8%, is **£589 million**. This comprises the following damage for the Proposed Sub-classes:

45.1. £238 million for the BT Voice Only Sub-class; and

45.2. £351 million for the BT Split Purchase Sub-class.

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<sup>11</sup> The class size, as estimated above, may also include members that have passed away either during or since the period of infringement. I understand that claims can be made on their behalf by their estates, so I have not adjusted the class size to reflect deaths. Note that any small discrepancies between the figures are the result of rounding.

<sup>12</sup> All estimates have been rounded.

<sup>13</sup> All estimates have been rounded.



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46. My preliminary estimate of aggregate damages for the Class, inclusive of VAT and *compound* interest at 8%, is **£608 million**. This comprises the following damage for the Proposed Sub-classes:

46.1. £248 million for the BT Voice Only Sub-class; and

46.2. £360 million for the BT Split Purchase Sub-class.

47. Given the estimated number of unique customers in each Proposed Sub-class, this implies the following average quantum of damage per unique customer:

47.1. £148/£193/£201 per unique BT Voice Only Customer, on a no interest/8% simple interest/8% compound interest basis respectively; and

47.2. £265/£324/£333 per unique BT Split Purchase Customer, on a no interest/8% simple interest/8% compound interest basis respectively.

### 4.5 Additional data requirements

48. My preliminary findings are based on the data that is currently available to me through the relevant Ofcom documents and other public data sources. I will be able to update these findings when I have access to the appropriate data, much of which I expect to be held privately by (and therefore available to) BT. In large part, the additional data will allow me to develop more accurate estimates of specific data points that are needed for my analysis, using the methodology that I set out in this Report.

49. I have outlined these data requirements in the relevant parts of this Report.

## 5 KEY FACTUAL BACKGROUND

50. The telecoms sector is characterised by having a former statutory monopolist (BT) and a sector specific regulator (Ofcom).
51. Ofcom conducted market analysis exercises in 2009<sup>14</sup> (Ofcom’s 2009 Review) and 2017 (the Provisional Conclusions) for the purposes of determining whether BT’s provision of certain landline telephone services should be subject to *ex-ante* regulation. These reviews ultimately led to the Statement (in 2017) and to the BT Commitments. Ofcom is currently consulting on BT’s offer to extend the BT Commitments to Voice Only Customers for a further five years (the 2020 Review).
52. In order to understand Ofcom’s 2009 Review and the Provisional Conclusions (and ultimately the BT Commitments, the Statement, the 2020 Review, and the Claims), in this section I first set out a number of concepts and definitions used by Ofcom, which are used across the documents and in this report. I then summarise key aspects of Ofcom’s 2009 Review, the Provisional Conclusions, the BT Commitments, the Statement, and the 2020 Review.

### 5.1 Terms used by Ofcom

#### 5.1.1 The components of SFV Services

53. SFV services comprise the following two components:
- 53.1. The **access component** of SFV services (“**SFV access**”) is the provision of a fixed telephone line connection with the ability, once the call component is added, to make calls. Thus, the access component simply gives the consumer a telephone line. The access component is a prerequisite for the purchase of outgoing calls and the vast majority of customers will make some calls. In order to make calls, the consumer must obtain the “calls” component (see below). The access component is usually paid for by a periodic fixed **line rental charge** for access to the network. Thus, the price for the access component of SFV services is the line rental charge, and I use the two terms interchangeably in this report.
- 53.2. The **calls component** of SFV services (“**SFV calls**”) allows for outgoing call services over that line. This is often paid for by a variable

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<sup>14</sup> Ofcom, Fixed Narrowband Retail Services Markets, Identification of markets and determination of market power, Statement, September 2009, available at [https://www.ofcom.org.uk/data/assets/pdf\\_file/0023/51836/statement.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0023/51836/statement.pdf).

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payment for calls made from the telephone under a calling plan. Incoming calls are typically free of charge.

### 5.1.2 Customer Groups

54. Ofcom uses two categories of customers, depending on the combination of services bought:

54.1. **SFV customers** buy an SFV service and do not buy it as part of a bundle with broadband. If they do buy broadband, they do so separately.<sup>15</sup>

54.2. **Dual Play customers** buy a residential landline service as part of a bundle of services e.g. fixed voice and broadband services.<sup>16</sup> For the purposes of this report, the relevant bundle is fixed voice and fixed broadband services and I use “**Dual Play**” to refer to such a bundle. For clarity, I note that “multi-play” packages is the generic term for packages which bundle SFV services together with other communication services such as broadband and/or pay tv. As such, Dual Play refers to a type of multi-play package.

55. SFV customers are broken down by Ofcom into two further sub-categories, depending on whether or not they (separately) also buy broadband:

55.1. **Voice Only Customers** buy an SFV service, and do not buy broadband from either the same or any other provider;<sup>17</sup> and

55.2. **Split Purchase Customers** buy an SFV service and *separately* (i.e. not as part of a bundle) buy broadband, either from the same provider (Split Service customers) or any other provider (Split Supplier customers).<sup>18</sup>

56. This is set out in Figure 1, which is taken from the Provisional Conclusions:

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<sup>15</sup> Statement, Glossary p.31

<sup>16</sup> Statement, Glossary p.32

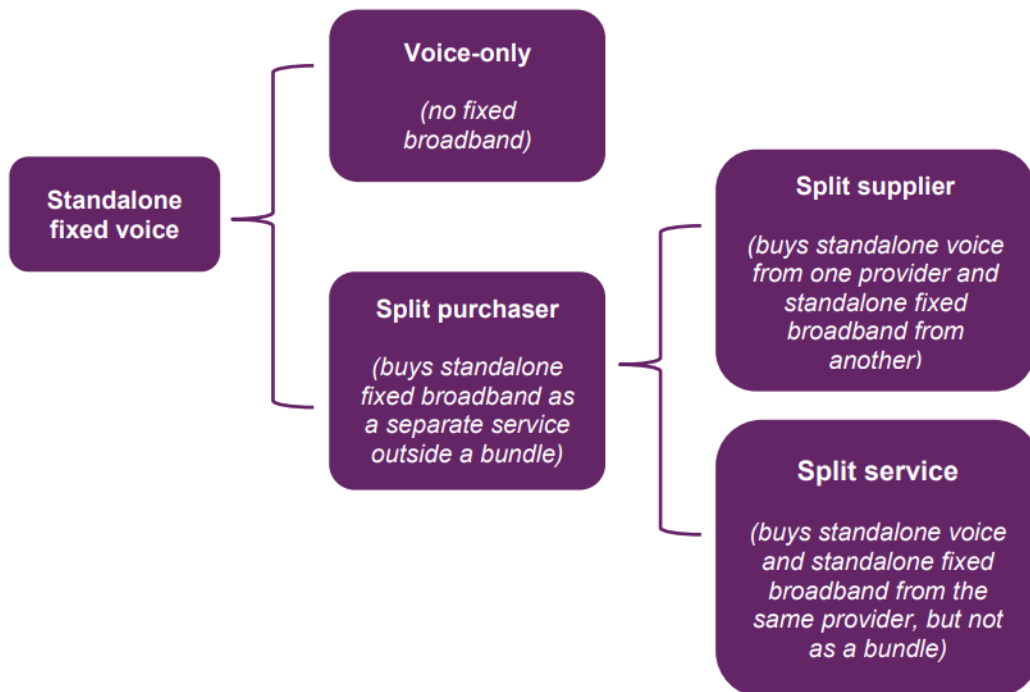
<sup>17</sup> Provisional Conclusions (para. 3.21)

<sup>18</sup> Provisional Conclusions (para. 3.21)

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Figure 1 Customer groups within SFV

Figure 3.1: Customer groups within SFV<sup>30,31</sup>



Source: Provisional Conclusions, replication of Figure 3.1.

### 5.1.3 BT's service offerings

57. While the two components of SFV services (access and calls) can theoretically be bought from separate providers, they are typically (and increasingly) offered and purchased jointly. This means that when purchasing SFV services, the package<sup>19</sup> purchased will often include both line rental and calling plan components.

58. Indeed, Ofcom found that “access services are typically offered to [Standalone Fixed Voice] customers as part of packages which include line rental and a call allowance” and, for BT specifically, that it “does not offer a standalone line-rental product – its standard rental has an inclusive call allowance for calls at weekends at no additional price (“Unlimited Weekend Calls” package)”.<sup>20</sup>

<sup>19</sup> This “package” is not to be confused with a “bundle”, the latter of which is where fixed voice services are combined in one offering with non-voice services such as broadband (as opposed to separate standalone services for voice services and non-voice services).

<sup>20</sup> Provisional Conclusions, (paras. 3.23 – 3.24)

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59. BT offered (and continues to offer) various calling plan component options as part of BT SFV Services during the Claim Period,<sup>21</sup> and these calling plan component options would then include or be combined with an access (line rental) component option to form the BT SFV Service. As a minimum, each line rental was combined with Unlimited Weekend Calls, which was provided free of charge with all line rental component options until October 2019.<sup>22</sup> This gave the consumer access to a phone line (as all access component options necessarily do) and included weekend calls to fixed numbers only.<sup>23</sup> Other calls had to be separately purchased, either on a “pay-as-you-go” basis billed individually for each call, or through specific calling plans which allowed unlimited calls for certain types of calls for a monthly fee.<sup>24</sup>
60. BT offered three relevant access (line rental) component options as part of its SFV services:<sup>25</sup>
- 60.1. Standard Line Rental;
  - 60.2. Line Rental Saver; and
  - 60.3. Line Rental Plus.
61. The three access component options differed principally in the dimensions set out in Figure 2 below.

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<sup>21</sup> For example, see “Calling Packages & Charges”  
[https://www.bt.com/assets/pdf/BT\\_PhoneTariff\\_Residential.pdf](https://www.bt.com/assets/pdf/BT_PhoneTariff_Residential.pdf) .

<sup>22</sup> See p.6,  
[https://web.archive.org/web/20191001003445/https://www.bt.com/assets/pdf/BT\\_PhoneTariff\\_Residential.pdf](https://web.archive.org/web/20191001003445/https://www.bt.com/assets/pdf/BT_PhoneTariff_Residential.pdf)

<sup>23</sup> This includes both fixed UK geographic numbers and 0870 and 0845 numbers but not premium rate services.

<sup>24</sup> I note that the choice of calling plans available to a customer is independent of the variant of Line Rental product they have taken.

<sup>25</sup> By definition (given the meaning of SFV services) these line rental component options are residential services. They do not include line rental component options available exclusively to business customers.

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**Figure 2 Features of BT access component options**

<b>Dimension</b>	<b>Line Rental Saver</b>	<b>Standard Line Rental</b>	<b>Line Rental Plus</b>
<b>Payment methods accepted</b>	Credit or debit cards.	Direct debit only	Any payment method can be used (e.g. cheque, cash, etc.)
<b>Billing periodicity</b>	Requires payment up-front on an annual basis	Payable on monthly/quarterly basis	Payable on monthly/quarterly basis
<b>Bills</b>	Electronic basis only	Paper or electronic bills	Paper or electronic bills

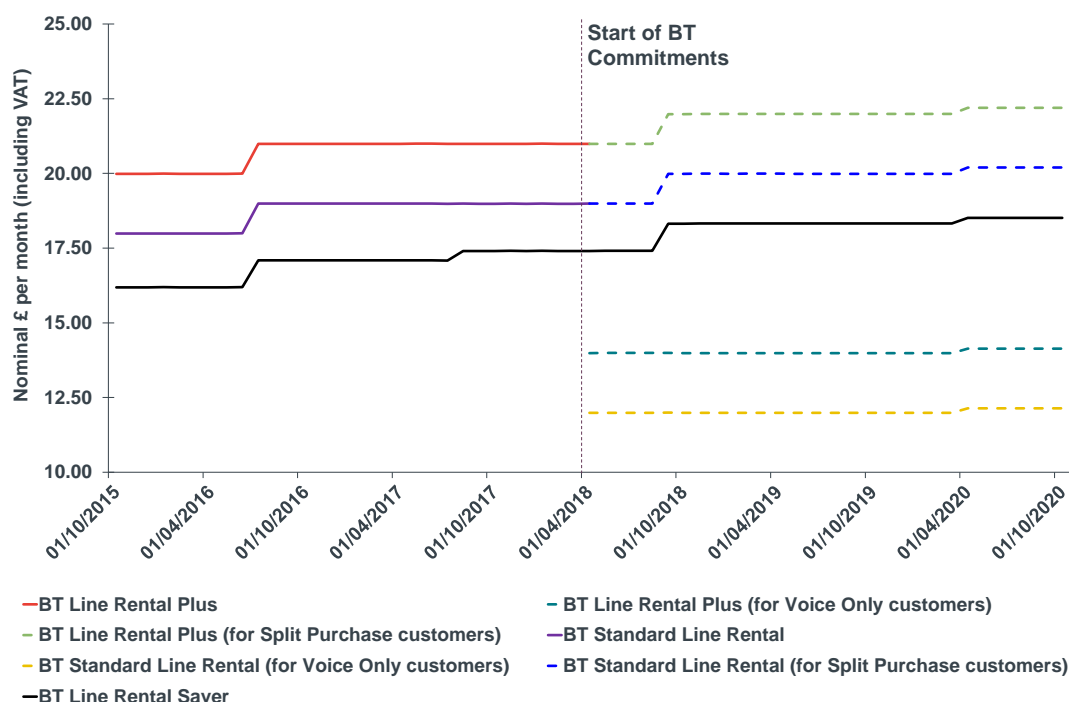
Source: See [https://www.bt.com/assets/pdf/BT\\_PhoneTariff\\_Residential.pdf](https://www.bt.com/assets/pdf/BT_PhoneTariff_Residential.pdf). These differences appear to have been consistent over the relevant period, based on the other publicly available price guides. See <https://www.bt.com/mobile/pdf/bt-consumer-price-guide-15.pdf>

62. The three access component options offered by BT were offered at different prices. Information on the monthly price of Standard Line Rental until July 2019 of the Claim Period is available from Ofcom.<sup>26</sup> For the period thereafter, and for the prices of Line Rental Saver and Line Rental Plus during the Claim Period, I have relied on BT's Consumer Price Guides and other public sources (see Annex A for more details). These data are shown in Figure 3 below.

<sup>26</sup> Pricing Trends for communication services. See <https://data.gov.uk/dataset/f1425d4d-61f4-4596-a06a-8ff2522d8a46/pricing-trends-for-communications-services>

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**Figure 3 Price evolution of the access component (line rental) of BT SFV Services (nominal terms)**



Source: Frontier Economics, Ofcom data and BT Consumer Price Guide data, prices presented in nominal terms, estimated based on a combination of a price index and real prices.

Notes: The y-axis begins at £10 for presentational clarity. 1) Prices are presented in nominal terms and include VAT. 2) It was not possible to calculate a reduced price paid by Line Rental Saver customers after 1 April 2018 as the discount they received would have depended on when they first took Line Rental Saver. In any case, Line Rental Saver is no longer available to Voice Only customers. 3) The vertical dotted line represents the introduction of the BT Commitments on 1 April 2018. 4) Until 1 August 2017 (note: this is an estimate and is explained in Annex A.1), the discounted Line Rental Saver price represented a free month in each year versus the Standard Line Rental price, i.e. 11 months for the price of 12 (a c.8.3% discount). Thereafter, customers instead received a reduction of 10% relative to the Standard Line Rental price.

63. I will refine the above estimate of the prices of the access component options (which I will rely on in my analysis of overcharge and damage) once I have access to better data. The information I will require is as follows:

63.1. Full, monthly, price lists for the following BT offerings offered to **Voice Only customers** – BT Standard Line Rental, BT Line Rental Plus and BT Line Rental Saver. The price lists should cover each month during the Claim Period.

63.2. Full, monthly, price lists for the following BT SFV access products offered to **Split Purchase Customers** – BT Standard Line Rental, BT Line Rental Plus and BT Line Rental Saver. The price lists should cover each month during the Claim Period.

64. BT also offered two other SFV services, BT Home Phone Saver and BT Basic, described below, which were excluded from the BT Commitments and, I am

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instructed, have been excluded from the definition of BT SFV Services in the Class Definition (the Excluded Services):

64.1. **BT Basic** is a social telephony scheme provided by BT to customers who are recipients of specific means-tested Government benefits. It includes Line Rental as well as some free calls and calling credit. To qualify for BT Basic, the customer must receive one of the following benefits: income support, income-based job seekers allowance, pension credit (guarantee credit), employment and support allowance (income related), and universal credit (and on zero earnings).<sup>27</sup> The price of this service (currently £5.16/month inc. VAT)<sup>28</sup> is much lower than that of the line rental products described above and below that of the main cost input, WLR.

64.2. **BT Home Phone Saver** comes with a considerably more extensive calls package included compared to the three line rental offerings set out above.<sup>29</sup> Ofcom states that “*BT uses its Home Phone Saver tariff as a retention tool where it may lose its customers to competitors*”.<sup>30</sup> Home Phone Saver provides a substantial discount compared with purchasing all of the individual features separately, but is more expensive than buying a line rental product with weekend calls.<sup>31</sup>

65. As I set out in Section 6, I consider that BT Basic is in a separate market to Standard Line Rental, Line Rental Saver, and Line Rental Plus, as it is offered to only a restricted group of customers, at a price substantially below cost. By contrast, Home Phone Saver is in the same market(s), as it provides an additional way for customers to purchase SFV services. I therefore include data on Home Phone Saver customers in the assessment of dominance in Section 7. However, I do not assess in this Report whether Home Phone Saver was the subject of excessive pricing or not, as I explain in Section 8.2.3.

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<sup>27</sup> Provisional Conclusions, Annexes, (para. A8.111)

<sup>28</sup> For instance, see [https://www.bt.com/assets/pdf/BT\\_PhoneTariff\\_Residential.pdf](https://www.bt.com/assets/pdf/BT_PhoneTariff_Residential.pdf)

<sup>29</sup> For instance, see [https://www.bt.com/assets/pdf/BT\\_PhoneTariff\\_Residential.pdf](https://www.bt.com/assets/pdf/BT_PhoneTariff_Residential.pdf)

<sup>30</sup> Provisional Conclusions, (para. 8.29)

<sup>31</sup> Provisional Conclusions, para 4.66, apparently relating to 2015 or 2016 data (the reference is to a BT presentation to Ofcom of 17 November 2016). I have checked whether this statement continues to hold true and find that it does. In October 2020 the price of Standard Line Rental was £20.20 per month. The price of Home Phone saver was £1.79 per month higher at £21.99 per month but includes Anytime calls to UK National and Local numbers as well as Anytime calls to 0845 and 0870 numbers. Without Home Phone Saver these would cost £10.11 per month in addition to Standard Line Rental.



## 5.2 Ofcom's 2009 Review

66. In Ofcom's 2009 Review, Ofcom defined one market for "Residential Fixed Narrowband Analogue Access" (broadly, the access component of SFV services), and another market for "Residential Fixed Narrowband Calls" (broadly, the calls component of SFV services), each UK-wide (ex Hull).<sup>32</sup>

67. Ofcom found that BT did not have **SMP**<sup>33</sup> in the above defined access and calls markets<sup>34</sup> for the following main reasons:<sup>35</sup>

67.1. wholesale access remedies had lowered the barriers to entry and expansion for rivals;

67.2. new firms had entered and expanded in the market resulting in a fall in BT's market share;

67.3. consumers had been willing and able to switch provider (as evidenced by the fall in BT's market share); and

67.4. the average increase in the overall phone bill had continued to fall in real terms since retail price regulation had been lifted in 2006.<sup>36</sup>

68. Respondents to Ofcom's 2009 Review identified BT's high market share, and its potential ability to price discriminate against customers with a lower propensity to switch, as reasons to maintain a finding of SMP.<sup>37</sup> However, Ofcom decided that these arguments were not sufficiently compelling at that stage. In relation to price discrimination, Ofcom noted:

*"As part of our Consultation process we considered whether BT would be able to adversely discriminate against its relatively inert customers if the current*

<sup>32</sup> Ofcom also defined markets for retail fixed narrowband calls for business and consumers, for business services and for ISDN2.

<sup>33</sup> Significant Market Power is a concept used in telecoms regulation (only operators with SMP can have ex ante regulation applied to them). It is broadly equivalent to (but does not automatically equate to) the competition law concept of dominance. The difference is that SMP is a forward looking concept. Thus, a firm could have a dominant position today, but may not have SMP if it is expected that the markets will become more competitive and the strong position of that firm will be substantially weakened in the near future. (See the "Commission guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications networks and services", available at [https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52002XC0711\(02\)&from=EN](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52002XC0711(02)&from=EN), at para. 30)

<sup>34</sup> Ofcom's 2009 Review, (para. 1.23)

<sup>35</sup> Ofcom's 2009 Review, Sections 5 and 6 (in particular, paras. 5.16, 6.8)

<sup>36</sup> While retail price regulation had been removed in 2006 (with a commitment by Ofcom to review the removal, which is carried out as part of Ofcom's 2009 Review) (Ofcom's 2009 Review, para. 3.7), some non-price regulation had been maintained (Ofcom's 2009 Review, para. 3.5-3.7)

<sup>37</sup> Ofcom's 2009 Review, Sections 5 and 6.

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*regulations were lifted. Our analysis concluded that BT would find it hard to target these customers specifically because it is difficult to differentiate them from other customer segments.”<sup>38</sup>*

69. On this basis, Ofcom withdrew the existing *ex ante* regulatory controls imposed on BT in the retail markets for landline telephony, which included:<sup>39</sup>

- 69.1. “no undue discrimination” requirements;
- 69.2. price publication and notification requirements; and
- 69.3. cost accounting and accounting separation requirements.<sup>40</sup>

70. Removing those controls gave BT greater commercial freedom to bundle together broadband and voice services (i.e. to offer Dual Play services), and to price discriminate between different customer groups, as Ofcom anticipated:

*“We consider that the main impact of lifting current remedies will be to allow BT to offer bundled packages to consumers and bespoke prices to business.”<sup>41</sup>*

## 5.3 The 2017 Review

### 5.3.1 The Provisional Conclusions

71. Ofcom periodically monitors market developments as part of its General Duty to further the interests of consumers in relevant markets.<sup>42</sup> On 1 December 2016, Ofcom announced a review of the retail market for standalone landline telephone services to ensure that customers receive value for money.<sup>43</sup> This was prompted by a concern that consumers who buy landline services on their own were not being served well by the market.<sup>44</sup> Ofcom stated that its analysis showed that all major landline providers had increased their line rental charges significantly in recent years – by between 28% and 41% in real terms.<sup>45</sup> This was despite

<sup>38</sup> Ofcom's 2009 Review, (para. 5.54)

<sup>39</sup> Ofcom's 2009 Review, September 2009, (para. 1.20)

<sup>40</sup> Ofcom, “Fixed Narrowband Retail Services Markets, Identification and analysis of markets, making of market power determinations and setting of SMP conditions, Final Explanatory Statement and Notification”, November 2003, Section 4.

<sup>41</sup> Fixed Narrowband Retail Services Markets Consultation on the identification of markets and determination of market power: 19 March 2009, (para. 7.11), available at [https://www.ofcom.org.uk/data/assets/pdf\\_file/0026/55295/fnrsm\\_condoc.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0026/55295/fnrsm_condoc.pdf)

<sup>42</sup> Communications Act 2003, Section 3.

<sup>43</sup> <https://www.ofcom.org.uk/about-ofcom/latest/media/media-releases/2016/landline-prices-review-to-protect-elderly-and-vulnerable>

<sup>44</sup> *Ibid.*

<sup>45</sup> *Ibid.*

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providers benefitting from around a 25% fall in the underlying wholesale cost of providing a landline service.<sup>46</sup>

72. In February 2017, Ofcom identified several concerns regarding outcomes for BT SFV customers in the Provisional Conclusions, including:

72.1. While customers purchasing their landline telephone services in a bundle with other non-voice services, such as broadband, (i.e. Dual Play customers) were getting a good deal,<sup>47</sup> customers buying an SFV service were not benefiting from competition in the same way.<sup>48</sup> Ofcom was particularly concerned about price increases faced by these customers.<sup>49</sup>

72.2. SFV customers – often elderly people who had remained with the same landline provider for many decades – were getting increasingly poor value for money.<sup>50</sup>

73. Ofcom noted that rapid increases in BT SFV prices did not appear to relate to changes in either costs or the mechanism of cost recovery.<sup>51</sup> While the charges for key wholesale inputs to these services had fallen by up to 26% in real terms, residential line rental prices had risen by between 25% and 49% since 2010.<sup>52</sup>

74. Ofcom provisionally concluded that there were two relevant product markets:<sup>53</sup>

74.1. The access component for SFV services, which excluded Dual Play, mobile access and business services (the “**SFV access market**”);<sup>54</sup> and

74.2. The calls component for SFV services, which included all call packages and all types of calls, but excluded the provision of calls to customers who purchased ‘multi-play’ packages<sup>55</sup>, mobile access, Voice over Internet Protocol or other communication services (the “**SFV calls market**”).<sup>56</sup>

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<sup>46</sup> *Ibid.*

<sup>47</sup> Provisional Conclusions, (para. 1.2-1.3)

<sup>48</sup> Provisional Conclusions, (para. 1.5)

<sup>49</sup> Provisional Conclusions, (paras. 1.6-1.7)

<sup>50</sup> Provisional Conclusions, (para. 1.7)

<sup>51</sup> Provisional Conclusions, (para. 1.9)

<sup>52</sup> Provisional Conclusions, (para. 1.6)

<sup>53</sup> Provisional Conclusions, (para. 3.107)

<sup>54</sup> Provisional Conclusions, (para. 3.108)

<sup>55</sup> Provisional Conclusions, (para. 3.30)

<sup>56</sup> Provisional Conclusions, (para. 3.108)

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75. At this stage, Ofcom included Voice Only and Split Purchase Customers in the same market based principally on its finding that operators had not so far price discriminated between the two groups, and its expectation that they were unlikely to do so in future.<sup>57</sup>
76. Ofcom provisionally concluded that BT had SMP in each of the SFV access and calls markets.<sup>58</sup>
77. Ofcom estimated that:
- 77.1. there were around 2.9 million SFV lines in the UK (excluding BT Basic), and the overall consumer detriment across for SFV services at the time was of the order of £150 to £340 million per annum, depending on the choice of benchmark price;<sup>59</sup> and
- 77.2. BT SFV Service prices were approximately £8-£10 per line per month above the level of its costs and £5-7 per line per month above a level indicated using competitive benchmarks.<sup>60</sup>
78. Ofcom considered that SFV consumers had been deprived of the benefits which competition would bring in the form of lower prices, more choice, better quality, and greater innovation.<sup>61</sup> Competition in the provision of SFV services should also have led to more reliable connections, better add-on services, and the provision of different call packages and inclusive call allowances.<sup>62</sup>
79. Ofcom therefore proposed a price control in respect of BT SFV Services, as well as certain ancillary services<sup>63</sup>, involving a price cut on the access component of BT SFV Services of between £5-7 per month, with subsequent price increases for line rental and calls being capped at inflation.<sup>64</sup> This was to apply to all BT customers using BT SFV Services<sup>65</sup> whether or not they bought fixed broadband from BT or other providers outside of a bundle.<sup>66</sup>

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<sup>57</sup> Provisional Conclusions, (para. 3.48)

<sup>58</sup> Provisional Conclusions, (paras. 4.80, 5.36)

<sup>59</sup> Provisional Conclusions, (para. 6.5)

<sup>60</sup> Provisional Conclusions, (para. 6.4)

<sup>61</sup> Provisional Conclusions, (para. 6.7)

<sup>62</sup> *Ibid.*

<sup>63</sup> Provisional Conclusions, (para. 1.21); for ancillary services see the Provisional Conclusions: Annexes, p.113, which refers to call waiting, BT Privacy at Home.

<sup>64</sup> Provisional Conclusions, (para. 1.22)

<sup>65</sup> At this stage Line Rental Plus was excluded, but this appears to have been an error and this service was later included within the scope of The BT Commitments.

<sup>66</sup> Provisional Conclusions, (para. 1.23)

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80. Ofcom also proposed requiring BT to trial methods to increase customer engagement for customers who continued to buy SFV services.<sup>67</sup>

### 5.3.2 The BT Commitments

81. On 24 October 2017, BT put forward a proposed set of commitments (the BT Commitments<sup>68</sup>) comprising:

- 81.1. a one-off £7 reduction (inclusive of VAT) to the price of Standard Line Rental and Line Rental Plus on 1<sup>st</sup> April 2018;
- 81.2. an equivalent adjustment to the annual charge for the Line Rental Saver product for the period from 1<sup>st</sup> April 2018;
- 81.3. maintaining these prices until 31<sup>st</sup> March 2019 and then capping any increase at CPI+2.5% until 31<sup>st</sup> March 2021; and
- 81.4. capping the price of a basket of line rental and calls at CPI until 31<sup>st</sup> March 2021.

82. The BT Commitments excluded BT Basic and Home Phone Saver, Split Purchase Customers, and business customers.<sup>69</sup>

83. BT also agreed to work with Ofcom to trial methods for increasing customer engagement for Voice Only Customers.<sup>70</sup>

84. For Split Purchase Customers, BT proposed to “*further stimulate engagement by split-purchase customers by issuing an annual statement detailing the total spend of these customers which should help them to consider what alternatives are available for voice alone and in conjunction with their broadband service.*”<sup>71</sup>

### 5.3.3 The Statement

85. Ofcom made the following findings in its Statement.<sup>72</sup>

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<sup>67</sup> Provisional Conclusions, (para. 6.21)

<sup>68</sup> Statement, (para. 1.16 and Annex A1).

<sup>69</sup> Statement (Annex 1 “A1 BT’s Voluntary Proposal”, para. 2.2). While Home Phone Saver customers were excluded from the price reduction, BT did commit to not increasing the price of this package until 1<sup>st</sup> April 2021.

<sup>70</sup> *Ibid.*, (paras. 4.3-4.4)

<sup>71</sup> Statement, (para. 1.17)

<sup>72</sup> Statement, (paras. 3.30-3.32)

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- 85.1. In a change from its position in the Provisional Conclusions, it defined separate markets for SFV services to Voice Only Customers and Split Purchase Customers.
- 85.2. Ofcom found that: BT was the dominant provider of SFV services to Voice Only Customers, with a significant market share of around 70% in the markets for Voice-only access and calls, which had persisted over time;<sup>73</sup> that competitors faced significant barriers to expansion within the market; and BT had been able to increase prices above the competitive level.<sup>74</sup>
- 85.3. For Split Purchase Customers, Ofcom reiterated its findings from the Provisional Conclusions, that Split Purchase Customers paid materially more for standalone voice and standalone broadband services than they would have paid for functionally equivalent Dual Play services<sup>75</sup>, and that these customers had also been highly profitable for BT.<sup>76</sup> Ofcom also stated that BT had a very high market share with 97% of Split Purchase lines.<sup>77</sup>
86. While Ofcom had concerns for both customer groups, these were more acute for Voice Only Customers.<sup>78</sup> This was because Voice Only Customers generally did not engage with the market and tended to be older and less likely to shop around for a better deal.<sup>79</sup> As a result, Ofcom considered that a significant (forward-looking) price cut was necessary to alleviate the detriment suffered by Voice Only Customers.<sup>80</sup>
87. Ofcom found that Split Purchase Customers had suffered the same price increases as Voice Only Customers in line rental charges in recent years without significant offsetting benefits (since the two customer groups had until then been charged the same prices).<sup>81</sup> However, rather than include them in a price control,<sup>82</sup> Ofcom considered that these customers would benefit from being informed that, in many cases, they were not obtaining good value for money and could find themselves a better deal.<sup>83</sup>

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<sup>73</sup> Statement, (para. 1.12 and 3.54)

<sup>74</sup> Statement, (para. 3.48)

<sup>75</sup> Statement, (para. 3.51)

<sup>76</sup> Statement, (para. 3.52)

<sup>77</sup> Statement, (para. 3.53)

<sup>78</sup> Statement, (para. 1.11)

<sup>79</sup> Statement, (para. 1.11)

<sup>80</sup> Statement, (para. 1.13)

<sup>81</sup> Statement, (para. 1.14)

<sup>82</sup> Statement, (para. 1.15)

<sup>83</sup> Statement, (para. 1.15)

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88. Ofcom therefore accepted the BT Commitments.<sup>84</sup> In particular:
- 88.1. for Voice Only Customers, Ofcom found that the BT Commitments addressed its concerns about the price of BT SFV Services by bringing line rental prices (i.e. the access component) back down to levels last seen in 2009 (in real terms);<sup>85</sup> and
- 88.2. for Split Purchase Customers, Ofcom noted that whilst “*Split-purchase customers pay materially more, for standalone voice and standalone broadband services, than they would pay for functionally equivalent dual-play services*”,<sup>86</sup> “*the focus of BT’s proposal is now solely on encouraging engagement through an annual statement. We consider that this, plus the absence of a price cut, **might** encourage them to engage more actively with the deals available in the market for dual-play and other bundles*”<sup>87</sup> [emphasis added].

### 5.3.4 The 2020 Review

89. The BT Commitments are due to expire on 31 March 2021. BT has made another offer of voluntary commitments to last for a further five years.<sup>88</sup> The commitments apply to all voice-only products and services taken by customers, regardless of the technology used to deliver the service.
90. The main features of these voluntary commitments to Voice Only Customers only, are as follows:<sup>89</sup>
- 90.1. Continue with an inflation-linked control (CPI+0%) on the basket of line rental and call charges for voice-only products (excluding EE, Plusnet and BT’s business products and/or services).
- 90.2. Commit to an annual CPI+0% limit on prices for its Home Phone Saver product and a safeguard cap of CPI+2.5% for its line rental product.
- 90.3. Apply the commitments to any new products or services introduced throughout the 5-year commitment period and that are offered on a voice-only basis.

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<sup>84</sup> Statement, (para. 1.23)

<sup>85</sup> Statement, (para. 1.20)

<sup>86</sup> Statement, (para. 3.51)

<sup>87</sup> Statement, (para. 1.22)

<sup>88</sup> 2020 Review, p1.

<sup>89</sup> 2020 Review, p1.

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90.4. Provide information to Ofcom on its compliance with the commitments on an annual basis.

91. Ofcom has stated that it is minded to accept these further commitments and currently consulting on this decision in the 2020 Review.<sup>90</sup>

92. The 2020 Review sets out that Ofcom considers that the market dynamics are largely unchanged since the Statement and the Provisional Conclusion: *“We continue to believe that price protection for voice-only customers remains necessary to address our previous concerns from our last review in 2017, which included lack of competition in the market and poor value for money for this group of customers.”*<sup>91</sup> However, Ofcom carries out little additional empirical analysis in the 2020 Review, and so in what follows I rely primarily on the evidence in the Provisional Conclusions and the Statement and refer to the 2020 Review where additional evidence is reported there.

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<sup>90</sup> [https://www.ofcom.org.uk/data/assets/pdf\\_file/0016/209050/voice-only-consultation.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0016/209050/voice-only-consultation.pdf)

<sup>91</sup> 2020 Review, p2.



## 6 MARKET DEFINITION

93. Against this background, I consider whether BT's charges for BT SFV Services were excessive and therefore an abuse of a dominant position within the meaning of the Chapter II Prohibition.
94. In order to assess whether a firm occupies a dominant position, it is first necessary to define the relevant (i.e. affected) market or markets – both in terms of product and geography. In this section, I set out my preliminary views on how the affected markets should be defined.<sup>92</sup>
95. I rely primarily on the evidence collected and assessed in the Provisional Conclusions and Statement, as the most relevant and recent data available in the public domain. Ofcom used this evidence to define the relevant markets for the purpose of *ex-ante* regulation under the common regulatory framework.<sup>93</sup> Given that I am asked to consider whether pricing conduct which occurred in the past (and is on-going for some customers) is abusive, my assessment takes account of the evidence assessed by Ofcom, but from an *ex-post* competition perspective.
96. I therefore form my preliminary conclusions on that basis. Where my analysis differs from that of Ofcom I explain why below.

### 6.1 Economic framework for market definition

97. For competition law purposes, a market is defined on two dimensions:
- 97.1. Product dimension – this is to identify the group of products or services that can be considered to act as competitive constraints on each other; and
- 97.2. Geographic dimension – this is to identify the area within which this group of products or services can be found.
98. The standard economic approach for defining the relevant market is the hypothetical monopolist or so-called “SSNIP” test.<sup>94</sup> This involves asking, for a starting set of goods and services (based on the product under consideration), whether a hypothetical monopolist of those goods or services would be able

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<sup>92</sup> I analyse the market definition for the potential Claim Period beginning in October 2015 to present, and except where explicitly identified I consider that the markets in this section apply throughout the period from October 2015 to present.

<sup>93</sup> See Directive 2002/21/EC on a common regulatory framework for electronic communications networks and services.

<sup>94</sup> Commission Notice on the definition of relevant market for the purposes of Community competition law (97/C 372/03), (paras. 15-19)

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profitably to raise prices by a small but substantial amount for a non-transitory period (i.e. a SSNIP), usually of 5% or 10%. Whether a SSNIP would be profitable depends on two key factors:

- 98.1. the extent of demand-side substitution (whether sufficient customers would switch away to make such a price increase unprofitable); and
- 98.2. the extent of supply-side substitution (whether rivals outside the hypothetical market would switch sufficient capacity into the market to make such a price increase unprofitable).<sup>95</sup>

99. The issue of supply side substitution is closely related to the question of barriers to entry and expansion and for analytical ease is sometimes dealt with in the assessment of dominance, rather than at the market definition stage, although here I consider it as part of the market definition assessment.

100. The same framework can be applied to both the product and geographic dimensions of the market.

101. I note that the full set of evidence required to carry out a formal assessment of the SSNIP test is often not available, and instead the SSNIP test provides a useful thought experiment and way for structuring one's thinking. In these circumstances, one needs to draw inferences as to the relevant market definition on the basis of the best available evidence.

### Cellophane fallacy

102. In applying the SSNIP test - in particular in relation to a dominant firm, it may be necessary to have regard to the “**Cellophane fallacy**” which can arise where a dominant firm has used its market power to increase prices above the competitive level. If those inflated prices are then used as the baseline for determining whether a further SSNIP would be profitable, the SSNIP test would tend to lead to markets being defined too widely, as products that are not substitutes when prices are at the competitive level, could nonetheless become substitutes where the prices are above the competitive level.

103. Accordingly, if the Cellophane fallacy is present but not recognised, use of the SSNIP test on actual prices could result in an incorrectly wide market definition. However, if the firm is found to be dominant on a market which has been defined too widely as a result of the Cellophane fallacy, then the finding of dominance remains valid because the dominant firm would have an even higher

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<sup>95</sup> Commission Notice on the definition of relevant market for the purposes of Community competition law (97/C 372/03), (paras. 15-19, 20-23)

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share of a narrower market if the market were correctly defined. Consequently, if a firm is found to be in a dominant position even where the Cellophane fallacy may apply, it follows that the conclusion of dominance would follow even if one were able to control for the Cellophane fallacy.

104. Since I have provisionally found BT to be dominant in the relevant markets through the Claim Period without controlling for the Cellophane fallacy, my conclusions would be unchanged were I to do so. I therefore do not explore this issue further.

## 6.2 Product market definition

105. As set out in Section 5.3.1 above, the Provisional Conclusions and Statement identified that the price for the access component (i.e. the 'line rental' charge) paid by residential SFV customers had increased significantly since the market was fully liberalised in 2009. Ofcom found that this price appeared to be above the competitive level in 2017. I therefore consider this to be the focal product for the purposes of assessing market definition.

106. I have explored whether this is an appropriate market definition for the purposes of the Claim, or whether it should be modified to include other services. In particular, I examine whether:

- 106.1. SFV services aimed at business customers and SFV services aimed at residential customers are in the same market;
- 106.2. the line rental and calls components of SFV services are in the same market;
- 106.3. SFV services to Voice Only Customers and Split Purchase Customers are in the same market;
- 106.4. Dual Play services and SFV services are in the same market; and
- 106.5. mobile phone services and (fixed) SFV services are in the same market.

### 6.2.1 Are SFV services aimed at business customers in the same market as SFV services aimed at residential customers?

107. During the relevant period BT had separate services aimed at residential and business consumers, which differed in price and features. I have therefore considered whether SFV services aimed at business customers are in the same market as SFV services aimed at residential customers. The analysis applies

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equally to Voice Only and Split Purchase Customers and so, for convenience, I consider both together here.

108. Ofcom defined separate markets for services aimed at business and residential users in Ofcom’s 2009 Review<sup>96</sup>, and it excluded business SFV services from its relevant markets in the Provisional Conclusions.<sup>97</sup> I find, consistent with Ofcom’s views, that services aimed at business users should be excluded from the relevant markets.

### Demand side substitution

109. The evidence reported by Ofcom in the 2009 Review<sup>98</sup> outlines the differences in residential and business plans with regards to their tariff structure and key features.

110. As can be seen below, at the time of the 2009 Review, the price of the access component of BT’s business service was higher than that of the standard residential tariff but similar to that of the “International” tariff. Moreover, the prices of calls within the business tariff were lower, and offered additional features such as assurances around quality of service/better fault repair, billing and call waiting. This suggested that the services were meeting different needs.

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<sup>96</sup> Ofcom, Fixed Narrowband Retail Services Market Review, Consultation, March 2009, (para. 4.21)

<sup>97</sup> Ofcom Provisional Conclusions, paras. 3.10-3.12 and 3.54 – 3.56. The Statement did not differ from this view but did not re-examine the issue.

<sup>98</sup> Ofcom Fixed Narrowband Retail Services Market Review, Consultation, March 2009, (paras.4.12-4.21)

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**Figure 4 BT Residential and Business tariffs outlined in Ofcom's 2009 review**

	BT Business Plan	Unlimited Evening and Week-end Plan (Residential)	BT Anytime + International saver (Residential)
Access Price	£16.21* -£17.10**	£10.27	£16.10
Geographic landline (off-peak)	Capped at 10p/hour	Free	Free
Geographic landline (peak)	Capped at 10p/hour	235p/hour	Free
Calls to UK mobiles	25p/hour	734p/hour	440p/hour
International calls	US capped at 10p/hour Europe capped at 20p/hour <sup>21</sup>		US/Europe 2.94p/minute
Other main benefits	BT assurance fault reporting One Bill and Bill analyst Call waiting and call diversion	BT 1471 voicemail	BT 1471 voicemail
Conditions	*2 year min contract, **1 year min. contract, min. spending commitment	1 year min. contract	1 year min. contract



Source: Ofcom Fixed Narrowband Retail Services Market Review, Consultation, 2009, para.4.14

111. The conditions of the two services also differ, with the contract period/spend requirements being more stringent on the business tariff.

112. Similar observations apply when comparing services today. As can be seen in Figure 5 and Figure 6 below for products aimed at business and residential users respectively, business tariffs are structured and presented differently, appear to have a higher monthly charge, have longer contract lengths and also include a number of additional features such as low/guaranteed fault repair times.

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**Figure 5 Prices and product features of BT business SFV services, November 2020 (prices exclude VAT)**

	Value phone line	Standard phone line	Featureline	Value phone line
	From <b>£20.90</b> /month + installation charge	From <b>£27.70</b> /month + installation charge	From <b>£27.20</b> /month + installation charge	From <b>£23.70</b> /month + installation charge
	<a href="#">Buy now</a>	<a href="#">Buy now</a>	<a href="#">Buy now</a>	<a href="#">Buy now</a>
<b>Contract length</b>	24 months	24 months	60 months	12 months  
<b>Unlimited UK call packages</b>	From £13.90 a month	From £13.90 a month	×	×
<b>International call packages</b>	From £10 a month	From £10 a month	×	×
<b>Included call features</b>	2	2	Includes 14 phone features	2
<b>Phone system compatible</b>	×	✓	✓	×
<b>Fault repair time</b>	2 working days	1 working day fault fix	1 working day fault fix	2 working days

Source: <https://business.bt.com/products/voice/phone-lines/>

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**Figure 6 Prices and product features of BT SFV Services (i.e. packages aimed at residential users), November 2020**

### Line Options

If you take a Broadband Package from BT, your package price includes Standard Line Rental. For Package prices click [here](#)

	Features	Monthly Rental	Quarterly Rental	Annual Rental
Standard Line Rental	<ul style="list-style-type: none"> <li>12 month minimum term</li> <li>Payment by Direct Debit only</li> <li>Payable monthly or quarterly</li> <li>Paper* or e-bill</li> </ul>	£20.20	£60.60	
Line Rental Saver	<ul style="list-style-type: none"> <li>Pay in advance by debit/ credit card and get one month free</li> <li>Payable annually</li> <li>E-bill only</li> <li>Available on 1 telephone number per account</li> </ul>			£219.84
Line Rental Plus	<ul style="list-style-type: none"> <li>12 month minimum term</li> <li>Payment by any currently accepted method</li> <li>Payable monthly or quarterly</li> <li>Paper or e-bill</li> <li>Up to 7 handy Calling Features (opt-in)</li> </ul>	£22.20	£66.60	

### UK Calling Plans & Popular Call Prices

Plan Charges	Pay as you go	500 minutes	700 minutes	Unlimited minutes
Monthly Fee (A 30 day rolling contract applies for chargeable calling plans)	£0	£5.00	£7.00	£15.00***

**Call Rates** We calculate our calls including VAT and some calls will be rounded up to the next whole penny. Calls from landlines to mobiles will always do this. For more details click [here](#). These plans have no set up fee.

Calls to UK* National & Local numbers	20p per minute	First 500 minutes are included*	First 700 minutes are included*	Included*
Calls to 0845 & 0870 Numbers**				
Calls to the Channel Islands (landlines)	20p per minute			
Calls to Service Numbers 090, 118 and other 084 & 087 (at all times)	20p per minute + Service Charge			
Calls to UK Mobile numbers (at all times)	20p per minute	First 500 minutes are included*	First 700 minutes are included*	Included*

Source: [https://www.bt.com/assets/pdf/BT\\_PhoneTariff\\_Residential.pdf](https://www.bt.com/assets/pdf/BT_PhoneTariff_Residential.pdf). Note that the BT Commitments will also apply where relevant.

113. These differences suggest that customers may not switch in sufficient numbers between services aimed at business and residential users in response to a SSNIP on SFV services.

114. There also appear to be further limits to the scope for demand-side substitution from residential to business services. I understand, based on Ofcom's findings, that in order to purchase a business access line from BT, a customer may be required to submit a company registration number.<sup>99</sup> If so, this

<sup>99</sup> Provisional Conclusions, (para. 3.55)

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would likely prevent most residential users from acquiring a business line, even if the difference in package features were not present.<sup>100</sup>

115. I therefore consider that there would be insufficient switching to services aimed at business users to defeat a SSNIP on residential SFV services.

### Supply-side substitution

116. A supplier of SFV services aimed at business customers should be able to switch easily to the provision of residential-focussed SFV services. Indeed, most suppliers provide SFV services to both business and residential customers. Thus, supply-side substitutability, to the extent that it exists, has to some degree been exhausted.

117. In any case, given that Ofcom concluded that BT appears to have managed to increase and sustain the price of SFV services well above the level of a SSNIP, as shown in Section 5.3.1 above<sup>101</sup>, any supply-side substitution from business-focussed SFV services appears to have been insufficient to justify their inclusion in the same market.

### Conclusion

118. I consider that SFV services aimed at business customers are in a separate market to SFV services aimed at residential customers.

## 6.2.2 Are fixed calls and access in the same product market?

119. The access and calls components are closely linked since access is a pre-requisite for the purchase of calls, and the majority of customers will make some calls. However, as part of the liberalisation of the market, regulation allowed residential customers buying line rental from BT to make calls using other operators through indirect access (carrier selection or carrier pre-selection), so in principle these could be considered separately.<sup>102</sup>

120. As I explain below, given that calls and access are typically bought together and can be jointly supplied (see Section 5.1.1 above), I consider that it is

<sup>100</sup> Ofcom estimates that 9% of SMEs purchased a residential SFV service (see Provisional Conclusions, para. 3.11). If these users had a company registration number, they may have had the ability to switch to a residential SFV product. However, given the differences in prices and features in the business and residential SFV products highlighted above, I do not consider it likely that sufficient switching would take place to defeat a SSNIP were one to be imposed on residential SFV products.

<sup>101</sup> Para. 73.

<sup>102</sup> See for example Carrier Pre-Selection in the UK Consultative Document July 1998 available at [https://webarchive.nationalarchives.gov.uk/20080715022547/http://www.ofcom.org.uk/static/archive/oftel/publications/1995\\_98/competition/cps798.htm#Introduction](https://webarchive.nationalarchives.gov.uk/20080715022547/http://www.ofcom.org.uk/static/archive/oftel/publications/1995_98/competition/cps798.htm#Introduction)



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appropriate to treat them as being in the same market. I have therefore adopted a different approach to Ofcom on this issue, as I explain below.

### Demand side

121. The Provisional Conclusions record that there had been a marked decline in consumers using different suppliers for calls and access in the decade leading up to the review<sup>103</sup>, and that access and calls were almost invariably bought as a package.<sup>104</sup> However, it placed the access and calls components of SFV services in separate markets on the basis that there was scope for differences in competitive conditions between them.<sup>105</sup> It noted that this was consistent with its approach in the 2009 Review.<sup>106</sup>

122. In theory, there may be differences in the competitive conditions for calls and access components of SFV services.<sup>107</sup> This is because the nature of substitution for calls and access is likely to be different. For instance, customers can consider a variety of substitutes in response to a SSNIP for the calls component:<sup>108</sup>

122.1. they could switch to another access provider who provides competitive prices for calls and access;

122.2. they could make fewer calls outside of ‘inclusive call times’, switch to a service with a less generous inclusive call allowance and/or adjust call times to fall within inclusive call windows; or

122.3. they could switch to making calls on a mobile phone (a large share of customers also own a mobile phone which is also likely to have an inclusive call allowance).

123. A customer has fewer ways of responding to a SSNIP for access components of SFV services,<sup>109</sup> as their only option is to switch access provider or stop using their landline. This may be difficult for customers to do, if (for

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<sup>103</sup> Provisional Conclusions, (para. 3.14)

<sup>104</sup> *Ibid.*

<sup>105</sup> Provisional Conclusions, (para. 3.20)

<sup>106</sup> *Ibid.*

<sup>107</sup> Provisional Conclusions, (para. 3.15)

<sup>108</sup> Assuming a hypothetical monopolist for both access and calls who attempts to increase prices for calls alone above a competitive level.

<sup>109</sup> Again, assuming a hypothetical monopolist for both access and calls who attempts to increase prices for access alone above a competitive level.

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instance) there is a large base of contacts that know the individual's landline number.

124. However, in practice, there has been a decline in customers using different suppliers for calls and access lines over the past decade. The percentage of residential consumers buying access and calls components of SFV services from different suppliers has diminished to negligible levels: see the Provisional Conclusions which find that, although 21% of residential survey respondents reported considering the costs of these components separately,<sup>110</sup> only 1% of survey respondents reported actually using separate suppliers for them.<sup>111</sup>
125. Ofcom also states that access and calls are almost invariably bought in a package.<sup>112</sup> When customers purchase residential line rental, they commonly receive some calls included as part of a package with the purchase. For example, in its most basic home phone plan, Post Office offers free anytime calls to other Post Office home phone numbers.<sup>113</sup> Similarly, Virgin Media offers customers free weekend calls to UK landlines and Virgin Mobile numbers,<sup>114</sup> and BT's Standard Line Rental, Line Rental Saver and Line Rental Plus had all included unlimited weekend calls till October 2019 (as set out above in Section 5.1.3).
126. This indicates that - even though in theory they can be bought separately - competitive conditions are broadly similar for the two services. Consequently, they should be included in the same market, as far as the demand side is concerned.

### Supply side

127. BT's wholesale line rental (WLR) service was introduced to allow retailers other than BT to offer both calls and access components over BT's local access network. Other forms of retail competition including infrastructure based competitors such as Virgin Media and local loop unbundling based operators also provide both calls and access components to customers. From a supply

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<sup>110</sup> Provisional Conclusions, (para. 3.19)

<sup>111</sup> Provisional Conclusions, (para. 3.14) In the Provisional Conclusions Ofcom noted that, although an exact figure pertaining to SFV customers could not be identified in the survey results, it was possible to establish an upper bound for this group of customers. In particular Ofcom noted that, even if one were to assume all the customers who purchase calls and access from separate suppliers are SFV customers, this would translate into only 9% of total SFV customers purchasing calls and access from separate suppliers.

<sup>112</sup> Provisional Conclusions (para. 3.14)

<sup>113</sup> <https://www.postoffice.co.uk/broadband-phone/home-phone>

<sup>114</sup> <https://www.virginmedia.com/shop/phone/phone-only>

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side perspective, this would also suggest that the two services are included in the same market.

### Conclusion

128. I therefore consider that, because the access and calls components are almost always jointly supplied and purchased, they form a single market. In this I differ from Ofcom, which treated them as being in separate markets.

129. But whether I treat access and calls as forming a single market or two separate product markets makes no difference to my preliminary conclusions that (i) BT was/is dominant in the provision of SFV services throughout the Claim Period; and (ii) it excessively priced the access component of those services.<sup>115</sup> Nor does it make any difference to my estimate of the amount of the overcharge, or the methodology.

130. This conclusion is consistent with Ofcom’s view that whether calls and access were in the same or separate markets would “*not fundamentally change*” its competition assessment.<sup>116</sup>

### 6.2.3 Are Voice Only and Split Purchase Customers in the same market?

131. The Statement found that “*there are separate markets for the purchase of each of access and calls by voice-only customers.*”<sup>117</sup> on the basis that providers could identify which of their customers were Voice Only and which were Split Purchase Customers.<sup>118</sup> Although providers had not historically discriminated between them, Ofcom considered that they had the ability to do so if they wished.<sup>119</sup>

132. I agree with Ofcom’s view that SFV services bought by Voice Only and Split Purchase Customers are in separate markets. This is clearly the case from 1 April 2018 when the BT Commitments were implemented and so there was price discrimination. Prior to that, I consider that the key issue is that providers had the ability to price discriminate, as they subsequently demonstrated, and so it is correct from an economic perspective to treat services to each customer group

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<sup>115</sup> As I discuss later, I do not have the data necessary to assess whether calls prices were excessive over the Claim Period. I can revisit this post-certification once the necessary data is available to me.

<sup>116</sup> Statement, (para. 3.32)

<sup>117</sup> Statement (para 3.11). This was a change in position from the Provisional Conclusions, which had earlier considered that the market encompassed both in the same market (3.44 – 3.49).

<sup>118</sup> Statement, (para. 1.10)

<sup>119</sup> Statement, (para. 1.10)

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as being in separate markets for the whole of the Claim Period. However, as I demonstrate below, it makes no difference to my subsequent conclusions on dominance, or to my analysis of abuse, or to my methodology for an assessment of aggregate damages, whether one treats SFV services to these two customer groups as being in the same or separate markets.

**Demand side substitution**

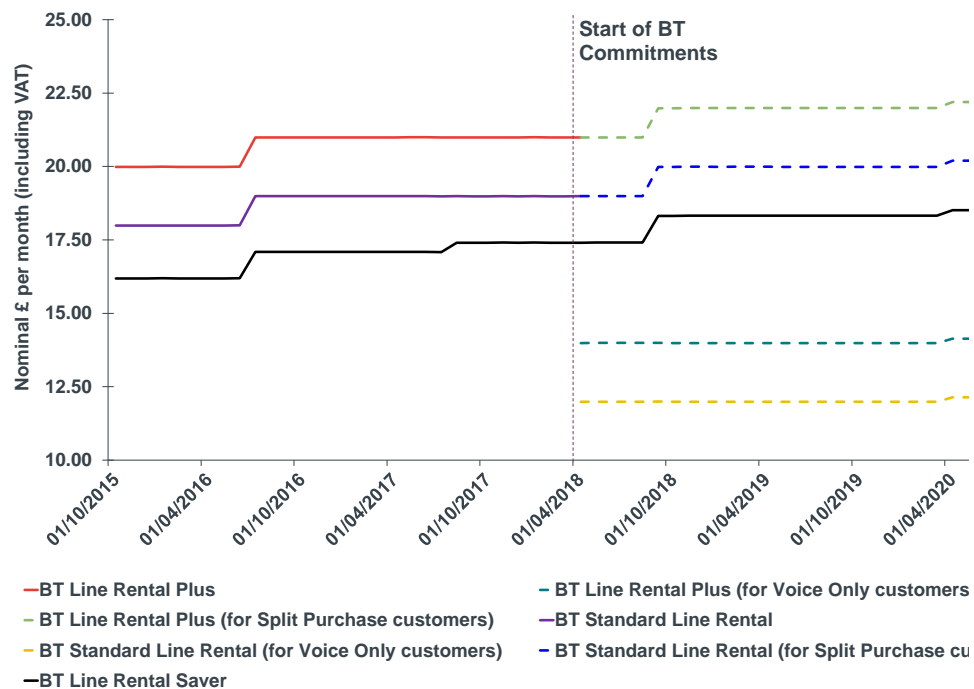
133. Whether the purchaser is a Voice Only or Split Purchase Customer (whether split-service or split-supply), the SFV service which is bought is identical in each case. The two customer groups differ only as to whether they have also bought a fixed broadband service or not, as discussed in paragraph 55. From a ‘functional characteristics’ perspective, therefore, there is no reason to separate the two Proposed Sub-classes into separate markets.
134. I agree with Ofcom that it can be appropriate to treat two customer groups as being in separate markets where providers have the ability to price discriminate between them. Ofcom ultimately found that BT did have the ability to discriminate between Voice Only and Split Purchase Customers, as BT confirmed that it could obtain information from Openreach, on a monthly basis, on which of its lines are Voice-only.<sup>120</sup>
135. BT has acted on this ability since 1 April 2018, when it applied a discount to the access component as per the BT Commitments to (certain) Voice Only Customers only, and not to Split Purchase Customers. As a result, the two customer groups were thereafter charged different prices for the same underlying services. This can be seen in the figure below.

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<sup>120</sup> Statement, (para. 3.18).

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**Figure 7 Price evolution of the access component of BT's Standard Line Rental, Line Rental Plus and Line Rental Saver products**



Source: Frontier Economics and Ofcom data. Detail on how these series were constructed is available in Annex A. 1.

Note: 1) Prices include VAT and are presented in nominal terms. 2) The y-axis begins at £5 for presentational clarity.

136. Using the framework of the hypothetical monopolist test, BT has increased the relative price for Split Purchase Customers well in excess of a SSNIP above the level for Voice Only Customers.<sup>121</sup> While Split Purchase Customers may not have been able or willing to switch to being Voice-only to obtain the discount (because that would mean dropping their broadband service), the fact that separate prices were charged for these two customer groups demonstrates that, at least from 1 April 2018, there are separate markets.

137. Moreover, prior to 1 April 2018, the ability to price discriminate between the two customer groups existed, as discussed above. Had there been a similar SSNIP prior to 1 April 2018 (i.e. the access price for Split Purchase Customers being 5-10% higher than Voice Only Customers), I consider it unlikely that there would have been sufficient switching from Split Purchase Customers to the access component sold to Voice Only Customers to defeat this SSNIP, as they would likely not have been willing or able to give up broadband. I therefore

<sup>121</sup> Over this period the price of the main cost input (wholesale line rental) was decreasing, so the competitive price level is likely to have been decreasing as well, reinforcing the view that BT has been able to introduce a SSNIP above the competitive price level. See Section 7.2.3 for further details.

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consider that from an economic perspective, the most appropriate conclusion is that there are separate markets throughout the Claim Period.

138. However, given that BT did not actually charge different prices to Voice Only and Split Purchase Customers prior to 1 April 2018, it would not make any difference to my analysis of whether the prices were excessive if I treated the two customer groups as being in the same market prior to 1 April 2018.

### Supply side substitution

139. As far as I am aware, the infrastructure and processes used to provide SFV services to Voice Only Customers are the same as those used to provide SFV services to Split Purchase Customers and vice versa given that the SFV services in each case are identical. As such, there is a high degree of potential supply-side substitution. However, this has not been sufficient to prevent the price differential from being sustained, so does not affect the conclusions I have drawn based on demand side substitution.

### Conclusion

140. I consider, in line with Ofcom, that these two customer groups form two separate markets throughout the Claim Period. This conclusion is stronger from 1 April 2018, when actual price discrimination is observed, whereas prior to that point there was the ability to price discriminate, even if it was not taken up.

141. However, as I explain below, even if a single market for these two customer groups was defined prior to 1 April 2018, my conclusions on dominance and abuse would be unchanged.

## 6.2.4 Is Dual Play in the same market as SFV services to Voice Only customers?

142. I have considered whether Dual Play services should be included in the market for SFV services to Voice Only Customers. Dual Play services include the same access and calls components as SFV, with the addition of non-voice components such as broadband, in a single bundle.

143. In the Provisional Conclusions, Ofcom provisionally concluded that Dual Play services were not in the same market as SFV services bought by Voice Only Customers.<sup>122</sup> For Voice Only Customers, Ofcom stated that the prices and

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<sup>122</sup> Provisional Conclusions, (para. 3.38)

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profits for the access component of SFV services were substantially above competitive levels, which would not be sustainable if they were constrained by competition from Dual Play packages.<sup>123</sup>

144. Ofcom confirmed this conclusion in the Statement and updated its analysis of price trends for SFV and Dual Play services, noting that the updated figures continued to support its position.<sup>124</sup>

145. Consistent with Ofcom’s conclusions, I do not consider Dual Play to be in the same market as SFV services to Voice Only Customers.

### Demand side substitution

146. By definition, Voice Only Customers do not use broadband. I therefore consider whether these customers would nonetheless switch to Dual Play - even though it incorporates a service which they do not use (i.e. broadband) - in the event of a SSNIP on SFV.

147. In my view, the evidence indicates that, irrespective of relative prices, Dual Play is not and would not be seen as a substitute for Voice Only Customers by virtue of the fact that it includes broadband. For instance, Ofcom noted from survey evidence that *“68% of voice-only respondents said that the reason they do not take a bundle which includes broadband was that they do not use broadband. A much smaller proportion (8%) said they did not take a bundle including broadband due to the price of fixed broadband.”*<sup>125</sup>

148. This suggests that the driving factor for not taking broadband is not the price, but rather the fact that they do not need broadband.<sup>126</sup> Moreover, as shown in Section 5.3.1 above,<sup>127</sup> BT was able to increase the price for SFV services (including for Voice Only Customers) well above the level of a SSNIP during the Claim Period. Thus, the existence of Dual Play services has not acted as a sufficient constraint to defeat this price rise, and so Dual Play services are not in the same market.

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<sup>123</sup> Provisional Conclusions, (para. 3.38)

<sup>124</sup> Statement, (paras. 3.23-3.29)

<sup>125</sup> Provisional Conclusions, (para. 3.36.2)

<sup>126</sup> I note that even if there was a potential Cellophane Fallacy issue here, this would suggest that the market definition I have found is inappropriately wide, which would support the view that Dual Play services are not in the same market.

<sup>127</sup> Para. 73.

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### Supply side substitution

149. Operators offering Dual Play services can offer an SFV service over the same infrastructure.

150. While the range of suppliers for both services overlaps, fewer providers offer SFV than Dual Play services (e.g. TalkTalk stopped offering SFV to new customers).<sup>128</sup> This is likely because although it may be technically possible for a broadband provider to offer SFV services, there are likely high barriers to entry and expansion in the provision of SFV services, particularly to Voice Only Customers, as they tend to be relatively disengaged. For example, Ofcom's survey evidence suggests low levels of engagement from Voice Only Customers:

150.1. Only 6% of Voice Only Customers were classified as "engaged" compared to 20% of Dual Play;<sup>129</sup>

150.2. Only 3% of Voice Only Customers had switched suppliers in the last 12 months compared to 14% for Dual Play;<sup>130</sup> and

150.3. 74% of Voice Only Customers had been with their supplier for over 10 years compared to 34% for Dual Play.<sup>131</sup>

151. I therefore consider that the barriers to entry are sufficiently high that supply side substitution from Dual Play is not enough to constrain a hypothetical monopolist providing SFV services to Voice Only Customers. I note that this conclusion is confirmed by the fact that the existence of Dual Play has in practice been insufficient to defeat the price rises faced by Voice Only Customers.

### Conclusion

152. I conclude that Dual Play (and by the same logic other multi-play) services should not be considered in the same market as SFV services to Voice Only Customers. This is consistent with Ofcom's conclusion.<sup>132</sup>

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<sup>128</sup> Ofcom's Evidence (para. 1.30)

<sup>129</sup> Ofcom's Evidence, (Figure 1.53)

<sup>130</sup> Ofcom's Evidence, (Figure 1.57)

<sup>131</sup> Ofcom's Evidence, (Figure 1.55)

<sup>132</sup> Provisional Conclusions, (para. 3.38)



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### 6.2.5 Is Dual Play in the same product market as SFV services to Split Purchase Customers?

153. I have also considered whether Dual Play should be in the same market as SFV services to Split Purchase Customers, who also buy broadband.

154. Ofcom stated in the Provisional Conclusions that SFV services bought by Split Purchase Customers are not in the same market as Dual Play services for a number of reasons:<sup>133</sup>

154.1.1. On average, a Split Purchase Customer could save more than 20% per month by switching to an equivalent Dual Play service, and this price difference would not have been sustainable if Dual Play had been a close enough substitute.<sup>134</sup>

154.1.2. Prices for the access component of SFV services had been increasing on an annual basis. Those price increases had not been prevented by the potential for Split Purchase Customers to switch to Dual Play bundles over this period.<sup>135</sup>

154.1.3. BT SFV Services to both Voice Only and Split Purchase Customers had been highly profitable. Ofcom did not consider this to be sustainable if these services had been facing sufficiently strong competitive constraints from Dual Play services as for those to be included in the same market.<sup>136</sup>

155. In its Statement, Ofcom did not consider it necessary to reach a conclusion on market definition<sup>137</sup> but noted that consultation responses had not provided evidence or arguments to lead it to change its view from the provisional conclusion reached in February.<sup>138</sup> Indeed, it stated that “*dual-play bundles do not competitively constrain standalone fixed voice prices to split purchasers*”.<sup>139</sup>

156. My conclusion – again consistent with Ofcom’s assessment – is that Split Purchase and Dual Play services are not in the same market.

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<sup>133</sup> Provisional Conclusions, (paras. 3.39 – 3.43 and 3.108)

<sup>134</sup> Provisional Conclusions, (para. 3.41.1)

<sup>135</sup> Provisional Conclusions, (para. 3.41.2)

<sup>136</sup> Provisional Conclusions, (para. 3.42.2)

<sup>137</sup> Statement (para. 3.49)

<sup>138</sup> Statement, (para. 3.52)

<sup>139</sup> Statement, (para. 3.52).

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### Demand side substitution

157. Unlike Voice Only Customers, Split Purchase Customers:

157.1. buy the same voice and broadband functionality that is available from Dual Play bundles, the only difference being that they purchase them as separate, standalone services, either from the same or different providers.

157.2. are more similar to customers who take Dual Play services than Voice Only Customers, according to survey evidence<sup>140</sup>, in terms of their demographics; and have relatively higher levels of engagement and are more likely to switch service provider than Voice Only Customers (although they are still substantially less likely to switch than Dual Play customers).<sup>141</sup>

158. Given the above, one might expect Split Purchase Customers to be more likely to switch to Dual Play services than Voice Only Customers in response to a SSNIP on the SFV service. However, the evidence set out below demonstrates otherwise: BT was able to introduce a price differential greater than a SSNIP between the price of the SFV service and separate broadband service for Split Purchase Customers, compared to the price of its Dual Play packages. As a result, I do not consider that Dual Play services should be treated as being part of the same market.

159. In the Provisional Conclusions, Ofcom collected price and customer data from various providers<sup>142</sup> and carried out a price comparison on the most frequently purchased packages. Its analysis demonstrated that Dual Play prices were typically significantly lower, particularly on packages that are most frequently bought by customers, than the prices paid by Split Purchase Customers:

<sup>140</sup> Ofcom's Evidence, (Table 1.39, Table 1.40, Figure 1.53, Figure 1.57, paras. 1.1112-1.113) Ofcom survey evidence relates to just split-supplier customers rather than both split-supplier and split-service customers as they had difficulty isolating/identifying split-service customers. However, Ofcom considers that survey evidence from split-supplier customers is reasonable proxy for Split Purchase Customers as it estimates that split-supplier customers account for around 80% of Split Purchase Customers, with the remaining 20% being split-service customers. See Ofcom's Evidence (paras 1.103 to 1.107)

<sup>141</sup> We note that the data on recent switching is likely to understate the willingness of Split Purchase Customers to switch, because those who switched to Dual Play in the previous 12 months will be counted in the Dual Play data.

<sup>142</sup> Ofcom states that it collected data from BT, Plusnet, PostOffice, Sky, and TalkTalk, on the prices paid by their standalone fixed broadband customers and the number of customers on each tariff. They used this information to estimate each provider's average standalone fixed broadband price weighted by the number of customers on each tariff. Ofcom's Evidence, (para 1.88)

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159.1. Ofcom found that over 80% of standalone fixed broadband customers, supplied by BT, Sky, TalkTalk, and Plusnet, received standalone fixed broadband with a speed of 17Mb, and 85% of customers within this group bought Unlimited packages.<sup>143 144</sup>

159.2. When comparing the price difference between the Dual Play package and buying the components separately (as a standalone broadband service with BT standard line rental<sup>145</sup>), Ofcom found that the monthly price differential *i.e.* the saving that an SFV Split Purchase Customer would make from switching to the relevant Dual Play package, in February 2017 was:

159.2.1. £8.77 for a BT customer on a standard Dual Play package;

159.2.2. £16.77 for a BT customer on a promotional Dual Play package;

159.2.3. £3 for a Sky customer on a standard Dual Play package;

159.2.4. £13 for a Sky customer on a promotional Dual Play package; and

159.2.5. £16.35 for a TalkTalk customer on a Dual Play package.

160. These data are shown in Figure 8.

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<sup>143</sup> Ofcom's Evidence, (para 1.89, Footnote 93)

<sup>144</sup> The comparison focuses on 17Mb packages, and for other package types there are examples where the savings from switching to Dual Play are smaller. However, as Ofcom stated, 80% of customers were on 17 MB/Unlimited packages, so I consider focussing on these packages appropriate and representative. Ofcom analysis also excludes smaller providers such as SSE (SSE has a market share of less than 5% - see The Provisional Conclusions, (Table 1.10)) or those that have exited the market such as Tesco. I do not consider that this affects my assessment - the fact that BT was able to maintain this price difference for the substantial majority of customers shows that the SFV services for Split Purchase Customers are not in the same market as Dual Play.

<sup>145</sup> The BT Line Rental product cost £18.99.

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**Figure 8 Comparing prices paid by Split Purchasers with Dual Play, February 2017**

**Figure A8.43: Standalone fixed broadband and dual-play prices (£/month): BT, Sky and TalkTalk**

	(1) Standalone fixed broadband weighted average price (31/10/2016)	(2) Standalone fixed broadband plus line rental (£18.99)	(3) Dual-play: promotional price (per month)	(4) Dual-play: standard price (per month)	(5) = (2)–(3) Price difference for split purchaser compared to promotional dual-play price	(6) = (2)–(4) Price difference for split purchaser compared to standard dual-play price
<b>BT</b>						
17Mb/12Gb	24.80	43.79	24.99*	33.99	18.80	9.80
17Mb/25Gb <sup>180</sup>	24.00	42.99	24.99*	33.99	18.00	9.00
17Mb/Unlimited	30.77	49.76	32.99*	40.99	16.77	8.77
52Mb/Unlimited	28.58	47.57	39.99*	47.49	7.58	0.08
76Mb/Unlimited	36.26	55.25	49.99*	53.99	5.26	1.26
<b>Sky</b>						
17Mb/Unlimited <sup>181</sup>	13.00	31.99	18.99*	28.99	13.00	3.00
38Mb/Unlimited <sup>182</sup>	20.00	38.99		38.99		0.00
<b>TalkTalk</b>						
17Mb/Unlimited <sup>183</sup>	20.31	39.30	22.95*	22.95*	16.35	16.35
<b>Weighted average<sup>184</sup></b>	<b>20.16</b>	<b>39.15</b>	<b>24.58</b>	<b>31.14</b>	<b>14.57</b>	<b>8.01</b>

Source: s. 135 response data; dual-play promotional and standard prices from operator websites (accessed 1 February 2017).

Notes: asterisk indicates the promotional price applies to a 12-month period. This table excludes a small number of Phone Co-op standalone fixed broadband customers (<1000).

Source: A8.43, Provisional Conclusions, Annexes.

161. Ofcom summarised these results as follows: “Our analysis... shows that on average a split purchaser paying a combined price for standalone voice from BT and standalone broadband from BT, Sky or TalkTalk could save £8 per month (more than 20%) by switching to an equivalent dual-play service from their broadband provider at standard prices, and just over £14.50 per month (more than 35%) at promotional dual-play prices.”<sup>146</sup>

162. The price differences remained of a similar order of magnitude when Ofcom carried out the analysis again in August 2017, as shown in Figure 9.

<sup>146</sup> Provisional Conclusions, (para. 3.41.1)

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**Figure 9 Comparing prices paid by Split Purchasers with Dual Play, August 2017**

Table 1.32: Standalone fixed broadband prices, and promotional and standard dual-play prices

		(1)	(2)	(3)	(4)	(5) = (3)–(2)	(6) = (4)–(2)
	Download speed / Data usage cap	Standalone fixed broadband weighted average price (Q1 2017)	Standalone fixed broadband + Monthly line rental (£18.99)	Cheapest promotional dual-play price	Cheapest standard dual-play price	Difference to promotional dual-play price	Difference to standard dual-play price
BT	17Mb / 12Gb	32.89	51.88	24.99	34.99	-26.89	-16.89
BT	17Mb / 25Gb	25.44	44.43	24.99	34.99	-19.44	-9.44
BT	17Mb / Unlimited	33.79	52.78	24.99	34.99	-27.79	-17.79
Sky	17Mb / Unlimited	15.16	34.15	20.00	28.99	-14.15	-5.16
TalkTalk	17Mb / Unlimited	22.71	41.70	19.95	27.00	-21.75	-14.70
<b>Weighted average</b>	<b>Various</b>	<b>23.73</b>	<b>42.72</b>	<b>24.89</b>	<b>34.85</b>	<b>-17.83</b>	<b>-7.87</b>

Source: S135 response data; dual-play promotional and standard prices from operator websites (accessed 21 August 2017)

Notes: For BT 17Mb / 25Gb we use the promotional and standard price of a 17Mb/12Gb service as a proxy for 17Mb/25Gb, since this usage limit is no longer available.

Source: A8.43, Provisional Conclusions, Annexes.

163. In relation to these results, Ofcom stated that, “Compared to average dual-play prices which split purchasers would pay if they bundled these services, they are paying an average of £17.83 more per month compared to promotional dual-play prices or £7.87 more per month compared to standard dual-play prices.”<sup>147</sup>

164. These price differences are well above the level of a SSNIP on the SFV price (a 5% SSNIP on the average SFV Split Purchase price is £2.14). If Dual Play had operated as a sufficient competitive constraint on prices paid by Split Purchase Customers so as to justify including Dual Play in the same market as SFV services to Split Purchase Customers, the observed price differences would not have been sustainable.<sup>148</sup> Instead, it seems that BT was able to profitably sustain this price difference. Ofcom states that “our analysis indicates that SFV services for both voice only and split-purchase customers have been highly profitable. We would not expect providers of SFV services to split purchasers to

<sup>147</sup> Ofcom’s Evidence, (para. 1.91)

<sup>148</sup> To the extent that the Cellophane fallacy applies here this would lead to our overestimating the extent to which Dual Play services are in the same market. Given that I conclude that they are not in the same market, the potential existence of the Cellophane fallacy does not distort my conclusions.

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*be able to sustain such a high level of profitability if they were facing competitive constraints from dual-play services”.*<sup>149</sup>

165. In relation to the level of switching, Ofcom noted “*While the number of SFV customers has been falling over time, and this is likely to include a proportion of former split-purchase customers switching to dual-play, **there remains a sizeable group of split purchasers (about 1.2 million) who have not responded to these price increases by switching to dual-play.** Reported annual switching rates are equally low for both voice-only and split supplier customers (3%) compared to dual play (12%) (see Annex 8, Figure A8.55). In view of this, on a forward-looking basis we consider that the remaining split purchasers are unlikely to switch to dual-play in response to a SSNIP in sufficient numbers to constrain SFV prices to competitive levels.*”<sup>150</sup> [emphasis added].

166. So, while there was a degree of switching, this was insufficient to lead to the removal of the price differential.

167. Thus, the evidence shows that BT was able to sustain a SSNIP on SFV services to Split Purchase Customers. I therefore consider, in line with Ofcom, that from a demand side perspective Dual Play services are not in the same market as SFV services to Split Purchase Customers.

### Supply side substitution

168. As for Voice Only Customers, suppliers are likely to have the ability to switch between the supply of SFV services (for Split Purchase Customers) and Dual Play services easily.

169. However, most providers of Dual Play services either do or have previously provided SFV services<sup>151</sup>, and such substitution has been insufficient to constrain BT’s pricing in relation to SFV services. Accordingly, supply side substitution does not indicate that the market should be widened to include Dual Play services.

<sup>149</sup> Provisional Conclusions, (para. 3.42.2). As most of the profitability data has been redacted, I am unable to carry out further analysis on this issue at this stage.

<sup>150</sup> Provisional Conclusions, (para. 3.41.3)

<sup>151</sup> For instance, see <https://www.postoffice.co.uk/broadband-phone/home-phone> or <https://www.virginmedia.com/shop/phone/phone-only>

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### Conclusion

170. As a result, and consistent with Ofcom’s conclusions, I do not consider that Dual Play services are in the same market as SFV services for Split Purchase Customers.

### 6.2.6 Are mobile services in the same market as SFV services?

171. Finally, I consider whether mobile services operate as a sufficient substitute for SFV services, to justify including them in the same market as SFV services. As my analysis applies equally to Voice Only and Split Purchase Customers, I consider both together for convenience.

172. In the Provisional Conclusions,<sup>152</sup> Ofcom excluded mobile services from its relevant markets (i.e. both calls and access components of SFV services) because Ofcom saw fixed and mobile access as largely serving different needs, with consumers having a low willingness to abandon their landline which limited any overall indirect constraint from mobile services.<sup>153</sup>

173. Consistent with Ofcom’s conclusions, I do not consider mobile services to be a part of the same market as SFV services for either Voice Only or Split Purchase Customers.

### Demand-side substitution

174. The relevant question here is whether a customer of SFV services would switch to the use of mobile services in the event of a SSNIP on SFV services. In the case of access, this would involve giving up their landline service and switching exclusively to the use of mobile; while for calls this would mean switching a sufficient proportion of call volumes to mobile calls.

175. Had mobile services been acting as a significant constraint on SFV services, a SSNIP on SFV services prices would not have been sustainable. However, as shown in Section 5.3.1 above, the price of the access component of SFV services (for both Voice Only and Split Purchase Customers) has increased over the relevant period well above the level of a SSNIP. And, as I show subsequently in Section 8.4, BT’s call prices have also increased.<sup>154</sup> This suggests that any constraint from mobile has already been felt and incorporated into pricing

<sup>152</sup> Provisional Conclusions, (para. 3.108)

<sup>153</sup> Provisional Conclusions, (para. 3.61)

<sup>154</sup> This finding applies to BT call prices across the board, as I do not have evidence at this stage on call prices for customers of SFV services only.

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decisions, and prices to Voice Only and Split Purchase Customers have increased – in an apparently sustainable manner – despite the existence of this potential constraint.

176. I consider therefore that mobile services do not appear to be a sufficient demand-side substitute for SFV services so as to include them in the same market.

### Supply-side substitution

177. Mobile services and SFV services are provided over entirely different networks and infrastructure. It is unlikely that a mobile provider would enter the SFV market in a timely manner to defeat a SSNIP. It may not even find it profitable to do so because it is likely to be difficult to win customers – as set out above, SFV customers tend to be disengaged and are therefore less likely to react to new offers.

178. Finally, I note a number of providers of SFV services (Sky, Virgin, BT) do offer mobile services. However, these were originally fixed-line operators that moved into mobile, either through operating a Mobile Virtual Network Operator (which essentially re-sells the host mobile network's product) or by acquiring an existing mobile network operator (e.g. BT acquired EE). Thus any supply-side substitution that exists appears to be primarily from fixed into mobile, which is not relevant to the question of whether mobile services constrain fixed services.

### Conclusion

179. I do not consider the constraint from mobile to have been sufficient to prevent SFV service prices being raised above the level of a SSNIP. I therefore do not consider mobile services to be a part of the market for SFV services (for either Voice Only or Split Purchase Customers). This is consistent with Ofcom's views.

## 6.2.7 Exclusion of BT Basic from the market

180. As set out in paragraph 64.1, BT Basic is a social telephony scheme sold by BT to customers who are recipients of specific means-tested Government benefits. This product is provided at a much reduced price relative to other BT line rental products<sup>155</sup> and as such, it is likely in a market of its own. I therefore exclude it from the markets I have defined here (and so exclude it from my

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<sup>155</sup> Statement, (Footnote 8)



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assessment of dominance). Furthermore, as BT Basic Customers are excluded from the definition of the Class, I do not consider them in my assessment of abuse.<sup>156</sup>

### 6.3 Geographic market definition

181. I note and apply the guidance from the EU Commission, in its Commission Notice on relevant markets, that the relevant geographic market “*comprises the area in which the undertakings concerned are involved in the supply and demand of products or services, in which the conditions of competition are sufficiently homogeneous and which can be distinguished from neighbouring areas because the conditions of competition are appreciably different in those area*”.<sup>157</sup>

182. Ofcom concluded that: “*In the UK excluding the Hull Area, we consider that competitive conditions are broadly similar and there is a clear national dimension in competition for SFV services.*”<sup>158</sup>

183. I also consider that the relevant geographic scope for each of the relevant services markets in this matter is the UK, excluding the Hull Area. This reflects the similarity in competitive conditions across this geographic area.

183.1. First, the incumbent network provider in Hull is KCOM (formerly Kingston Communications), whereas in the rest of the UK it is BT. BT does not compete to offer SFV services in the Hull area. As such, the competitive conditions in Hull are significantly different from the rest of the UK.

183.2. Second, BT faces a Universal Service Condition which requires it to provide retail landline telephony services across the UK (excluding the Hull Area) that are priced uniformly, irrespective of geographic location, in the area in which it operates.<sup>159</sup>

183.3. Third, access-based rivals to BT can use BT’s infrastructure throughout the UK to deliver retail services based on regulated wholesale services which are priced on a geographically averaged basis. Ofcom notes that competitors to BT price nationally at the retail level.<sup>160</sup>

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<sup>156</sup> Home Phone Saver is included in the defined market and is considered as part of my dominance assessment. However, as it is excluded from the Class, I do not consider it within my assessment of Abuse.

<sup>157</sup> Commission Notice on market definition, (para. 8)

<sup>158</sup> Statement, (para. 3.33)

<sup>159</sup> Provisional Conclusions, (para. 3.113)

<sup>160</sup> *Ibid.*

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184. While infrastructure based competition to BT, largely from Virgin Media, is only available in approximately half of the households,<sup>161</sup> the national pricing policies of BT and access based rivals mean that competitive conditions in the areas served by Virgin Media do not materially differ from the rest of the UK.

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<sup>161</sup> Ofcom states that Virgin Media cover 14.7 million premises (Table 1.2), and the UK has 30.5 million premises (Table 7.1), implying that Virgin Media's coverage is c.48%. Given that BT's network is almost ubiquitous, this implies it faces infrastructure-based competition in at least 48% of premises.  
[https://www.ofcom.org.uk/data/assets/pdf\\_file/0029/188822/wftmr-volume-2-market-assessment.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0029/188822/wftmr-volume-2-market-assessment.pdf)

## 7 DOMINANCE

185. In the previous section I have identified separate relevant markets for:
- 185.1. SFV services for Voice Only Customers; and
  - 185.2. SFV services for Split Purchase Customers.
186. For both of these markets the relevant geographic dimension is “in the UK excluding the Hull Area”. For brevity I omit this dimension in the subsequent discussion.
187. This section assesses whether BT had or has a dominant position in these markets over the Claim Period. While I consider that the access and calls components of SFV services should be in the same market, my assessment of dominance would be the same if I had defined separate markets for the access and calls components of SFV services. I demonstrate this by carrying out a dominance assessment under each approach.
188. Furthermore, while I consider that it is appropriate to define separate markets for SFV services to Voice Only and Split Purchase Customers throughout the Claim Period, I also demonstrate that my assessment of dominance would remain unchanged if a single market was defined for SFV services for Voice Only and Split Purchase Customers prior to 1 April 2018.
189. To assess dominance I follow the legal and economic framework set out in Section 7.1 below.
- 189.1. I start by assessing market share. From a legal perspective, dominance is unlikely at a share below 40%, while there is a rebuttable presumption of dominance at a share above 50%. From an economic perspective, the concept of dominance is equivalent to the economic concept of significant market power. There is no absolute threshold of market share above which significant market power is inevitable. However, the higher the market share, the greater the countervailing factors would need to be (for instance, in relation to the absence of barriers to entry and expansion) in order to conclude that the firm in question had no market power. I find, for each market, that BT’s market share was above (often well above) the level which gives rise to a rebuttable presumption of dominance.
  - 189.2. I have then considered relevant countervailing factors (such as whether there are low barriers to entry and expansion). I find that there are no sufficient countervailing factors which affect my conclusion that BT has a dominant position.

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190. I therefore conclude that BT has occupied a dominant position in these markets throughout the Claim Period.

191. I draw primarily on the evidence in Ofcom’s Review as this is the most recent and relevant data available in the public domain.

### 7.1 Legal and economic framework for assessing dominance

192. Dominance has been defined as “a *position of economic strength enjoyed by an undertaking, which enables it to prevent effective competition being maintained on a relevant market, by affording it the power to behave to an appreciable extent independently of its competitors, its customers and ultimately of consumers*”.<sup>162</sup> From an economic perspective, this involves assessing whether the undertaking in question is able profitably to raise prices above the competitive level for a significant period of time, or in other words has significant market power.<sup>163</sup>

193. In practice, the assessment typically starts by considering the market share of the firm in the relevant market or markets. High market shares can provide a useful – if preliminary – indication of whether the firm occupies a dominant position in the relevant market or markets, particularly where the level of market share has been persistent over time. EU precedent is that a finding of dominance at a share below 40% is unlikely, while there is a rebuttable presumption of dominance at a share above 50%.<sup>164</sup>

194. From an economic perspective, information on market shares alone is not sufficient for the assessment of whether a firm has significant market power (and so dominance). In principle, if barriers to entry and expansion for rivals were sufficiently low, a firm could have no market power even at very high levels of market share. In the extreme, if where a market is fully contestable – which is the case where there are no barriers to entry or expansion, no sunk costs, and entry can happen immediately – then even a monopolist would not be able to increase prices above the competitive level (as to do so would immediately attract so-called “hit and run” entry).

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<sup>162</sup> Judgment of 14 February 1978, *United Brands and United Brands Continentaal v Commission*, 27/76, EU:C:1978:22

<sup>163</sup> Commission Guidance on Article 82 Enforcement Priorities, (para. 11)

<sup>164</sup> Case C-62/86 *AKZO Chemie BV v Commission* ECLI:EU:C:1991:286, (para. 60)

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195. However, as a general matter, the higher the market share of the potentially dominant firm, the stronger must be the evidence of an absence of barriers to entry and expansion, in order to overturn a conclusion of significant market power. One therefore also needs to consider factors such as the constraints on the firm from actual competitors, from potential competitors (i.e. the threat of new entry or expansion of rivals), and from countervailing buyer power.<sup>165</sup>
196. As mentioned above<sup>166</sup>, the concept of dominance is similar to but not exactly the same as the question of whether a firm has SMP in a regulatory context. The key difference between the two concepts is that the assessment of dominance relates to the period of infringement, while the assessment of SMP is forward-looking. This means that a firm could have had a dominant position in the past but, if there is expected to be a material change towards increased competition in the future, then the same firm may not have a position of SMP for the purposes of whether *ex ante* regulation should be applied.

## 7.2 Dominance assessment in the market for SFV services to Voice Only Customers

197. In relation to the provision of SFV services to Voice Only Customers, the Statement noted that *“BT is the dominant provider of standalone fixed voice services to voice-only customers with around 70% of the market.”*<sup>167</sup> and *“...we do not consider that BT faces any significant constraints on its ability to act independently within the markets for the purchase of voice-only access and calls”*.<sup>168</sup>
198. I note that Ofcom’s analysis was forward-looking, whereas I have assessed dominance in respect of the entire Claim Period. However, my conclusions are in line with those of Ofcom.

### 7.2.1 Market shares

199. As set out above, I assess market shares in:
- 199.1. a (hypothetical) market for the SFV access component to Voice Only Customers; and

<sup>165</sup> Commission Guidance on Article 82 Enforcement Priorities, (para. 12).

<sup>166</sup> Para.67 and Footnote 33.

<sup>167</sup> Statement, (para. 3.54)

<sup>168</sup> Statement, (para. 3.48)

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199.2. a market for SFV services (i.e. including both access and calls components) to Voice Only Customers.

200. While I consider that the latter market is the correct relevant market, I carry out the assessment in this order because Ofcom provides data on market shares on the access and calls components separately. I therefore set out the data on the separate components first, followed by my assessment of the combined position.

201. For each, I make an assessment based on the data available to me at this stage. I go on to set out the additional data I would need to confirm or refine my findings, and the methodology I would use to do, so post-certification.

### Market shares in the (hypothetical) market for SFV access to Voice Only Customers

202. The data considered by Ofcom for the assessment of SMP shows that for the access component of SFV services for Voice Only Customers, as measured by the number of lines<sup>169</sup>, BT's share was between 76% and 68% over the period 2013 to Q1 2017.

**Figure 10** Voice-only access market shares<sup>170</sup>

**Table 1.10: Shares of lines to voice-only lines by CP (in ranges)**

	BT	Post Office	TalkTalk	SSE	Virgin Media	Sky	Phone Co-op	Total non-BT
2013	76%	10% - 20%	< 10%	< 5%	< 5%	< 1%	< 1%	24%
2014	73%	10% - 20%	< 10%	< 5%	< 5%	< 1%	< 1%	27%
2015	73%	10% - 20%	< 10%	< 5%	< 5%	< 1%	< 1%	27%
2016	71%	10% - 20%	< 10%	< 5%	< 5%	< 1%	< 1%	29%
Q1 2017	68%	10% - 20%	< 10%	< 5%	< 5%	< 1%	< 1%	32%

Source: s.135 responses

Source: Ofcom's Evidence

Note: Ofcom has excluded Direct Save Telecom, Plusnet and Utility Warehouse from the analysis as it considered that these communications providers have an immaterial share of lines. (See para. 1.35)

203. As more recent data is not available from Ofcom (and the more recent data is relevant to the Claim Period), I have considered whether the decline in BT's market share seen up to Q1 2017 suggests that its market share would have fallen below 50% in the period from Q1 2017 to the present time.

<sup>169</sup> Where the geographic scope of the market is as set out above i.e. the UK excluding the Hull Area.

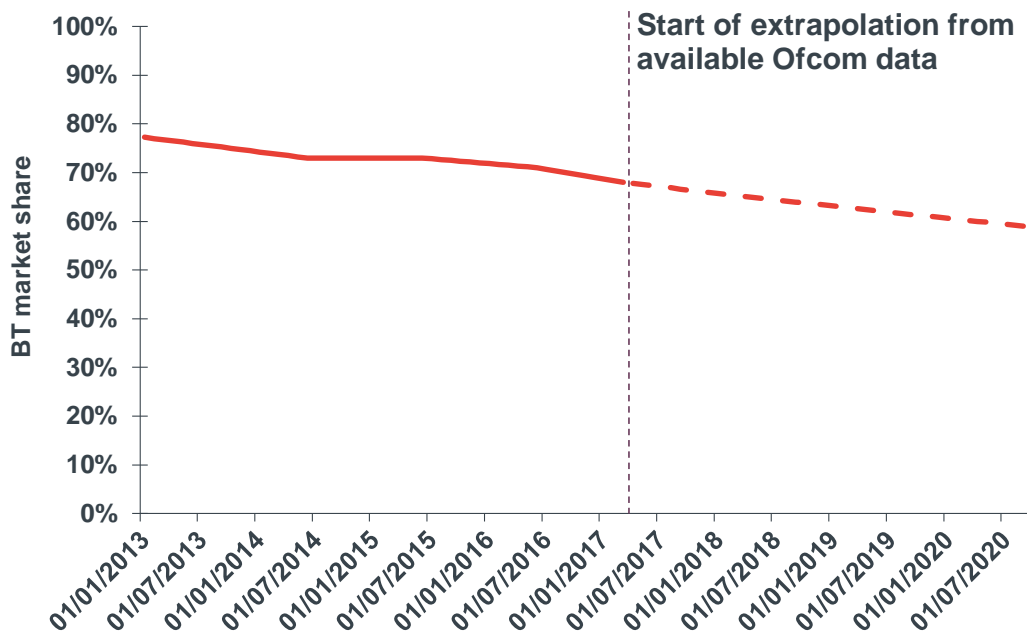
<sup>170</sup> Whilst Ofcom also assessed revenue shares this data is redacted, and therefore I am unable to form my own view on the basis of this data at present.

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204. I do not think this likely to be the case. Projecting the trend in BT's market share forwards, I estimate BT's current share of access to be around 61%. This can be seen in Figure 11 below.

205. As set out above, this level of market share, sustained through the Claim Period, gives rise to a rebuttable presumption of dominance for BT in the (hypothetical) market for SFV access to Voice Only Customers.

**Figure 11 Projecting BT's market share for SFV access to Voice Only Customers**



Source: Frontier Economics and the Provisional Conclusions

206. To estimate these shares, I have used the annual data provided by Ofcom, shown as the solid line in Figure 10 above, to calculate the implied monthly cumulative aggregate growth rate ("CAGR") for BT's share. I have then applied this CAGR to the annual numbers to a) derive estimates for monthly market shares, and b) project BT's market shares forward beyond Q1 2017.

207. I note that in the 2020 Review, Ofcom reports that BT's volumes are declining (from 1.5m customers in early 2017 to 1.2m customers in late 2019).<sup>171</sup> Ofcom also reports that BT's share is increasing and is currently over 75%.<sup>172</sup> If anything, this would suggest my conclusions as to BT's current share are an

<sup>171</sup> 2020 Review, p2.

<sup>172</sup> 2020 Review, p2.

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underestimate, and hence my subsequent conclusions as to dominance are conservative.

208. Following certification, I would need access to the following data to better estimate market shares for the periods in which I currently have projections:

208.1. Monthly volume of the access component of SFV services *i.e.* number of lines (specifically for Standard Line Rental, Line Rental Saver, Line Rental Plus and Home Phone Saver<sup>173</sup>) sold to Voice Only Customers by BT from 1 April 2017 to 1 April 2018.

208.2. Monthly volume of the access component of SFV services *i.e.* number of lines sold to Voice Only Customers by rivals from 1 April 2017 to 1 April 2018, or estimates thereof.

209. I expect this data to be held by BT.

### Market shares in the market for SFV services (i.e. including both access and calls components) to Voice Only Customers

210. In order to assess BT's market share in this combined market, I rely on the evidence collected and assessed by Ofcom in the Provisional Conclusions and the Statement, as the most relevant and recent data available in the public domain. However, the detailed tables of market shares in the Provisional Conclusions are entirely redacted.<sup>174</sup> Accordingly, the volume-based market shares available to me are Ofcom's estimates of:

210.1. market shares for the access component of SFV services, as measured by number of lines, for Voice Only Customers, for 2013 to Q1 2017, as reported above in Figure 10; and

210.2. a statement from Ofcom on market shares for SFV calls, as measured by number of minutes, but not split by Voice Only and Split Purchase Customers.<sup>175</sup> The detailed data underlying this statement has been redacted<sup>176</sup> so the precise time-period covered is not clear, although it is likely to cover data up to 2016/17 giving the timing of Ofcom's review.

<sup>173</sup> I note that customers of Home Phone Saver are in principle in the relevant markets even though this is an Excluded Service. I therefore require data on Home Phone Saver for the purposes of the market definition and dominance assessment, but thereafter (i.e. for the purposes of assessing abuse) I exclude Home Phone Saver from the analysis.

<sup>174</sup> For instance, see Provisional Conclusions, Annexes, (Figure A8.16 – 8.18)

<sup>175</sup> Ofcom did not have any evidence on which to break down the calls component of SFV services into calls made by Voice Only Customers and those made by Split Purchase Customers: Ofcom's Evidence, (para. 1.42)

<sup>176</sup> Ofcom's Evidence, (Table 1.18)



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211. I have set out above that I estimate that BT’s market share for the access component of SFV services for Voice Only Customers has remained materially above 50% throughout the Claim Period. With regard to calls, Ofcom states that “[BT] also has a high market share of over 70% for standalone fixed voice calls based on volume”.<sup>177</sup>
212. While the latter does not distinguish between Voice Only and Split Purchase Customers, and combined market shares cannot be calculated across access and calls (as access is measured by number of lines and calls are measured in minutes), I consider the shares for the individual components support the view that BT’s overall share of the market for SFV services for Voice Only Customers is materially above the level at which there is a rebuttable presumption of dominance.
213. Ofcom also assessed revenue-based market shares<sup>178</sup>, but the detailed data underlying this assessment is redacted. However, I note that:
- 213.1. BT appears to have the largest share of revenues for the access component of SFV services – Ofcom presents a graph which shows BT’s revenue market shares for the access component of SFV services to be above 80% from 2013/14 to 2015/16.<sup>179</sup> (In this analysis, Ofcom does not distinguish between Voice Only and Split Purchase Customers.)
- 213.2. BT appears to have the largest share of revenues for the calls component of SFV services – Ofcom states in relation to SFV calls that “BT’s market share has been in excess of 76% over the past four years”.<sup>180</sup> Again, Ofcom has not distinguished between Voice Only and Split Purchase Customers for these purposes.
214. This suggests that BT’s revenue market shares whether for (i) the calls component (ii) the access component separately or (iii) calls and access together are also likely to be materially above 50%.<sup>181</sup> However, in the absence of more granular data on the specific services in question, I am unable to assess this further at this stage.
215. Thus, based on the information currently available, my preliminary conclusion is that, on both a volume and revenue market share basis, BT had a

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<sup>177</sup> Statement, (para. 3.38)

<sup>178</sup> Provisional Conclusions, Annexes, Annex 8

<sup>179</sup> Provisional Conclusions, Annexes, (Figure A8.14)

<sup>180</sup> Provisional Conclusions, Annexes, (para. 8.48)

<sup>181</sup> Indeed, there is no obvious reason to expect that BT’s share of the calls component would be different to its share of the access component.

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share materially above 50% throughout the Claim Period. This conclusion appears to be true whether the market is defined to include both the access and calls components, or the access component only.

216. I therefore conclude (on a preliminary basis) that BT's share is at a level which gives rise to a rebuttable presumption of dominance, throughout the Claim Period.

217. To make a more accurate assessment of market shares, I would need to following data:

217.1. Annual volume (number of minutes) of calls made by BT Voice Only Customers (excluding customers of BT Basic) from 2015 to 2018.

217.2. Annual volume (number of minutes) of calls made by Voice Only SFV customers of rivals from 2015 to 2018.

217.3. Annual revenues from BT Voice Only Customers for the SFV access component (excluding BT Basic) from 2015 to 2018.

217.4. Annual revenues from rivals' Voice Only Customers for the SFV access component from 2015 to 2018.

217.5. Annual revenues from BT Voice Only Customers for the SFV calls component (excluding BT Basic) from 2015 to 2018.

217.6. Annual revenues from rivals' Voice Only Customers for the SFV access component from 2015 to 2018.

218. This information, alongside the data set out in paragraph 208, will allow me to estimate annual revenue and volume market shares for the access and calls components from 2015 to 2018 and thereby provide a more accurate assessment of BT's market shares within the two components individually and jointly. This can be used to update the accuracy of this part of my dominance assessment.

219. In addition to the above data, I would also need access to the confidential versions of the key Ofcom documents (as held by BT) and BT's submissions to Ofcom. This will allow me to understand Ofcom's analysis on market shares and so further refine my assessment of dominance.<sup>182</sup>

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<sup>182</sup> Indeed, more generally I will need access to the following to verify the initial conclusions I set out in this report: BT confidential versions of key Ofcom documents, any s.135 submissions referred to within the key Ofcom documents, BT unredacted Consultation responses and correspondence with Ofcom BT submissions, and any correspondence relating to BT seeking to alter the Commitments.

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## 7.2.2 Barriers to entry and expansion

220. Based on the evidence available, I find that there are likely to be significant barriers to customer acquisition in the (hypothetical) market for SFV access to Voice Only Customers, as well as in the market for SFV services to Voice Only Customers.
221. First, there are barriers to entry and expansion for rivals resulting from the limited level of customer switching. Ofcom's survey data indicates that Voice Only Customers tend, in general, to be less engaged and more brand loyal than other customers, particularly if they are customers of BT:
- 221.1. Only 6% of all Voice Only Customers and 3% of BT's Voice Only Customers were classified as "engaged";<sup>183</sup>
- 221.2. Only 3% of all Voice Only Customers and 1% of BT Voice Only Customers had switched suppliers in the last 12 months;<sup>184</sup>
- 221.3. 74% of all Voice Only Customers and 77% of BT's SFV customers had been with BT for over 10 years.<sup>185</sup>
222. This low level of engagement and switching indicates that a new entrant in the market, or an existing operator looking to expand, would face significant challenges in inducing customers to switch to its own service, and so face high barriers to expansion. As could be seen in Section 7.2.1, rivals have been growing their *combined* share within the access component for Voice Only Customers by around 2 percentage points per year only. Furthermore, TalkTalk has taken a decision no longer to offer SFV access to new customers.<sup>186</sup> Ofcom also points to the fact that other operators in the market have stated that they face barriers to entry and expansion,<sup>187</sup> and barriers to customer acquisition for SFV access in particular.<sup>188</sup>
223. The barriers described above would apply equally to a market defined to include only the access component, or one defined to include both the access and calls components of SFV services.

<sup>183</sup> Ofcom's Evidence, (Figure 1.53, Figure 1.54, p.44)

<sup>184</sup> Ofcom's Evidence, (Figure 1.57, Figure 1.58, p.47)

<sup>185</sup> Ofcom's Evidence, (Figures 1.55, Page 54 and Figure 1.56, p.46)

<sup>186</sup> Ofcom's Evidence, (para. 1.30)

<sup>187</sup> Statement, (para. 3.40)

<sup>188</sup> Provisional Conclusions, (paras. 4.77-4.79)

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224. I therefore conclude that barriers to entry and expansion are not sufficiently low to alter the view that BT's market share is sufficient to give rise to a dominant position in the market for SFV services for Voice Only Customers (or indeed, a hypothetical market for SFV access for Voice Only Customers).

### 7.2.3 Pricing and Profitability analysis

#### Price analysis

225. I have assessed whether BT faces or has faced over the Claim Period material competitive constraints on its pricing for SFV services. I have therefore analysed both the level and trend in prices of SFV services, and done so separately for the access and calls components.

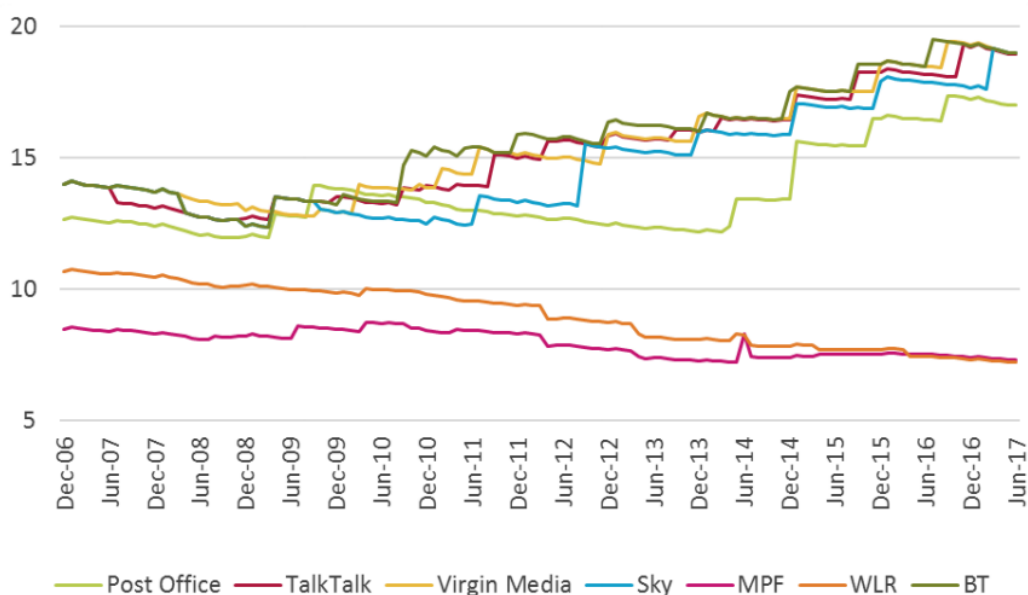
#### Access component

226. Ofcom has analysed the evolution of the prices of the access component of SFV services for the major providers in the market. Prices have trended upwards since 2009 (and throughout the Claim Period) while costs (as measured by WLR and MPF, the key wholesale inputs) have declined over the whole period. As a result, the gap between prices and costs has increased significantly over time. This suggests the presence of (increasing) market power for BT.

227. This data is shown in Figure 12.

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**Figure 12 Ofcom’s analysis of price evolution of the access component of SFV services, BT and rival providers, compared to the evolution of the cost of key wholesale inputs (WLR and MPF), 2006-2017**



Source: Ofcom’s Evidence.

Ofcom notes: Adjusted for CPI, excludes line rental saver pre-payment tariffs, Y-axis starts at £5/month

228. Ofcom also found evidence that BT acts as a price leader, with other CPs following its increases in line rental in terms of both timing and magnitude.<sup>189</sup> It would therefore be wrong to conclude that BT does not have market power on the basis that its prices were at a similar level to those of rivals.

229. Rather, for the Claim Period, it can be seen from the figure above that:

229.1. BT has been the first to raise its prices.<sup>190</sup>

229.2. When rivals do react, they have typically set their prices at or just below BT’s, with the result that any “undercutting” broadly maintains the previous price differential, while BT’s prices have consistently remained the highest in the market.

229.3. While the Post Office appears to have had a different strategy until 2014, with prices substantially below those of BT, it failed to capture sufficient sales to cause BT to respond by cutting prices itself. Moreover, since 2014, the Post Office has substantially increased prices to a level close to BT’s prices and those of other providers.

<sup>189</sup> Provisional Conclusions, (para. 4.67)

<sup>190</sup> I note that there are isolated examples of Virgin Media appearing to move first (between December 2009 and January 2010, and again in January 2013), but these fall outside the Claim Period.

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230. Moreover, the costs of the main input to the access component of SFV services (namely, WLR) have been declining over the Claim period – this can be seen for the period up to June 2017 in Figure 12 above.<sup>191</sup> Had rivals been setting prices at the competitive level, I would have expected them to decline over time.
231. The evidence above indicates that BT has been able to raise prices substantially above the competitive level over time and in contrast to the reduction in its costs. That evidence therefore reinforces my view that BT is dominant in the access component of SFV services to Voice Only Customers.

### Calls component

232. Ofcom does not present a similar analysis for the price of the calls component of SFV services, and its assessment of the evolution of non-access revenues (which I assume would consist largely of call-related revenues) is mostly redacted. It notes in the Provisional Conclusions that BT's prices for call plans are typically lower than for its competitors, but also seems to suggest that revenues are higher than competitors and that price increases have not obviously been linked to costs.<sup>192</sup> However, as key parts of this paragraph are redacted, I cannot draw firm conclusions based on this (and Ofcom itself does not draw any firm conclusions).<sup>193</sup>
233. I therefore carry out my own assessment of how call prices may have evolved over the Claim Period. I do not have sufficient information on the prices or volumes of the calls component of SFV services for Voice Only Customers. I am instead able only to review data on BT and its rivals' *total* call revenues and *total* call volumes.
234. Figure 13 below shows the Average Revenue Per Minute (ARPMs), a proxy for average unit call prices paid by customers, split by BT and non-BT customers, over the period 2009 – 2019.
235. Figure 13 below shows that BT's call prices have, on average, increased since 2009 while prices charged by BT's competitors have fallen.

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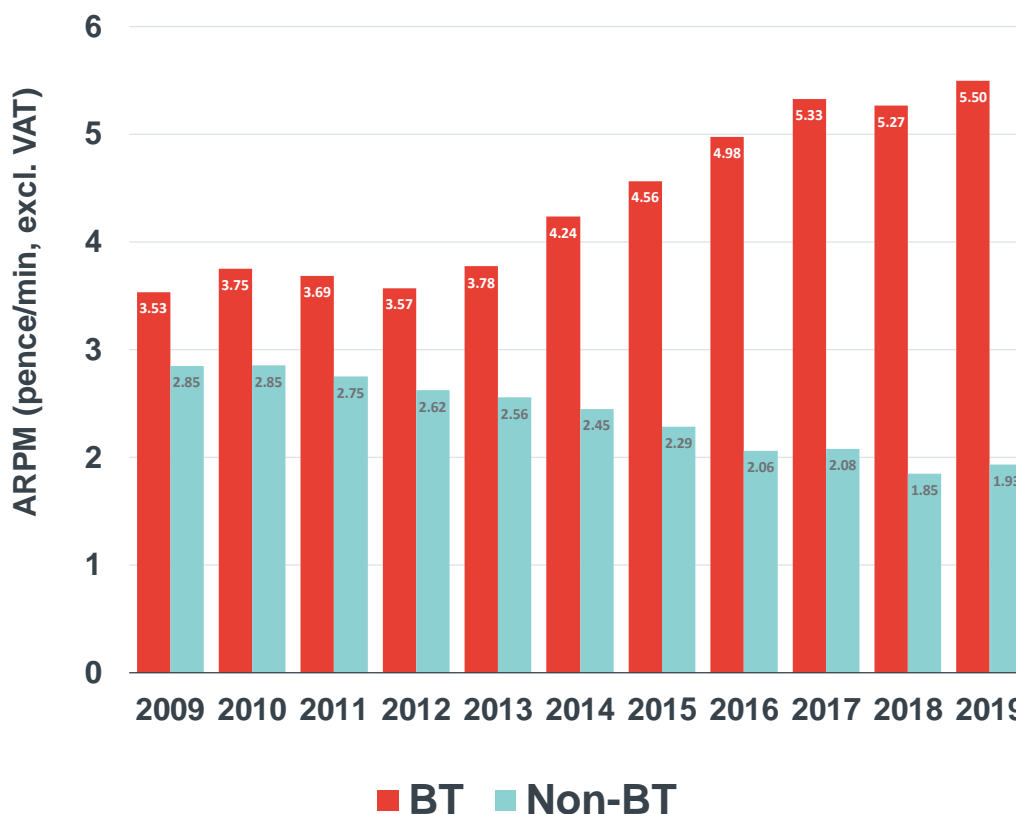
<sup>191</sup> This is also true for the rest of the Claim Period for Voice Only Customers, as will be seen in Section 8.2.1.

<sup>192</sup> Provisional Conclusions, (para. 5.26)

<sup>193</sup> Provisional Conclusions, (para. 5.26)

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**Figure 13 BT vs. non-BT calls ARPMs, 2009 – 2019**



Source: Frontier Economics and Ofcom data.

Note: ARPMs do not control for differences in the distribution of call types made by different customers. However, I have checked using information on the distribution of call types between BT and its competitors and found that the differences in ARPMs cannot be explained by differences between the calling patterns of BT and non-BT customers. This analysis is set out in Annex B.

236. Since BT's competitors have lower market shares and likely face similar underlying costs to BT<sup>194</sup>, their prices are more likely to reflect the competitive level for calls. If so, these data suggest that BT's calls prices have been set at above the competitive level over the Claim Period.

237. While this analysis is preliminary, it supports my conclusion that BT has a dominant position in the market for SFV services to Voice Only Customers (or indeed, a hypothetical market for SFV calls to Voice Only Customers).<sup>195</sup>

238. Once I have detailed data on actual call volumes and revenues for SFV calls by Voice Only Customers, I will be able to revisit this finding. To this end, I require data on total revenues and total volumes of calls made by Voice Only Customers

<sup>194</sup> BT has an SMP obligation of non-discrimination in wholesale markets so the relevant cost inputs should be on an equivalent basis to that for BT (see for instance [https://www.ofcom.org.uk/consultations-and-statements/category-3/bt\\_smp](https://www.ofcom.org.uk/consultations-and-statements/category-3/bt_smp))

<sup>195</sup> I note that in the combined market for SFV services as a whole (access and calls), to overturn the view that BT has a dominant position in this market it would be necessary to show that the prices of the calls component were sufficiently below the competitive level so as to overturn the finding that the prices of the access component are above the competitive level.

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of SFV services for each year between 2015 to 2018, for both BT (excluding BT Basic) and rivals.

239. Using this data I could construct an ARPM time series for SFV calls by Voice Only Customers in the same way I have constructed the ARPM series in Figure 13. As the ARPM acts as a proxy for price – it reflects the average unit price per minute – it will allow me to assess the trend in prices for the calls component of SFV services in the way I have set out above in paragraphs 234 and 235.

### Profitability analysis

240. Limited data is available on profitability as much of that information is redacted from the Ofcom documents.<sup>196</sup> However, the unredacted material shows that BT's profitability per line (therefore covering both access and calls components) has been high and increasing over time. For instance, Ofcom found that BT's EBIT margins had been increasing and were at 34-42% in 2015/6, and that BT was making higher profits on fixed voice customers than its rivals.<sup>197</sup>

241. While Ofcom's assessment of profitability on the individual components is redacted, Figure 12 above shows that the price of the access component was increasing, while the cost of the most important cost input was declining, up to June 2017. This suggests that the profitability on the access component was increasing (which would appear consistent with Ofcom's view across both components). However, I will revisit this view upon access to better data (which I set out below).

242. On the basis of this evidence, I consider there is no reason to depart from the view that BT had a dominant position in the market for SFV services to Voice Only Customers (or indeed, a market for SFV access to Voice Only Customers) over the Claim Period.

243. In order to better assess the profitability of BT's SFV services to Voice Only Customers over the Claim Period, I would need BT's annual gross margins from 2015 to 2018 for:

243.1. the access component of SFV services sold to Voice Only Customers by product (excluding BT Basic); and

<sup>196</sup> For instance, see Provisional Conclusions, Annexes, Annex 5.

<sup>197</sup> Provisional Conclusions, Annex 5, paragraph A5.59, A5.70 and A5.71. I note that much of Ofcom's analysis is redacted, and that the some of the analysis applies across all of BT's fixed voice customers rather than relating to SFV customers only. Nor is there any split between Voice Only and Split Purchase Customers.



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243.2. the calls component of SFV services for Voice Only Customers by product (excluding BT Basic).

244. I would also need to have the confidential version of the Provisional Conclusions in order that I can examine its methodology and conclusions further.

245. This should allow me to assess both the absolute level and the trend in the profitability of the two components of SFV services to Voice Only Customers over the Claim Period.

### 7.2.4 Countervailing buyer power

246. In principle, customers that are very large could threaten to withhold purchases in a manner that puts a dominant firm at risk or could sponsor entry from alternative rivals to increase the level of competition in the market. If either feature was present, this could give rise to a countervailing force that would make it impossible for a firm with a high share to exert market power.

247. However, given that the customers here are individual end-customers, they are individually small and have no realistic prospects of sponsoring alternative entry. As such, countervailing buyer power is not a relevant issue for the purposes of my analysis.

### 7.2.5 Conclusion

248. My preliminary conclusion is that BT has a dominant position in the market for SFV services to Voice Only Customers (or indeed, a hypothetical market for SFV access to Voice Only Customers) over the Claim Period.

## 7.3 Dominance assessment in the market for SFV services to Split Purchase Customers

249. In this section, I assess whether BT has a dominant position in the market for SFV services for Split Purchase Customers, on the basis of separate markets for access and calls, and a single combined market.

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### 7.3.1 Market shares

#### Market shares in the (hypothetical) market for SFV access to Split Purchase Customers

250. Figure 14 below shows that Ofcom estimated that BT has sustained a share of the access component of SFV services for Split Purchase Customers (as measured by number of lines) close to 100% over the period 2013 to Q1 2017.

**Figure 14** Market shares for the access component of SFV services to Split Purchase Customers

	BT	Post Office	TalkTalk	SSE	Virgin Media	Sky	Phone Co-op	Total non-BT
2013	98%	< 3%	< 1%	< 1%	< 1%	< 1%	< 1%	2%
2014	97%	< 3%	< 1%	< 1%	< 1%	< 1%	< 1%	3%
2015	97%	< 3%	< 1%	< 1%	< 1%	< 1%	< 1%	3%
2016	97%	< 3%	< 1%	< 1%	< 1%	< 1%	< 1%	3%
Q1 2017	97%	< 3%	< 1%	< 1%	< 1%	< 1%	< 1%	3%

Source: Ofcom's Evidence

Note: Ofcom has excluded Direct Save Telecom, Plusnet and Utility Warehouse from the analysis as it considered that these communications providers have an immaterial share of lines. (See para. 1.35)

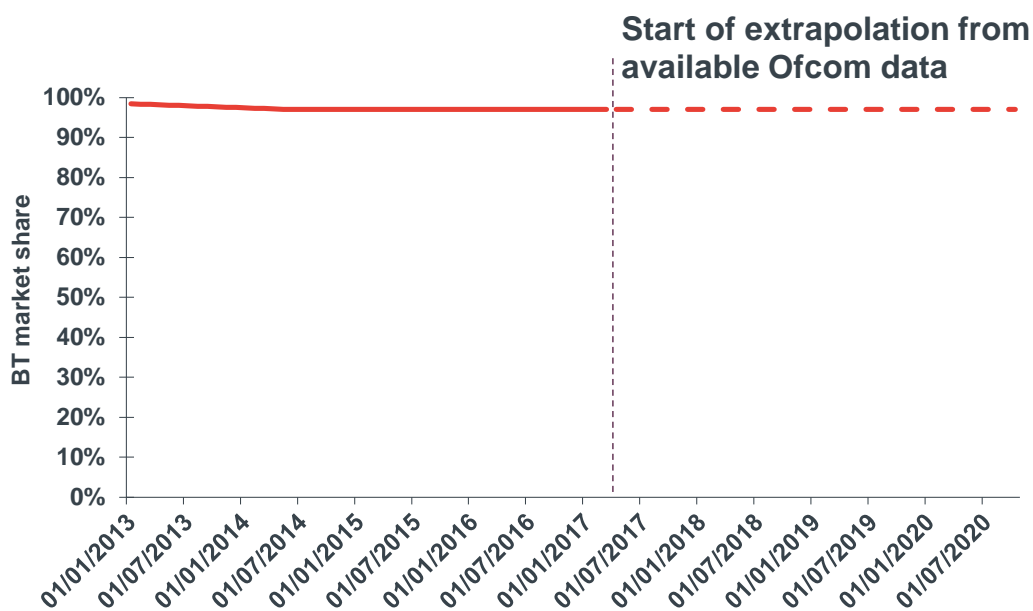
251. Ofcom also noted that *"BT had by far the largest share of split-purchaser access revenue in all financial years for which we have data."*<sup>198</sup>

252. Projecting BT's market shares forward based on the trend seen in the table above, I estimate that its share today is likely still to be around 97%. To do this I have used the data provided by Ofcom, shown in Figure 14 above, to estimate the implied monthly CAGR for the market shares. I then applied this CAGR to the annual numbers to a) derive estimates for monthly market shares, and b) project the market shares forward so as to estimate shares beyond Q1 2017. The results are shown in Figure 15.

<sup>198</sup> Ofcom's Evidence (para. 1.41)

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**Figure 15** Projecting BT's market share for access for Split Purchase Customers



Source: Frontier estimates based on Ofcom data

253. Following certification, I would need access to the following data from BT to better estimate market shares for the periods in which I currently have projections:

253.1. Volumes (as measured by the number of lines) for the access component of SFV services by product (specifically, for Standard Line Rental, Line Rental Saver, Line Rental Plus and Home Phone Saver) sold to Split Purchase Customers by BT from 1 April 2017 to 1 April 2018, on a monthly basis.

253.2. Volumes (as measured by the number of lines) of the access component of SFV services sold to Split Purchase Customers by rivals from 1 April 2017 to 1 April 2018, on a monthly basis.

**Market shares in the market for SFV services (i.e. including both access and calls components) to Split Purchase Customers**

254. Since Ofcom's data on SFV call volumes and revenues does not distinguish between calls made by Voice Only Customers and Split Purchase Customers, I rely on Ofcom's overall conclusion regarding BT in respect of both customer

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groups that “*It also [has] a high market share of over 70% for standalone fixed voice calls based on volume*”.<sup>199</sup>

255. While it is difficult to compute volume shares for a combined market - as the access component of SFV services is measured in lines, whereas the calls component is measured in minutes - BT has a share of close to 100% in the access component of SFV services for Split Purchasers till Q1 2017 of the Claim Period, and over 70% for the calls component of SFV services (albeit across Split Purchase and Voice Only Customers), as discussed in Section 7.2.1 above.<sup>200</sup>
256. As set out in the dominance assessment for Voice Only Customers, whilst Ofcom also assessed revenue shares for both access and calls,<sup>201</sup> detailed data on this is redacted. I note though that:
- 256.1. BT appears to have the largest share of revenues for the access component of SFV services: Ofcom presents a graph which shows BT’s revenue market shares for the access component (Ofcom does not distinguish between Voice Only and Split Purchase Customers) to be above 80% from 2013/14 to 2015/16.<sup>202</sup>
- 256.2. BT appears to have the largest share of revenues for the calls component of SFV services: Ofcom states in relation to the calls component (again, Ofcom does not distinguish between Voice Only and Split Purchase Customers) that “*BT’s market share has been in excess of 76% over the past four years.*”<sup>203</sup>
257. This suggests that BT’s revenue market shares are also likely to be above 50% but in the absence of granular data, I cannot assess this further at this stage.
258. In my view, therefore, based on the information available to me currently, both volume and revenue market shares for SFV services to Split Purchase Customers appear to have been persistently above 50%, whether the market is defined to include both the access and calls components, or the access component only. This share is at a level that gives rise to a rebuttable presumption of dominance on the part of BT.

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<sup>199</sup> Statement, (para. 3.38)

<sup>200</sup> The detailed data underlying this statement has been redacted (see Ofcom’s Evidence, (Table 1.18)) so the precise time-period covered is not clear although it will likely cover data till 2016/7 giving the timing of the review.

<sup>201</sup> Provisional Conclusions, Annexes, Annex 5.

<sup>202</sup> Provisional Conclusions, Annexes, (Figure A8.14)

<sup>203</sup> Provisional Conclusions, Annexes, (para. 8.48)

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259. The data I would need to make a more accurate assessment of market shares are as follows:
- 259.1. Annual volume (number of minutes) of calls made by BT Split Purchase Customers (excluding customers of BT Basic) from 2015 to 2020.
  - 259.2. Annual volume (number of minutes) of calls made by Split Purchase Customers of rivals from 2015 to 2020.
  - 259.3. Annual revenues from BT Split Purchase Customers of the SFV access component (excluding BT Basic) from 2015 to 2020.
  - 259.4. Annual revenues from rivals' Split Purchase Customers of the SFV access component from 2015 to 2020.
  - 259.5. Annual revenues from BT Split Purchase Customers of the SFV calls component (excluding BT Basic) from 2015 to 2020.
  - 259.6. Annual revenues from rivals' Split Purchase Customers of the SFV access component from 2015 to 2020.
260. This information, alongside the data set out in paragraph 253, should allow me to estimate more precisely BT's annual revenue and volume market shares for the access and calls components throughout the Claim Period, and thereby confirm the correctness of my preliminary conclusion that BT's market shares within the two components individually, and across both, have been materially above 50% throughout the Claim Period.

### 7.3.2 Barriers to entry and expansion

261. My assessment for Split Purchase Customers (and the evidence on which it is based) is largely the same as for Voice Only Customers. I consider that this assessment applies to a market for SFV services for Split Purchase Customers whether calls are included or not.
262. While Ofcom's survey evidence does suggest that Split Purchase Customers – using data on Split Supplier customers as a proxy, as data on Split Purchase Customers as a whole was not available<sup>204</sup> – are more engaged than Voice Only

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<sup>204</sup> Ofcom survey evidence relates to just Split Supplier customers rather than both Split Supply and Split Service customers as they had difficulty isolating/identifying Split Service customers. However, Ofcom considers that survey evidence from Split Supplier customers is a reasonable proxy for Split Purchase Customers as a whole as it estimates that Split Supplier customers account for around 80% of Split Purchase Customers, with the remaining 20% being Split Service customers. See Ofcom's Evidence (paras. 1.103 to 1.107)

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Customers, I do not consider that Split Purchase Customers are sufficiently engaged such that operators could easily enter or expand their operations:

262.1. Only 15% of Split Supplier customers were classified as “engaged”;<sup>205</sup>

262.2. Only 6% of Split Supplier customers had switched suppliers in the last 12 months;<sup>206</sup> and

262.3. 43% of Split Supplier customers had been with their supplier for over 10 years.<sup>207</sup>

263. A new entrant or existing operator is likely to find it difficult to attract new customers. This is demonstrated by the negligible decline in BT’s share for Split Purchase Customers reported by Ofcom and set out above in Figure 15. Ofcom also points to the fact that other operators in the market have stated that they face barriers to entry and expansion,<sup>208</sup> and barriers to SFV customer acquisition in particular.<sup>209</sup>

264. I therefore conclude that barriers to entry and expansion are not sufficiently low so as to alter my conclusion that BT has had a dominant position in the market for SFV services to Split Purchase Customers (or a hypothetical market for SFV access to Split Purchase Customers) throughout the Claim Period.

### 7.3.3 Price and Profitability analysis

265. The assessment of pricing and profitability for Split Purchase Customers is largely the same as for Voice Only Customers as set out in Section 7.2.3. In relation to prices, this is because prices for SFV access for Split Purchase Customers were identical to those for Voice Only Customers until the introduction of the BT Commitments (and prices for Split Purchase Customers have increased after the introduction of the BT Commitments for Voice Only Customers, as shown in Figure 7).

266. The profitability data carried out by Ofcom to which I refer in Section 7.2.3 is not available for Split Purchase Customers and Voice Only Customers separately. I therefore draw the same inferences as for Voice Only Customers, namely that BT’s EBIT margins had been increasing and were at 34-42% in

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<sup>205</sup> Ofcom’s Evidence (Figure 1.53, p. 44)

<sup>206</sup> Ofcom’s Evidence (Figure 1.57, p.47)

<sup>207</sup> Although I note that this is based on responses from less than 100 respondents. Ofcom’s Evidence (Figures 1.55, p. 45)

<sup>208</sup> Statement, (para. 3.40)

<sup>209</sup> Provisional Conclusions, (paras. 4.77-4.79)

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2015/6, that BT was making higher profits on fixed voice customers than its rivals<sup>210</sup>, and that the data suggests that the profitability on the access component was likely to have been increasing over time.

267. On the basis of this evidence, I consider there is no reason to depart from the view that BT had a dominant position in the market for SFV services to Split Purchase Customers (or indeed, a market for SFV access to Split Purchase Customers) over the Claim Period.

268. To confirm my assessment of pricing over time for the calls component of SFV services, I would need data on total revenues and volumes of calls made by BT Split Purchase Customers of SFV services (excluding BT Basic) for each year between 2015 to 2020.

269. In order to better assess the profitability of BT's SFV services to Split Purchase Customers over the Claim Period, I would need BT's annual gross margins from 2015 to 2020 for:

269.1. SFV access component options sold to Split Purchase Customers (excluding BT Basic)

269.2. the calls components of SFV services for the Split Purchase Customers (excluding BT Basic).

270. This should allow me to assess both the absolute level and the trend in the profitability of the two components of SFV services to Split Purchase Customers over the Claim Period.

### 7.3.4 Countervailing buyer power

271. As set out above in relation to Voice Only Customers, and for the same reasons, there is no relevant countervailing buyer power on the part of Split Purchase Customers.

### 7.3.5 Conclusion

272. My preliminary conclusion is that BT has a dominant position in the market for SFV services to Split Purchase Customers, or alternatively in a hypothetical market for SFV access to Split Purchase Customers, over the entire Claim Period.

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<sup>210</sup> Provisional Conclusions, Annex 5, paragraph A5.59, A5.70 and A5.71. I note that much of Ofcom's analysis is redacted, and that the some of the analysis applies across all of BT's fixed voice customers rather than relating to SFV customers only. Nor is there any split between Voice Only and Split Purchase Customers.

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273. Furthermore, for completeness, I note that the conclusions of this Section would also apply if a single market was defined for Voice Only and Split Purchase Customers up until 1 April 2018, and separate markets were defined thereafter, for the reasons set out above, namely:

273.1. market shares of the combined customer group would be at a level giving rise to a rebuttable presumption of dominance;

273.2. barriers to entry are similarly high across customer groups;

273.3. prices and profitability have remained high across both customer groups;  
and

273.4. there is unlikely to be countervailing buyer power in either customer group.



## 8 ABUSE

274. I am instructed to consider whether BT's pricing in the relevant markets was excessive and so amounts to an abuse of a dominant position contrary to the Chapter II prohibition. As I have defined a single market for SFV services including both the access and calls components, I need to consider whether prices of BT SFV Services as a whole (i.e. across the access and calls components when considered collectively) were excessive, for each customer group.

275. To do so I have adopted (and propose to adopt if the CPO is certified) the following approach:

275.1. First, I consider whether the price of the *access* component of SFV services (i.e. line rental) charged by BT for SFV services for Voice Only and Split Purchase Customers has been significantly and persistently above the competitive level. I begin by identifying meaningful competitive benchmarks against which to compare prices for the access component.

275.2. Second, I examine whether there is evidence that the prices for the calls component of BT SFV Services for Voice Only and Split Purchase Customers were *below* the competitive level, so as to offset any excessive price for the access component of the BT SFV Service.<sup>211</sup>

276. Ofcom also adopted this broad approach but most of its analysis is redacted.<sup>212</sup> I therefore make use of the data available in the public domain to carry out my assessment. At each stage, I identify what further information I will ultimately need to refine my analysis, and the methodology I propose to use at trial if the Claim is certified.

277. Accordingly, this section:

277.1. briefly sets out the legal framework within which I conduct the economic assessment of whether BT's prices were/are excessive;

277.2. identifies a competitive benchmark for access pricing for SFV service customers (Section 8.2);

277.3. assesses if the access prices were excessive (Section 8.3); and

<sup>211</sup> If the calls prices themselves are above the competitive level, then this would be a conservative approach to estimating damages.

<sup>212</sup> For instance, see Provisional Conclusions, (paras. 4.56-4.59), Provisional Conclusions, Annexes 5 and 8.

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277.4. examine if there is evidence that any excessive pricing of access has been offset by calls prices being below the competitive level, or by competitive rebalancing between calls and access (Section 8.4).

### 8.1 Framework for assessing abuse through excessive pricing

278. Article 102 TFEU/Chapter II of the Competition Act 1998 prohibit abuses of dominance.<sup>213</sup> In this case the relevant category of abuse is excessive pricing. I am instructed that the applicable legal principles on excessive pricing abuses have been articulated in a number of key cases, which set out the legal framework for my economic assessment.<sup>214</sup>

279. The abuse of unfair pricing is enshrined in the text of Article 102 TFEU as: “*directly or indirectly imposing unfair purchase or selling prices.*”<sup>215</sup> The Commission has explained that this notion of unfair pricing captures “[c]onduct which is directly exploitative of consumers, for example charging excessively high prices.”<sup>216</sup>

280. In the seminal case of *United Brands*, the CJEU held:

280.1. that the imposition of unfair selling prices is an abuse;

280.2. it is advisable to ascertain whether the dominant undertaking has used its dominant position to reap trading benefits which could not have been obtained in normal and sufficiently competitive conditions;<sup>217</sup>

280.3. a price that bears no reasonable relation to “*the economic value of the product supplied* [emphasis added]” is excessive;<sup>218</sup> and

280.4. that one approach for determining whether a price is unfair is whether: “*the difference between the costs actually incurred and the price actually charged is excessive and if the answer to this question is*

<sup>213</sup> Commission Guidance on Article 82 Enforcement Priorities, paragraph 1, Competition Act 1998, Section 18

<sup>214</sup> Judgment of 14 February 1978, *United Brands and United Brands Continentaal v Commission*, 27/76, EU:C:1978:22 (“*United Brands*”); *Pfizer and Flynn v CMA* [2020] EWCA Civ 339 (“*Flynn CoA*”); utortiesību un komunikēšanās konsultāciju aģentūra / Latvijas Autoru apvienība vs Konkurences padome, Case 177/16, 14 September 2017 (“*Latvian Copyright Society*”)

<sup>215</sup> Consolidated version of the Treaty on the Functioning of the European Union – Part three: Union Policies and Internal Actions – Title VII: Common Rules on Competition, Taxation and Approximation of Laws – Chapter 1: Rules on competition - Section 1: Rules applying to undertakings - Article 102 (ex Article 82 TEC) <https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:12008E102:EN:HTML>, paragraph (a)

<sup>216</sup> Guidance on Commission’s Enforcement Priorities in applying Article 102 TFEU, February 2009: [https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52009XC0224\(01\)&from=EN](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52009XC0224(01)&from=EN).

<sup>217</sup> *United Brands*, (para. 249).

<sup>218</sup> *Ibid.* (para. 235).

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*in the affirmative whether a price has been imposed which is either **unfair in itself** or when **compared to competing products** [emphasis added].”<sup>219</sup>*

281. The principles laid down in *United Brands* have been extensively discussed in the case law and economic literature. I understand that the most recent judgment is that of the Court of Appeal in *Flynn CoA*, which sets out the following (non-exhaustive) relevant principles:<sup>220</sup>

281.1. The basic test for abuse is whether the price is ‘unfair’. In broad terms, a price will be unfair when the dominant undertaking has reaped trading benefits which it could not have obtained in conditions of ‘normal and sufficiently effective competition’, i.e. ‘workable competition’.

281.2. One example of an unfair price is a price that is excessive because it bears no reasonable relation to the economic value of the good or service.

282. The Court of Appeal also emphasised that there is no single method or “way” in which abuse might be established and competition authorities have a margin of manoeuvre or appreciation in deciding which methodology to use and which evidence to rely on.

283. Green LJ also observed that the above propositions are supported by the economic literature, in particular that: there are many different tests; there are or may be difficulties with all tests and much will depend on the availability of evidence / data; all cases are highly fact and context specific.<sup>221</sup>

284. The Court of Appeal also emphasised that:

284.1. There is no discrete component of the test which assesses economic value: when the *United Brands* test is properly applied it is capable of assessing economic value so that **if a price is excessive it bears “no reasonable relationship to economic value”**;

284.2. “*The simple fact that a consumer will or must pay the price that a dominant undertaking demands is not therefore an indication it reflects a reasonable relationship with economic value. **But a proxy might be what consumers are prepared to pay for the good or service in an effectively competitive market ...***”<sup>222</sup>

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<sup>219</sup> *Ibid.*, (para. 252)

<sup>220</sup> *Flynn CoA*, (para. 97)

<sup>221</sup> *Flynn CoA*, (para. 107)

<sup>222</sup> *Flynn CoA*, (para. 155)

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284.3. *“Equally, if there is evidence of the prices being charged in relevant, comparator markets which were effectively competitive then those prices could be capable of acting as proxy evidence of the economic value of [the product in question]”.*<sup>223</sup> [Emphasis added]

284.4. The challenged price must also be “significantly and persistently” above the competitive benchmark in order to be deemed excessive.<sup>224</sup>

285. I note also that tests to screen for circumstances where excessive pricing (in the Chapter II CA98/Article 102 TFEU sense) is unlikely to arise have been discussed in the jurisprudence. For instance, AG Wahl’s Opinion in *Latvian Copyright Society* identifies that where there is a free market with no barriers to entry, high prices should normally attract new entrants and so the market will self-correct.<sup>225</sup> In his view, such situations should not result in excessive pricing antitrust cases.<sup>226</sup> Consequently, attention should concentrate on markets with such barriers, particularly in regulated sectors, and where any existing sectoral regulator has not acted to intervene.<sup>227</sup>

## 8.2 Identifying a competitive benchmark for access pricing

286. In the light of the above, it is necessary to identify a competitive benchmark to compare against the price in question. As an economist, I would typically adopt one of the following approaches to identifying the appropriate competitive benchmark(s), depending on the facts at issue:

286.1. a ‘cost plus’ estimate – building up a competitive benchmark price from its component costs, plus an appropriate profit margin;

286.2. prices in other comparable and competitive markets, which may be other geographic markets or adjacent product markets; and

286.3. prices of the same product in other time periods (to the extent that prices in these time periods were competitive).

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<sup>223</sup> *Flynn CoA*, (para. 172). I note that there may be other elements of economic value, but it is not clear what these are, and they would need to be considered on a case by case basis. I am not aware of any relevant elements of economic value in this case so do not explore this further at this stage.

<sup>224</sup> *Flynn CoA*, paragraph 40 (3). See also AG Wahl Opinion, *Latvian Copyright Society*, (para. 106)

<sup>225</sup> AG Wahl Opinion, *Latvian Copyright Society*, (para. 3)

<sup>226</sup> AG Wahl Opinion, *Latvian Copyright Society*, (para. 3)

<sup>227</sup> AG Wahl Opinion, *Latvian Copyright Society*, (paras. 4, 48 and 49)

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287. The products selected as a competitive benchmarks should be those whose prices most closely reflect the prices that would have prevailed in a sufficiently competitive market for the product(s) in question. That is obviously a highly fact-specific question.

288. In this section I consider the available benchmarks for my comparator exercise, identify the most appropriate benchmark or benchmarks, and explain why I have rejected other available benchmarks. I consider that there is no reason to consider separate benchmarks in relation to Voice Only Customers and Split Purchase Customers as the costs of provision (and so the competitive price levels) are likely to have been the same for both customer groups.

### 8.2.1 The best available competitive benchmark for the access component of SFV services

289. In my view, based on the information available to me, the most robust benchmark for the access component of SFV services is the price that prevailed in 2009 at the time of Ofcom's 2009 Review, adjusted to reflect changes over time in the key cost input - WLR. I consider this approach provides a good proxy for the competitive price level for access throughout the Claim Period.

290. I reach this preliminary conclusion because Ofcom found that BT did not have SMP in residential access to landline telephone services in 2009.<sup>228</sup> It is implicit in that finding that Ofcom considered that the line rental (i.e. access) prices of BT's SFV services in 2009 were at a sufficiently competitive level at that time, or at least that – if they were above the competitive level – they were expected to come down to the competitive level in future.<sup>229</sup> On this basis, my preferred benchmark is likely to be an upper bound on the true competitive price level.

291. Indeed, in the Provisional Conclusions in 2017, Ofcom took BT's profitability in 2009 as its starting point for calculating the magnitude of the price cut to SFV service charges which Ofcom was, at that stage, minded to impose.<sup>230</sup> In other words, it treated BT's 2009 prices as sufficiently competitive not to require

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<sup>228</sup> Ofcom's 2009 Review, (para. 1.2)

<sup>229</sup> For example, Ofcom, Fixed Narrowband Retail Services Market Review, Statement, September 2009 (paras. 5.80, 5.81), and Ofcom, Fixed Narrowband Retail Services Market Review, Consultation, March 2009, (para. 5.73-5.76, and 5.86-5.94)

<sup>230</sup> Provisional Conclusions, (para. 8.20)

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regulation. While Ofcom observed that the effect of the resulting price cut would be to “*largely reverse the price increases since 2009*”<sup>231</sup>, it went on to say that “[W]e recognise that the price cut may not reduce prices to the level BT which might charge **in a fully competitive market**”.<sup>232</sup> In other words, Ofcom also treated BT’s 2009 prices as a working upper bound on a competitive price even though those prices may have been above the competitive level.<sup>233</sup>

292. I have therefore treated BT’s prices for line rental in 2009 as the starting point for determining the competitive benchmark for the access component of BT SFV Services. As an upper bound on the true competitive price, it is a conservative basis for testing whether subsequent prices were excessive.

293. Indeed, as was seen in Figure 12, BT’s prices had been lower in 2008 than in 2009 (while still being above WLR cost). Given that price regulation had been removed in 2006,<sup>234</sup> it would be useful to analyse the evolution of prices leading up to 2009. To this end, I would need:

293.1. Full, monthly, price lists for 2008 and 2009 for the following BT offerings offered to **Voice Only Customers** – BT Standard Line Rental, BT Line Rental Plus and BT Line Rental Saver. The price lists should cover each month during the Claim Period.

293.2. Full, monthly, price lists for 2008 and 2009 for the following BT SFV access products offered to **Split Purchase Customers** – BT Standard Line Rental, BT Line Rental Plus and BT Line Rental Saver. The price lists should cover each month during the Claim Period.

### Adjusting this price to reflect cost changes

294. In a competitive market, prices would be expected to change in line with variable costs. I have therefore considered the available cost data to determine whether the 2009 price should be adjusted over time to reflect changes in material variable cost inputs for the access component of BT SFV Services. In particular, there is data available from BT<sup>235</sup> on the evolution of Wholesale Line Rental (WLR) prices, which is the largest single cost for an SFV service,

<sup>231</sup> Provisional Conclusions, (para. 6.19)

<sup>232</sup> Provisional Conclusions, (para. 6.19)

<sup>233</sup> Provisional Conclusions, (para. 8.30)

<sup>234</sup> Ofcom’s 2009 Review, (para. 3.7)

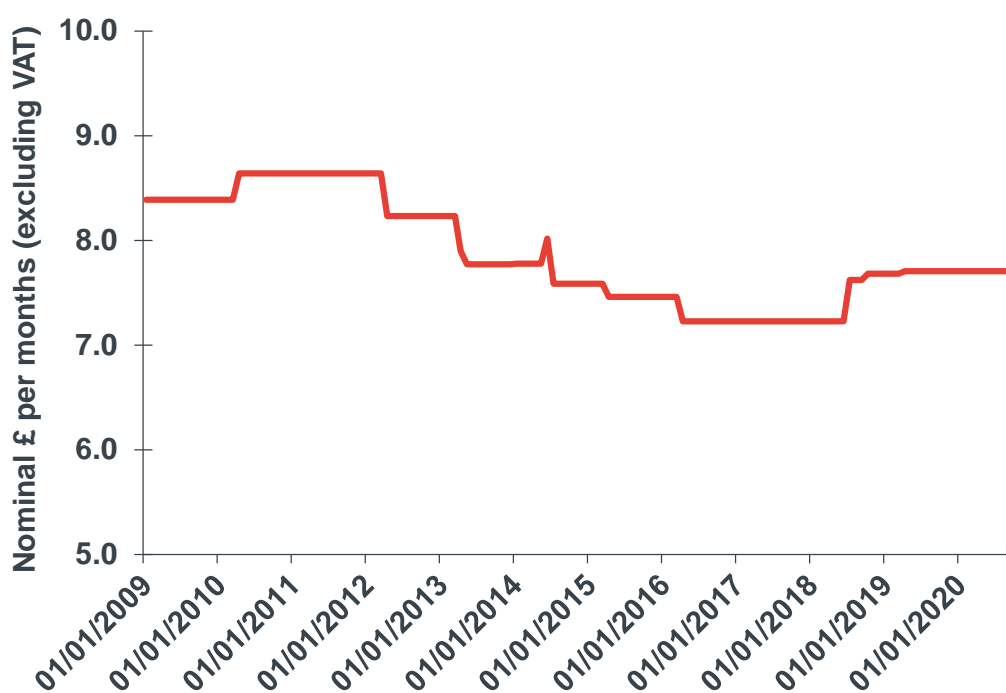
<sup>235</sup> Specifically from Openreach, the network division of BT. Sources set out in Annex A.

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accounting for two-thirds<sup>236</sup> of BT's price for the SFV access component in 2009.<sup>237</sup> WLR was the technology generally used to deliver SFV services in 2009, and was used by BT on an 'equivalence of inputs'<sup>238</sup> basis to deliver voice services throughout the period.<sup>239</sup>

295. Data on the evolution of WLR prices shows that they fell from 2010 to 2018, as shown in Figure 16 below (before increasing slightly). I would therefore expect the competitive price level also to have fallen over this period (before increasing slightly).

**Figure 16 Evolution of wholesale line rental (WLR) price over time**



Source: *Frontier Economics and Openreach data*

Note: 1) Price series presented in nominal terms. 2) The y-axis begins at £5 for presentational clarity.

296. I therefore adjust the 2009 price in each year to reflect these changes in input costs, in order to estimate a competitive benchmark price for the access component of SFV services which is reflective of costs at each point in time. This

<sup>236</sup> This can be seen in Figure 12 in Section 7.2.3

<sup>237</sup> If data becomes available on changes in other elements of BT's costs of supplying access, I would need to adjust my analysis to take that into account.

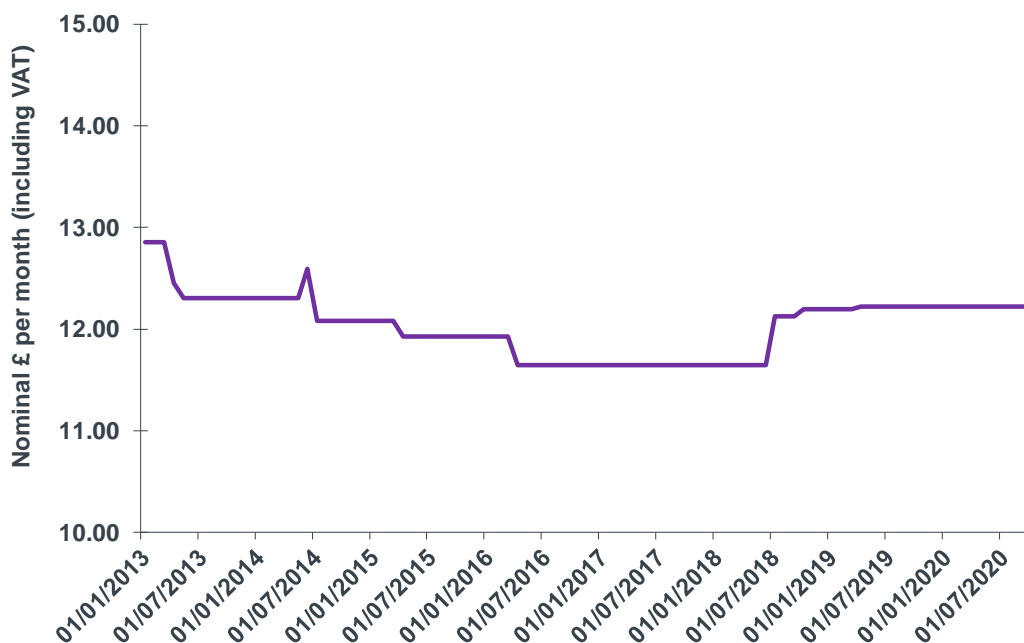
<sup>238</sup> This is a requirement on the network division of BT (Openreach) to provide the same products and services to all its customers (including its downstream arms, e.g. BT Wholesale and BT retail) on an equivalent basis, which means (subject to some limited exceptions) at the same prices, using the same processes and to the same timescales. <https://www.openreach.co.uk/org/home/aboutus/equivalence/equivalence.do>

<sup>239</sup> The price of Metallic Path Facility, used by some access seekers to deliver voice in conjunction with broadband services, has moved broadly in line with the price of WLR since 2009.

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is shown in Figure 17.<sup>240</sup> I present the price-series in nominal terms (i.e. not adjusting for inflation) in order to reflect the actual prices paid by BT SFV Service customers at each point in time.<sup>241</sup>

**Figure 17 Evolution of best available competitive benchmark over time**



Source: Frontier Economics, Ofcom data and Openreach data

Note: 1) Price series includes VAT as is presented in nominal terms. Detail on how this series was constructed is available in Annex A) The y-axis begins at £10 for presentational clarity.

297. The remaining costs of providing the access component of SFV services will include items such as customer care including fault clearance, billing and collection costs.<sup>242</sup> I do not have evidence on the evolution of these costs, but I note that each category will be small relative to the cost of WLR, given the share BT's total price accounted for by WLR. It therefore appears unlikely that changes in these cost inputs will materially affect my conclusions, but I will need to assess this when the relevant data becomes available.

<sup>240</sup> Detail on the adjustments I make, and how I estimate the competitive benchmarks more generally, is available in Annex A.

<sup>241</sup> Indeed I reflect all price series in nominal terms to reflect actual prices paid at any given point in time.

<sup>242</sup> I note that BT argued that an ASA ruling in 2016 would be expected to reduce prices. Ofcom considered and rejected this argument. "We have considered BT's argument that the ASA ruling will reduce incentives to raise line rental prices, and may lead to lower prices. The ASA announced its intention to introduce its new rules in May 2016 and implemented this in October 2016. After the ASA's announcement BT, Plusnet, TalkTalk, Post Office and Virgin Media each raised the price of line rental by approximately £1. Since implementation, none of the main providers has decreased its price, and Plusnet has increased its price.<sup>33</sup> We consider that the evidence to date does not demonstrate that that, as BT has suggested, the price of standalone fixed voice services would fall materially as a competitive response to the ASA ruling." (Statement, para. 3.29) I do not have any reason to disagree with Ofcom's view.



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298. To this end, the data I would need evidence on the non-WLR variable costs per line, on a robust and verifiable methodology, for provision of the following BT SFV access offerings:
- 298.1. Standard Line Rental;
  - 298.2. Line Rental Saver; and
  - 298.3. Line Rental Plus.
299. This data should be provided on a monthly basis for 2008 and 2009, and from 1 October 2015 to date.
300. I would also require the gross margin for these products in 2008 and 2009, which likely indicates (an upper bound on) the competitive level of gross margin. The data should be provided separately for Voice Only and Split Purchase Customers if the costs of provision to the two groups differ.
301. I request data for both 2008 and 2009 because, as set out in paragraph 293, it would be useful to analyse the trend in prices, cost and profits leading up to 2009.
302. Using this cost information, I will be able to create a time-series for the evolution of all costs relevant to the three offerings set out above.
303. I will then use this pricing, cost and profitability data to:
- 303.1. confirm if November 2009 is the right starting point for the competitive benchmark; and
  - 303.2. create a time-series for the competitive benchmark for each of the three access component offerings by adjusting the starting point to reflect changes in total cost. The methodology for doing so is the same as that set out above in paragraphs 294-296.

### 8.2.2 Alternative benchmarks

304. I have considered two further sets of prices as possible benchmarks for the competitive price of the access component of SFV services over the period.
- 304.1. **The 2009 price, unadjusted for costs.** The cost unadjusted price could in theory serve as a meaningful benchmark if there was reason to believe that the costs of unobserved elements (e.g. customer care, billing, etc.) had increased enough to offset the decline in WLR costs. However, I have no evidence to suggest this is the case. This will be confirmed upon access to the data set out in paragraphs 298 to 299 above as it will give me visibility of the quantum and evolution of non-WLR variable costs.

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304.2. **The price that BT agreed with Ofcom to be charged in the BT Commitments.** BT described the BT Commitments as follows: “*BT now voluntarily provides the commitments set out below and, in particular, provides the greatest possible price reduction for our true voice only customers **consistent with a competitive outcome***” (emphasis added).<sup>243</sup> The BT Commitments therefore provide an alternative estimate of the competitive price as of April 2018. However, the competitive benchmark would have changed in previous periods as input costs changed, so using the price in BT Commitments throughout the period would be less accurate than my preferred benchmark. I note that while BT states that this price is “the lowest price consistent with a competitive outcome”, this statement is not substantiated with further evidence. I consider that it is reasonable to assume that BT would not have committed to a discount which would have driven its price below the competitive level. I therefore consider the prices charged under the BT Commitments to represent, at best, an upper bound on the competitive price as of April 2018.

305. Whilst 2009 prices adjusted for cost increases are in my view the most compelling competitive benchmark, I have used the two sets of prices above as sensitivities in my analysis.<sup>244</sup>

306. The three benchmarks are shown in the figure below.

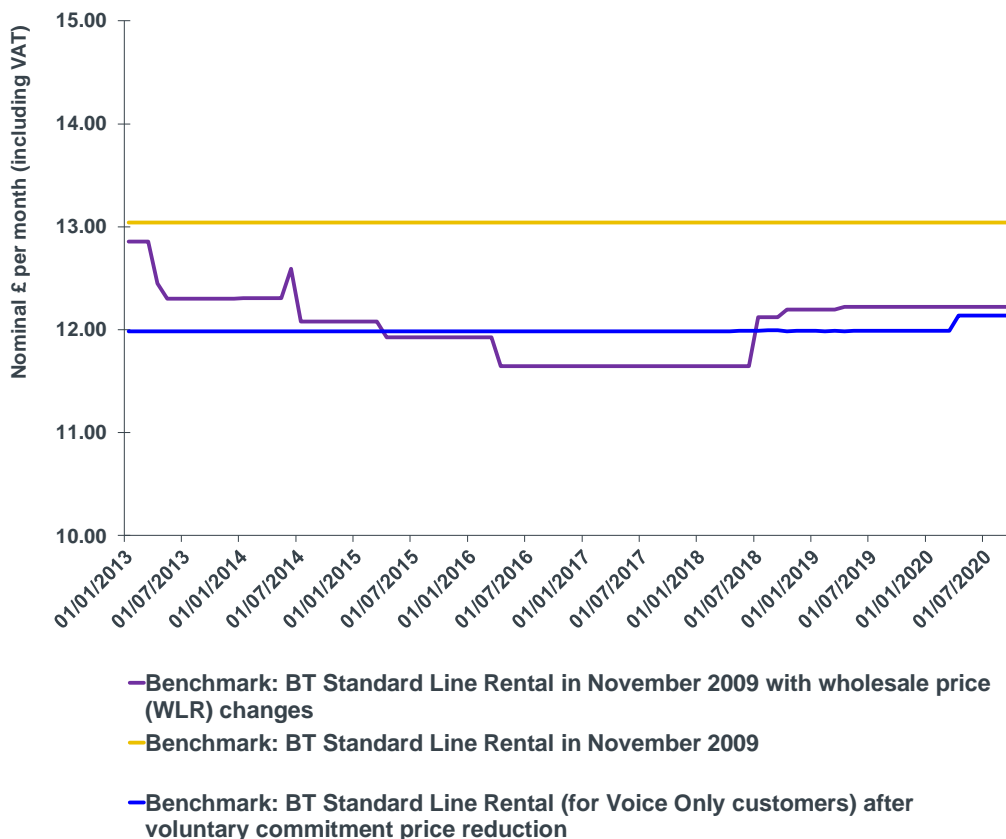
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<sup>243</sup> Statement, p.27, paragraph (B).

<sup>244</sup> I note that AG Wahl, in his Opinion in *Latvian Copyright Society*, identifies that “*in order to avoid (or, more correctly, to minimise) the risk of errors, competition authorities should strive to examine a case by combining several methods among those which are accepted by standard economic thinking and which appear suitable and available in the specific situation*”. (para. 43)

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Figure 18 Evolution of alternative competitive benchmarks over time



Source: Frontier Economics, Ofcom data and Openreach data

Note: 1) Price series includes VAT as is presented in nominal terms. 2) There is an increase in the BT Residential Line Rental (Voice-only) price in April 2020 as BT was allowed to adjust its prices upwards (but by no more than inflation). Changes to prices before that are an outcome of adjusting a real price series into a nominal one. Detail on how this series was constructed is available in Annex A) The y-axis begins at £10 for presentational clarity.

### 8.2.3 Benchmarks I consider less suitable for assessing the competitive line rental price

307. I have also considered whether the prices of certain other potentially comparable services could serve as reliable proxies for the competitive price level for the SFV access component over the period. However, I have rejected each for the reasons I give below.<sup>245</sup>

<sup>245</sup> AG Wahl, in his Opinion in *Latvian Copyright Society*, identifies that there are many potential benchmarks, and that one needs to consider the extent to which a comparison of price with the relevant benchmark is meaningful (paras. 18 and 19).

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### Home Phone Saver

308. Ofcom states in the Provisional Conclusions that “*BT uses its Home Phone Saver tariff as a retention tool where it may lose its customers to competitors. As such, this provides a market indication of the price cut BT is willing to offer commercially where it perceives the threat of competition*”.<sup>246</sup> I agree that Home Phone Saver is a commercial response to the threat of competition, in that it is a tariff offered to customers who threaten to switch.

309. In my view, however, this does not suggest that Home Phone Saver is set at the competitive level; rather, it merely indicates that Home Phone Saver is set at a more attractive level than the other SFV service options (Standard Line Rental, Line Rental Plus, and Line Rental Saver). That is because a customer that has contacted BT threatening to switch, or considering switching, still faces actual and/or perceived switching costs, and so may or may not in fact carry out their threat to switch away from BT. Knowing this, I would expect BT, as a profit-maximising firm, to offer a price that is lower than the current price which the customer faces (as an inducement to stay with BT) but not as low as the fully competitive price, given that there is a chance that the customer would in any event stay with BT, notwithstanding his or her threat to switch away.

310. Consequently, the Home Phone Saver package could itself be priced at an excessively high level compared to the competitive benchmark. But, at this stage, I do not have the data available to carry out an analysis of charges for Home Phone Saver.

311. I would observe that the exclusion of the Home Phone Saver service from the Proposed Class, at this stage, is in my view appropriate given (i) the absence of data available to me (ii) the fact that Home Phone Saver contains multiple additional calls services which may be difficult to control for in order to assess whether the access component is excessively priced and (iii) the fact that Home Phone Saver charges are to some extent discounted from the prices of other packages. I understand that this is a matter which could be revisited at a later stage following disclosure by BT of price, cost and gross profit margin data on the access and calls components of Home Phone Saver.

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<sup>246</sup> Provisional Conclusions (para. 8.29)

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### Dual Play Services

312. As set out in Section 5.3.1, Ofcom considered that while customers purchasing their landline telephone services in a bundle with other non-voice services, such as broadband, (i.e. Dual Play customers) were getting a good deal,<sup>247</sup> customers buying an SFV service were not benefiting from competition in the same way.<sup>248</sup> Indeed, Dual Play is a growing segment of the telecommunications sector, with an increasing share of consumers opting to buy a Dual Play bundle.<sup>249</sup> This would suggest that more providers are competing to win over this group of customers. Finally, while Ofcom does not publish market shares for just Dual Play, broadband market shares (the majority of which will relate to bundles<sup>250</sup>) show that the market shares are split far more evenly among the providers than within the SFV market. This suggests greater competition in this market than in the markets for SFV services for Split Purchase Customers and Voice Only Customers.

**Figure 19 Broadband market shares**

Year	1. BT	2. Sky	3. Virgin Media	4. TalkTalk	5. EE	6. Others	Total
2013	31.25	21.19	20.00	15.72	3.36	8.48	100.00
2014	32.02	22.50	19.64	14.58	3.63	7.64	100.00
2015	32.42	23.39	19.16	12.95	3.87	8.21	100.00
2016	36.45	23.36	19.42	11.67	0.00	9.11	100.00
2017	35.86	22.69	19.71	11.56	0.00	10.18	100.00
2018	34.59	22.53	19.75	11.28	0.00	11.84	100.00

Source: "Fixed broadband connections by ISP (%)", Ofcom Communications Market Report 2019<sup>251</sup>

Note: BT includes Plusnet, and from 2016 onwards, EE.

313. However, Dual Play bundles would not in my view serve as a useful benchmark for the price of the line rental aspect of SFV services given that they involve an additional product – e.g. broadband – with additional costs. One would need to strip out those additional costs from the assessment, plus control for the different product features. Given that I have identified more closely comparable

<sup>247</sup> Provisional Conclusions, (para. 1.2-1.3)

<sup>248</sup> Provisional Conclusions, (para. 1.5)

<sup>249</sup> The share of Dual Play bundles (as defined by landline and broadband) in total take-up of telecommunications services has increased from 17% in 2009 to 31% in 2018. See Figure 1.5, p.13 in [https://www.ofcom.org.uk/data/assets/pdf\\_file/0022/117256/CMR-2018-narrative-report.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0022/117256/CMR-2018-narrative-report.pdf)

<sup>250</sup> c.80% of customers bought their telecommunications services as part of a bundle, and most bundles include broadband. This can be seen in Figure 1.5 in [https://www.ofcom.org.uk/data/assets/pdf\\_file/0022/117256/CMR-2018-narrative-report.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0022/117256/CMR-2018-narrative-report.pdf)

<sup>251</sup> Available at <https://www.ofcom.org.uk/research-and-data/multi-sector-research/cmr/interactive-data>

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benchmarks, there is no reason to use what would be a more remote and estimated proxy.

### Prices in other geographic areas

314. I do not consider that prices in other geographic markets are robust benchmarks for the competitive price in the UK (excluding Hull) due to differences in the size, structure and costs of those networks, and the impact of regulation on the level of prices in other geographic markets. For instance, the network in the Hull Area is on a substantially smaller scale than that of BT's "rest of UK" network, and so its costs of operation will be very different. International comparisons would introduce further differences of regulation, customer behaviour and costs. These differences would materially distort any comparisons and would likely be impossible to control for.

### Cost-plus approaches

315. In principle, one could develop a competitive benchmark by building a bottom-up cost-plus model, which involves reflecting all costs of production and an appropriate profit margin. However, my approach of relying on the 2009 benchmark and adjusting for subsequent cost changes is in substance a cost-plus approach. This is because in 2009, assuming that the market was then competitive, BT would have set its price so as to account for relevant costs and include an appropriate margin reflecting the relevant allocation of common costs and a return on capital employed.

316. I have indicated that I would seek data on variable cost changes in items other than WLR (although, as set out above, I think it is likely that these costs – collectively – are much less material than the WLR cost). I am also not aware of any reason to think that the appropriate allocation of common costs would have changed over time, or that the level of capital employed or the appropriate return would have changed. This suggests that an approach of starting from the 2009 price, and adjusting for subsequent observed cost changes, is reasonable.

### Line rental (i.e. access) prices of other providers of SFV services

317. I have considered whether line rental prices charged by other providers of SFV services were set at the competitive level.

318. As I explained in Section 7.2.3, Ofcom presented the evolution of the prices of line rental (i.e. the access component of SFV services) set by the different

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major providers in the market over a ten-year period.<sup>252</sup> The evidence shows that in the Claim Period, BT acted as price leader, making price changes first, with rivals following in order to maintain price differentials at broadly the same level. If so, rivals are not setting prices at the competitive level, but rather are setting these above the competitive level by ‘sheltering under BT’s pricing umbrella’.<sup>253</sup>

319. Therefore, I do not consider it appropriate to treat competitors’ prices of the access component of SFV services as a relevant benchmark. Indeed, as was seen in Figure 12, the prices of competitors were also rising while the key cost input (WLR) was falling, which is inconsistent with the view that these prices were set at the competitive level.

### Profitability of other providers

320. In the Provisional Conclusions, Ofcom explored the Return on Sales made by other firms.<sup>254</sup> I do not think that this is a sensible benchmark from a theoretical perspective. Return on Sales is not a helpful measure when one is considering different firms at different scales and where fixed and/or common costs are relevant. Moreover, if rivals were themselves not setting prices at the competitive level – as the assessment of the “leader-follower” patterns of price would suggest<sup>255</sup> – then any returns would themselves be distorted from the perspective of trying to estimate a competitive price benchmark.

321. From a practical perspective, such an analysis would also require data from firms other than BT, which is not available to me. I note that Ofcom identified that for some other providers, data was only available at a whole firm level<sup>256</sup>, and so would include the returns made on Dual Play and other multi-play packages, even if this data were available.

322. Ofcom also assessed the profitability of a marginal subscriber.<sup>257</sup> However, this is not a competitive benchmark for the SFV access component. It is a tool for assessing how effective Ofcom’s proposed demand-side remedies would

<sup>252</sup> Ofcom, Evidence Supporting the Statement, (Figure 1.24, p.19)

<sup>253</sup> As a general matter., using the prices of rivals as a competitive benchmark would suffer from a problem similar to the Cellophane Fallacy. If BT is raising prices above the competitive level, one would expect rivals also to increase their prices above that level, and so it would be unsafe to conclude the BT’s prices were at the competitive level because they were at a similar level to those of rivals. This again suggests that one should look for alternative benchmarks such as those I use.

<sup>254</sup> Provisional Conclusions, (para 8.24-8.25)

<sup>255</sup> See para. 228 et seq. above.

<sup>256</sup> Provisional Conclusions, (para. 8.25)

<sup>257</sup> Provisional Conclusions, (paras 8.26-8.28)

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need to be in order that they provide an incentive for rivals to seek to acquire customers after price cuts of different levels by BT.<sup>258</sup> As above, from a practical perspective one would also require data from firms other than BT, which is not available to me or to BT.

### 8.3 Comparison of benchmarks with the price of the access component of BT SFV Services

323. In this section, I assess whether the prices for the access component of SFV services are excessive. To this end, I compare the prices of the relevant BT options for the access component of SFV services, as set out in Section 5.1.3 – Standard Line Rental, Line Rental Plus, and Line Rental Saver – with my proposed competitive benchmark and the two sensitivity benchmarks.<sup>259</sup> I then assess whether the prices of these access components are significantly and persistently above the competitive level.

324. I note that there are two separate time periods for the analysis.

324.1. As these components of BT SFV Services were available to BT Voice Only and BT Split Purchase Customers on identical terms until 1 April 2018, my analysis of whether prices have been excessive applies equally to both Proposed Sub-classes prior to 1 April 2018.

324.2. From 1 April 2018, I only consider prices for BT Split Purchase Customers as Voice Only Customers at that stage benefited from the Commitments. As Ofcom stated “[w]e consider that BT’s voluntary proposal addresses our concerns over the prices offered to voice-only customers. It brings line rental prices back down to levels last seen in 2009 in real terms”.<sup>260</sup>

#### BT’s Standard Line Rental

325. I have compared the price<sup>261</sup> of BT’s Standard Line Rental product against the various competitive benchmarks in Figure 20 below. This demonstrates (for data going back to 2013) that there is a material gap between each benchmark and the retail price (the rising red line). Moreover, this material gap has been

<sup>258</sup> Provisional Conclusions, (para. 8.28)

<sup>259</sup> I exclude the Excluded Services (Home Phone Saver and BT Basic) from the analysis.

<sup>260</sup> Statement, (para. 1.20)

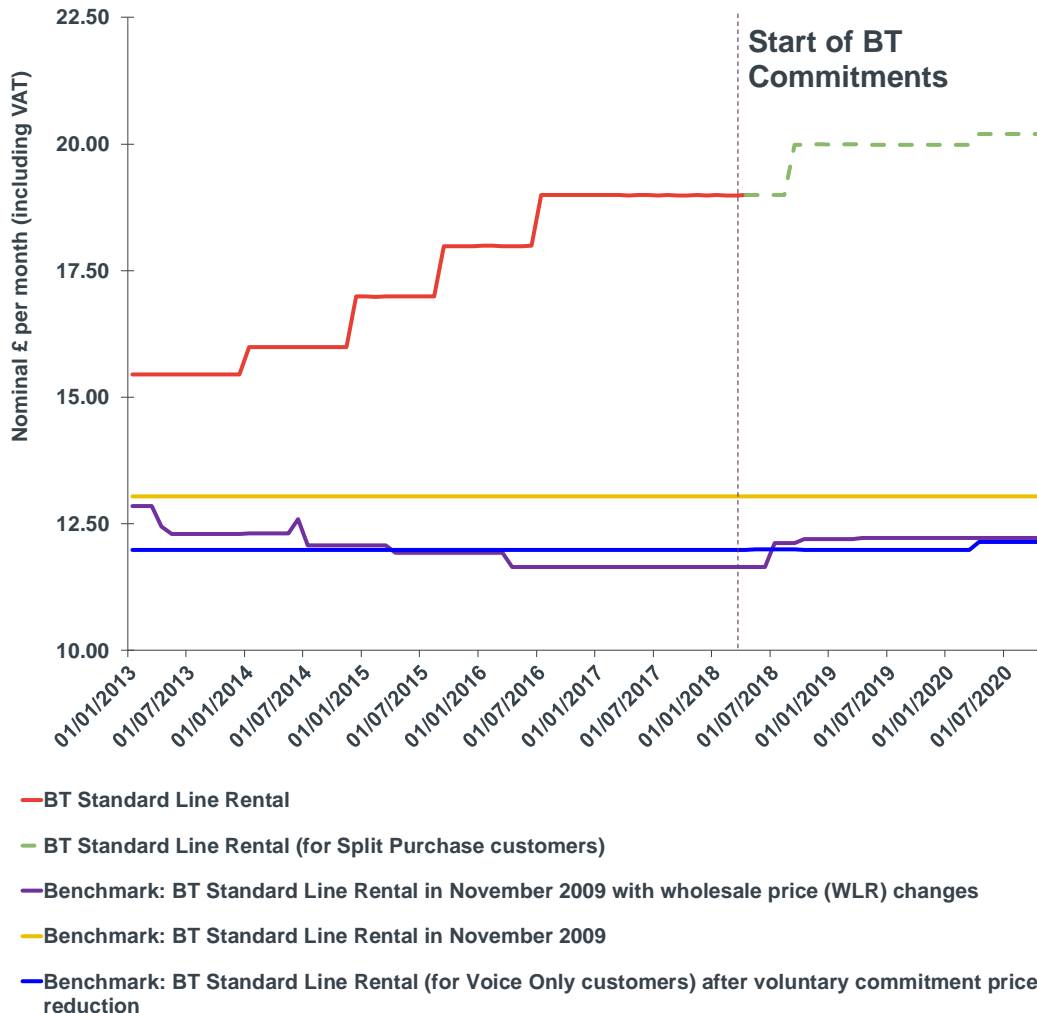
<sup>261</sup> Annex A provides more detail on how I have estimated the time series for the price of this product.



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present throughout the Claim Period and has widened consistently throughout the Claim Period.

**Figure 20 Analysis of BT Standard Line Rental prices against competitive benchmarks**



Source: Frontier Economics and Ofcom data.

Note: 1) Price series include VAT and are presented in nominal terms. Detail on how the price series and competitive benchmark series were constructed is available in Annex A. 2) The y-axis begins at £10 for presentational clarity.

326. Whether I use my preferred benchmark or either of the two sensitivities, my preliminary conclusion is that BT's prices for the access component of BT SFV Services (namely BT Standard Line Rental in this scenario) have been significantly and persistently above the competitive level. Using my preferred benchmark, in percentage terms, the price has varied between **51%** above the competitive level in October 2015 for both BT Voice Only customers and BT Split Purchase Customers and **65%** above the competitive level in latest available period, August 2020, for BT Split Purchase Customers. Using my sensitivity

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benchmarks, in percentage terms, the price has varied between **38%** and **50%** above the competitive level in October 2015 for both BT Voice Only customers and BT Split Purchase Customers and **55%** and **66%** above the competitive level in latest available period, August 2020, for BT Split Purchase Customers. This is shown in Figure 21.

**Figure 21 Percentage difference between price and relevant benchmarks, preferred benchmark in bold**

Benchmark	October 2015	April 2018	August 2020
<b>BT Standard Line Rental in November 2009 with wholesale (WLR) changes</b>	<b>51%</b>	<b>63%</b>	<b>65%</b>
BT Standard Line Rental in November 2009	38%	46%	55%
BT Standard Line Rental for Voice Only Customers after voluntary commitment price reduction	50%	58%	66%

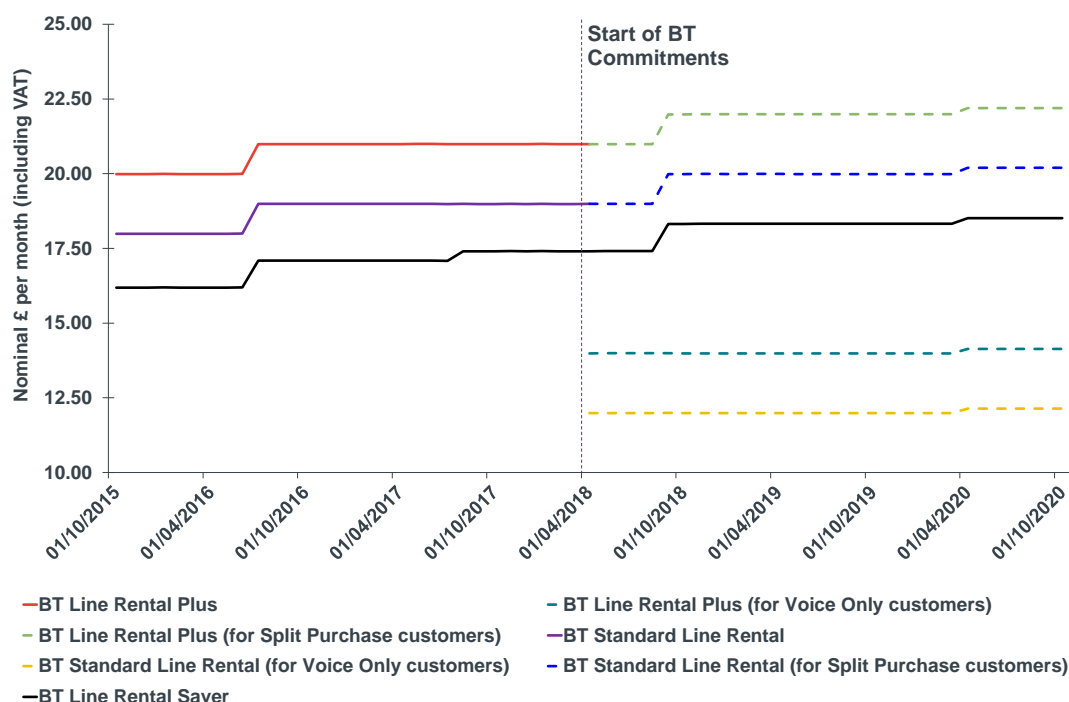
Source: Frontier Economics

### BT's Line Rental Saver and Line Rental Plus

327. As I show in Section 5.1.3 above and replicated in Figure 22 below for ease of reference, the prices for the three access (i.e. line rental) components for BT's SFV services are similar, with Line Rental Plus being £2 more expensive per month on average than Standard Line Rental, and Line Rental Saver being around £1.54 - £1.90 cheaper per month than Standard Line Rental.

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**Figure 22 Evolution of BT SFV access component prices (nominal terms)**



Source: Frontier Economics, Ofcom data and BT Consumer Price Guide data, prices presented in nominal terms, estimated based on a combination of a price index and real prices.

Notes: The y-axis begins at £10 for presentational clarity. 1) Prices are presented in nominal terms and include VAT. 2) It was not possible to calculate a reduced price paid by Line Rental Saver customers after 1 April 2018 as the discount they received would have depended on when they first took Line Rental Saver. In any case, Line Rental Saver is no longer available to Voice Only Customers. 3) The vertical dotted line represents the introduction of the BT Commitments on 1 April 2018. 4) Until 1 August 2017 (note: this is an estimate and is explained in Annex A), the discounted Line Rental Saver price represented a free month in each year versus the Standard Line Rental price, i.e. 11 months for the price of 12 (a c.8.3% discount). Thereafter, customers instead received a reduction of 10% relative to the Standard Line Rental price.

328. I do not have cost information for each individual product. I therefore cannot assess at this stage if adjustments need to be made to the competitive benchmark for these products. However, I do consider that the price differences are likely to reflect, at least in part, differences in the cost of provision:

328.1. Line Rental Plus, which is more expensive than Standard Line Rental, includes additional features such as “Call Barring”, “Choose to Refuse”, and “Helpful bill alerts” which could cost more to provide. It also offers the option of a paper bill or e-bill, where a paper bill would be more costly to provide due to the costs of printing and postage.<sup>262</sup>

328.2. Line Rental Saver, which is cheaper than Standard Line Rental, offers only e-bills which I expect to be less costly for BT to provide. Furthermore, this product must be paid on an annual basis and by credit or

<sup>262</sup> For example, see page 4/134 of BT’s October 2016 Price Guide - <https://www.bt.com/mobile/pdf/bt-consumer-price-guide-15.pdf>

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debit card, which further reduces costs. Annual payments reduce the risk of bad debt, while payments by credit/debit card could reduce transaction and administrative costs associated with direct debits.<sup>263</sup>

329. Thus, while I am currently unable to refine my preferred benchmarks for these alternative products, I consider it reasonable at this stage to assume that their prices were excessive to a similar degree (or equivalently that the differences in the prices of these products reflect the differences in the costs of provision). The fact that the £7 monthly price reduction in the BT Commitments was applied on a broadly equivalent basis to all three options for the access component to BT SFV Services adds further support to this preliminary conclusion.<sup>264</sup>

330. I note that I will need to update this analysis with better data post-certification. To do so, I would need the information on non-WLR costs for each of the three products (Standard Line Rental, Line Rental Plus, and Line Rental Saver) set out in paragraph 298 – 302 above. These costs, taken together with the November 2009 list prices of the three access offerings (as requested in paragraph 63) and the WLR costs (which I have access to already), will allow me to construct more accurate competitive benchmarks individually for each of the three relevant BT access offerings (as set out in paragraph 303).

331. Once I have the three competitive benchmarks, I will be able to assess the degree to which the actual prices for these options were above their individual competitive benchmarks, using the same methodology I have set out for Standard Line Rental in paragraphs 325 - 326.

### 8.3.1 Assessment of whether these prices were excessive

332. As set out in Section 8.1 above, I understand that the test for excessive pricing asks whether the relevant price has been “significantly” and “persistently” above the competitive benchmark.

<sup>263</sup> For example, see page 4/134 of BT’s October 2016 Price Guide - <https://www.bt.com/mobile/pdf/bt-consumer-price-guide-15.pdf>

<sup>264</sup> Statement (Annex A1, BT’s voluntary proposal)

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### Persistency

333. I consider that, for each relevant price, the gap between the price and the relevant competitive benchmark has been persistent because it has been present throughout the entire Claim Period.

### Significance

334. I am instructed that no objective benchmark or ‘bright line’ test has been identified in the case law on excessive pricing for determining whether a price is significantly above the level of the relevant competitive benchmark.<sup>265</sup> This is, in my view, consistent with the correct approach that the question of whether a particular price is excessive should be considered against the specific facts at issue.<sup>266</sup>

335. I draw the preliminary conclusion that BT’s SFV access component prices throughout the Claim Period are significantly above the competitive level, on the basis of all the evidence summarised in this Report. In particular, I note (i) the substantial difference between BT’s SFV access component prices and my preferred competitive benchmark of between 51% and 65% as set out in Figure 21 above; (ii) similar differences being present between BT’s SFV access component price and my alternative benchmarks (again set out in Figure 21 above) and (iii) Ofcom’s findings about the high level of BT’s SFV service prices, Ofcom’s proposal for a price control for SFV services to Voice Only and Split Purchase Customers, and Ofcom’s acceptance of the BT Commitments, as summarised in Section 5 of this Report.

### Excessive pricing

336. Given my conclusions on persistency and significance, my preliminary conclusion is that the BT’s prices for the access component of SFV services sold to Voice Only and Split Purchase Customers were excessive, in that they were significantly and persistently above the competitive benchmark.

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<sup>265</sup> AG Wahl, in his Opinion in *Latvian Copyright Society*, explains this as follows: “the price which that undertaking would hypothetically have charged had there been effective competition in the market” (paragraph 17), and identifies that “Existing case-law of the Court does not give very precise guidance on this issue. Nor can clear patterns be found in the practice of national authorities or in economic literature” (para. 110).

<sup>266</sup> AG Wahl, Opinion, *Latvian Copyright Society*, (para. 37)

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### Duration

337. The duration for which the price for the access component of BT SFV Services were excessive differs for BT Voice Only and BT Split Purchase Customers. This is because the BT Commitments applied only to BT Voice Only Customers from 1 April 2018.<sup>267</sup> Thus, BT Split Purchase Customers continued to face excessive prices after the introduction of the BT Commitments, up to the present day.

338. I therefore conclude that, in terms of the duration for which prices for BT SFV Services were excessive:

338.1. line rental prices (for Standard Line Rental, Line Rental Plus, and Line Rental Saver) for Voice Only Customers were excessive from at least 1 October 2015 to 31 March 2018 (inclusive); and

338.2. line rental prices (for Standard Line Rental, Line Rental Plus, and Line Rental Saver) for Split Purchase Customers were excessive from at least 1 October 2015 to the present day.

## 8.4 Whether there is an offsetting effect from the prices for the calls component of BT SFV Services

339. As I have defined a single market for SFV services including both the access and calls components, I must consider whether there is evidence that the prices for the calls component of BT SFV Services were below the competitive level to such a degree as to sufficiently offset the higher than-competitive prices for the access component of BT SFV Services.

### 8.4.1 No evidence that BT's call prices for BT SFV customers were below the competitive level

340. There is no evidence that the prices for the calls component of BT SFV Services were below the competitive level. Indeed, BT's average call prices (across all its customers) have increased since 2009, while average calls prices for other firms (across all their customers) have decreased.

341. While I do not have information on the prices and volumes for the calls component of BT SFV Services, I am able to review revenue and volume data

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<sup>267</sup> Statement, (para. 1.16)

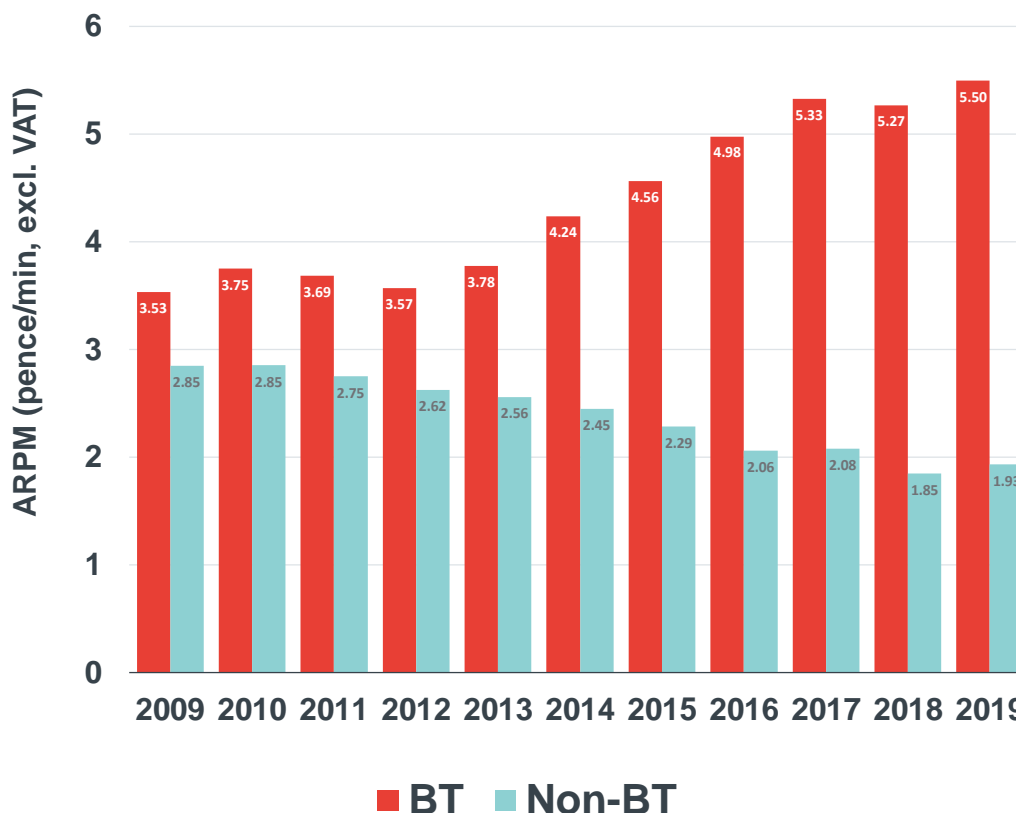
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on BT and its rivals' *total* calls. These data will include revenues and volumes generated from calls on non-SFV services, e.g. calls by Dual Play customers.

342. These data are reported in Figure 13 above (and replicated below in Figure 23 for convenience). Figure 23 shows the Average Revenue Per Minute (ARPM), a proxy for average unit call prices paid by customers, split by BT and non-BT customers, over the period 2009 – 2019.

343. As above, I note that Ofcom found that BT did not have SMP in 2009, suggesting that BT's call prices in 2009 were (an upper bound on) a competitive benchmark. The figure below suggests that BT's call prices have, on average, increased since 2009 while prices charged by BT's competitors have fallen.

**Figure 23 BT vs. non-BT calls ARPMS, 2009 – 2019**



Source: *Frontier Economics and Ofcom data.*

Note: *ARPMS do not control for differences in the distribution of call types made by different customers. However, I have checked using information on the distribution of call types between BT and its competitors and found that the differences in ARPMS cannot be explained by differences between the calling patterns of BT and non-BT customers. This analysis is set out in Annex B.*

344. My preliminary conclusion is that there is no evidence to suggest that BT's prices for the calls component of SFV services are below the competitive level. Consequently, there is no evidence of any offsetting effect that would indicate

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that the excessive charges that I observe on the access component of SFV services is an overestimate of their true level.<sup>268</sup>

345. I will subsequently need to confirm this finding for the calls component of BT's SFV services with more detailed data on BT SFV revenues, calls volumes and profitability for Voice Only and Split Purchase Customers. To this end, I will need the information set out below.

345.1. Data on revenues and volumes of calls made by BT Voice Only Customers of Standard Line Rental, Line Rental Saver and Line Rental Plus for each year between 2015 to 2018.

345.2. Data on revenues and volumes of calls made by BT Split Purchase Customers of Standard Line Rental, Line Rental Saver and Line Rental Plus for each year between 2015 to 2020.

345.3. BT's annual gross margins from 2015 to 2018 for:

345.3.1. SFV access offerings sold to Voice Only Customers, in particular:

345.3.1.1. Standard Line Rental;

345.3.1.2. Line Rental Saver; and

345.3.1.3. Line Rental Plus

345.3.2. the calls components of SFV services for the Voice Only Customers of the above offerings.

345.4. BT's annual gross margins from 2015 to 2020 for:

345.4.1. SFV access offerings sold to Split Purchase Customers, in particular:

345.4.1.1. Standard Line Rental;

345.4.1.2. Line Rental Saver; and

345.4.1.3. Line Rental Plus

345.4.2. the calls components of SFV services for the Split Purchase Customers of the above offerings.

346. This data will allow me to assess the trends in ARPMs for SFV calls as well as profitability over time and thereby assess if there is evidence of an offsetting

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<sup>268</sup> I am not able, based on the existing material, to analyse whether calls were also excessively priced; I would need access to further information to form my own view on the matter. The data that I request in paragraph 345.1 to 345.4 should allow me to make such an assessment, although the primary purpose of this data is to check my preliminary conclusion that there is no offsetting effect of calls prices being below the competitive level.



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effect from call prices. The methodology for doing so is the same for Voice Only and Split Purchase Customers.

### 8.4.2 There is no evidence of “competitive rebalancing”

347. Another possibility that could explain the increase in the prices for the access component of BT SFV Services is that it is the result of “competitive rebalancing” – a reallocation of the mark-ups on access and calls components of BT SFV Services. Ofcom briefly considered whether the increase in access revenues appeared to offset a reduction in calls revenues. It stated that *“we do not consider that it is likely that the increase in line rental can be attributed purely to a rebalancing of revenue between access and calls (even if this may be a contributing factor).”*<sup>269</sup>

348. Whilst Ofcom concluded that rebalancing was not a full explanation of the increase in prices for the access component of BT SFV Services, it did not assess whether BT faced a breakeven constraint that meant that it had no choice but to increase the access price in the face of lower calls revenues.<sup>270</sup> As a result, I investigate this issue further myself.

349. As I set out below, I do not find evidence that BT’s prices for the access component of BT SFV Services reflect “competitive rebalancing” between calls and access. This is for two reasons:

349.1. First, competitive rebalancing only occurs in a situation where a firm faces a break-even constraint (and so cannot absorb any reduction in profits in one part of its business without a commensurate increase in profits in another part of its business). I have not seen any evidence to suggest that BT has faced such a constraint at any time during the Claim Period.

349.2. Second, the BT Commitments contained a substantial price reduction for the access component of BT’s SFV services for BT Voice Only Customers, with no corresponding increase in calls prices, and an additional commitment not to increase calls prices at a rate above CPI in subsequent years. This is inconsistent with the view that there was any “competitive rebalancing”, because, if a break-even constraint did exist, BT’s own

<sup>269</sup> Provisional Conclusions, (para. 4.59)

<sup>270</sup> In other words, it is not clear why Ofcom felt that BT needed to make the same amount of profit on all SFV services at all times throughout the period.

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undertaking would have forced its revenues below its break-even level. In my view, this provides a strong basis for disregarding competitive rebalancing as a reason for BT’s price increases in respect of the access component of SFV.

350. I expand on these points below.

### “Competitive rebalancing” requires a breakeven constraint

351. A firm with fixed and common costs across services will need to recover those fixed and common costs through mark-ups above marginal cost on the services that it offers. The theory of “Ramsey pricing” shows that a monopolist facing a breakeven constraint will mark up its services in inverse proportion to the elasticity of demand on each services, so that services with more elastic demand have lower mark-ups.<sup>271</sup>

352. This result extends to competitive markets. Firms in such markets facing fixed and common costs will also be expected to mark-up according to inverse elasticities across products. If a firm is in a competitive market, it faces an effective breakeven constraint, as a key feature of a competitive market is that firms make zero economic profits.

353. Where a breakeven constraint exists, it follows that if there is a reduction in the price from one service as a result of the introduction of regulatory constraints, then this must be accompanied by an increase in prices on another service. This is because the profits of firms would otherwise fall below the breakeven level. In a competitive market, this would lead to sufficient exit to allow the remaining firms in the market to increase mark-ups and therefore increase their prices on other services, and so return to a breakeven (i.e. competitive) level.<sup>272</sup>

354. However, where a breakeven constraint does not exist – for instance, where a firm is making excess profits – there is no automatic mechanism whereby reductions in the prices on one service would lead to increases in price on the other services.

355. For instance, suppose that a monopolist selling two unrelated products initially sets monopoly prices on each product (and makes excess profits on each). Following entry on one product, the price of that product falls to the

<sup>271</sup> See <http://regulationbodyofknowledge.org/tariff-design/economics-of-tariff-design/ramsey-pricing/>

<sup>272</sup> In the monopoly context, the monopolist facing a breakeven constraint would go out of business if it were to face such a regulatory constraint on one service. This would likely provoke discussions with the relevant regulator about the sustainability.

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competitive level. This does not give rise to any “competitive rebalancing”: the monopolist continues to make excess profits on the other products, and so does not face any breakeven constraint, even though its overall profits have fallen.

356. For the increase in prices for the access component of BT SFV Services to reflect “competitive rebalancing”, therefore, it would need to be the case that BT had no choice but to increase these prices to offset reduced calls profits as otherwise it would have had to exit the markets for SFV services.

### No evidence of competitive rebalancing in the BT Commitments

357. The BT Commitments themselves provide compelling evidence that BT did not face a breakeven constraint. As described by Ofcom:

*“On 24 October 2017 BT put forward a voluntary proposal seeking to address some of the concerns identified in the February Consultation. BT’s proposal involves the following commitments for a three-year period in respect of its voice-only customers:*

*A **line rental price reduction of £7 per month** (inclusive of VAT) effective from April 2018; **[and]***

*Raising prices of calls and line rental **by no more than inflation (CPI)** each year”; [emphasis added]<sup>273</sup>*

358. The BT Commitments show that BT agreed to simultaneously reduce the price of line rental products by a substantial amount, and not to increase the price of calls products by more than CPI in future years (and I am not aware of any contemporaneous and substantial increase in calls prices to SFV customers).<sup>274</sup> Had BT faced a breakeven constraint, it would not have been able to agree to these terms, as it would have had to exit the market (i.e. cease offering SFV services). In my view, this provides a strong basis for disregarding competitive rebalancing as a reason for BT’s price increases in respect of the access component of SFV.

### Assessment of conditions discussed in *Latvian Copyright Society*

359. As mentioned in paragraph 285 above, AG Wahl’s Opinion in *Latvian Copyright Society* identifies that where there is a free market with no barriers to entry, high prices should normally attract new entrants and so the market will self-correct, and in his view, such situations should not result in excessive pricing

<sup>273</sup> Statement, (para. 1.16)

<sup>274</sup> The data requested at paragraph 345 above will allow me to confirm this understanding.

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antitrust cases. Consequently, attention should concentrate on markets with such barriers, particularly in regulated sectors, and where any existing sectoral regulator has not acted to intervene.

360. In this case, telecoms is a regulated sector, as set out in Section 5, and I have shown above in Section 7.2.2 and Section 7.3.2 that rival providers of SFV services face substantial barriers to entry and expansion. While Ofcom did investigate whether BT's SFV prices were excessive, and proposed that price controls be introduced, its intervention was not complete. For instance, in respect of Voice Only Customers, Ofcom has accepted forward-looking commitments (the BT Commitments), but has not required BT to compensate these customers for any historic overcharge. Similarly, in respect of Split Purchase Customers, Ofcom has not taken any action on either a backward-looking or a forward-looking basis. The 2020 Review does not set out any change in Ofcom's position.

### 8.4.3 Conclusion – no evidence of any offsetting effect from calls prices

361. My preliminary conclusion from the evidence above that there is no evidence that there is an offsetting effect from calls prices being below the competitive level, or being a result of competitive rebalancing. However, I will need to revisit my conclusion on calls prices when better data is available. I have set out the data I will need and the methodology I would use at the relevant points in this section.

## 8.5 Overall conclusion

362. My preliminary conclusion is that BT's prices for the access component of BT SFV Services (i.e. line rental) to Voice Only and Split Purchase Customers were excessive. For Voice Only Customers, these prices were excessive from the start of the Claim Period until 1 April 2018. For Split Purchase Customers, these prices were excessive throughout the Claim Period to the present day.

363. I have explored whether the excessive prices for the access component of BT SFV Services were offset by prices for the calls component of BT SFV Services that were below the competitive level. My preliminary conclusion is that there is no evidence that this is the case, and if anything, that the prices for the calls component may themselves have been excessive.

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364. I have also explored whether the increase in prices for the access component of BT SFV Services represented competitive rebalancing. My preliminary conclusion is that this is not the case, as otherwise BT would not have been expected to agree to the BT Commitments.

## 9 ASSESSMENT OF QUANTUM

365. In this section I assess the aggregate damage suffered by the Class. I first set out the methodology I will employ. At present, I do not have accurate data on all elements of that methodology, and so elements of my current assessment are based on best estimates. I set out the data requirements for a more accurate assessment where relevant.
366. I then employ this methodology to provide an interim assessment of damage for the purposes of certification. This assessment is based on the information to which I currently have access. For both the methodology and my interim assessment, I address the excess pricing of the access component of BT's SFV services, specifically relating to the Standard Line Rental, Line Rental Saver and Line Rental Plus offerings which are the line rental products within the scope of the Proposed Class.
367. Since the damage in this case is suffered by final consumers (with one limited exception which I discuss in Section 9.1.1 below), the issue of pass-on is not, for the most part, relevant.

### 9.1 Methodology for estimating the aggregate damage suffered by the Class

368. I estimate aggregate damages for the Class by first estimating the damage for the two Proposed Sub-classes. As I set out below, the methodology for doing so is the same across both Proposed Sub-classes – only the period of infringement differs.
369. I intend to estimate the quantum of damage for BT Voice Only and BT Split Purchase Sub-classes for each line rental offering. The damage for each Proposed Sub-class can be quantified accordingly by using three main constituents:
- 369.1. First, the duration of the period over which damages arise:
- 369.1.1. For BT Voice Only Customers, the Claim Period runs from **01/10/2015 up till 31/03/2018** when the BT Commitments applied.
- 369.1.2. For BT Split Purchase Customers, the Claim Period runs from **01/10/2015** to present day (and ongoing), as the BT Commitments did not cover these customers.

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- 369.2. Second, the number of Voice Only and Split Purchase Customers purchasing each access component offering for BT SFV Services (namely BT's Standard Line Rental, Line Rental Saver and Line Rental Plus) at a reasonable periodicity. I do not have the full data currently (I employ estimates and assumptions for my interim calculations) and set out the precise data I will need below.
- 369.3. Third, the level of excessive price/overcharge in each month of the Claim Period, by comparing the price of each line rental offering with its competitive benchmark. I do not have the full data currently (I employ estimates and assumptions for my interim calculations) and I have set out the information I will need and methodology I will use in Section 8.3.
370. I undertake these calculations on a monthly basis. This is because both retail and wholesale prices change periodically, and estimating damages on a monthly basis means that prices are likely to be broadly accurate at any given time.
371. To estimate the damage for the Voice Only Sub-class using these constituents, I would carry out the following calculations.
- 371.1. For each Line Rental offering, multiply the level of overcharge in each month with the number of Voice Only Customers in each month from October 2015 to March 2018. This provides the total overcharge for Voice Only Customers taking the particular Line Rental offering in each month.
- 371.2. Add these monthly estimates of overcharge for each Line Rental Offering across the Claim Period. This provides the total overcharge for Voice Only Customers taking each Line Rental offering in the Claim Period.
- 371.3. Add the total overcharge across the three Line Rental Products to arrive at the total damage for the Voice Only Sub-class in the Claim Period.
372. I will also apply an appropriate interest rate to reflect the fact that this damage occurred in the past.
373. The same methodology applies for Split Purchase Customers, the only difference being that the period in which damage occurred for Split Purchase Customers runs to the present day, whereas for Voice Only Customers it ends on 31 March 2018.
374. I expect BT to hold the data I need to carry out this assessment given that it is data which relates to its own customers. As mentioned above, I have already set out some of the information I will need for this assessment as it is relevant to

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other parts of my analysis (e.g. data needed to estimate the degree of excessive pricing for the Line Rental offerings in Section 8.3). In addition, I will need the following information.

374.1. For each month between October 2015 and March 2018 (both inclusive), the number of BT **Voice Only Customers** on each of the following BT SFV access component offerings:

374.1.1. Standard Line Rental;

374.1.2. Line Rental Plus; and

374.1.3. Line Rental Saver.

For each offering, the number of known business users of these offering should be provided separately for each month. To the extent that BT has any information on whether these customers were VAT registered, this should be provided as well.

374.2. For each month from (and including) October 2015 to date, the number of **Split Purchase Customers** on each of the following BT SFV access component offerings:

374.2.1. Standard Line Rental;

374.2.2. Line Rental Plus; and

374.2.3. Line Rental Saver.

Again, for each offering, the number of known business users of these offerings should be provided separately for each month. To the extent that BT has any information on whether these customers were VAT registered, this should be provided as well.

### 9.1.1 Business users of BT SFV Services

375. As mentioned in Section 6.2.1, SFV services can be purchased by businesses, even though BT offers fixed voice services targeted specifically at business customers (which are not in the Proposed Class). In the Provisional Conclusions, Ofcom estimated that around 17% of all SFV customers may be business customers.<sup>275</sup>

376. Three main issues arise in relation to the estimation of aggregate damages to business customers of SFV services:

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<sup>275</sup> Provisional Conclusions, (para. 3.11)



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- 376.1. whether business customers would have passed on the abusive overcharge to their own customers;
- 376.2. the need to exclude VAT amounts which have been reclaimed by businesses from the amount of aggregate damages; and
- 376.3. if any businesses were Voice Only Customers, they would not have benefited from the BT Commitments.

### Pass-on

377. Although I understand that it is for BT to raise pass-on, I have considered, from a theoretical perspective, whether BT SFV customers who are businesses would likely have passed on some or all of the overcharge element of the excessive price of their BT SFV Service to end consumers. I consider that the degree of pass-on is likely to be limited or zero in most cases, for the following two reasons.

377.1. Many of these businesses were likely to have been competing with other businesses which were not on residential SFV tariffs and instead purchased their telephony services through another route (such as Dual Play, or a business service), which would not have faced the excessive charges which I have identified on residential SFV services. If so, the businesses purchasing (residential) SFV services would not be able to pass any of the excess price of this service on to end consumers.

377.2. The cost of BT SFV Services is likely to have been small compared to the total cost base of their business for many of these customers.

378. These points suggest that it is unlikely that the businesses in question would have been able to pass on a material proportion, if any, of the overcharge element of the excessive price.

379. Accordingly, my estimate of total damage currently assumes zero pass-on for business customers.

### VAT registration

380. Although BT SFV Services are residential, as explained above, I understand from Ofcom (as set out in Section 6.2.1) that a number of customers were businesses. It is therefore possible that some Members of the Proposed Classes were VAT registered, and so eligible to recover the VAT included in the price

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paid. Thus, the amount of aggregate damages must be reduced to reflect any VAT that has been reclaimed.

381. My Standard Line Rental price time-series and the time-series for my competitive benchmark both include VAT. While Ofcom provides an estimate of the number of SMEs taking SFV services (as set out in Section 6.2.1), Ofcom does not give an estimate for the number of such customers that were VAT registered (and indeed subsequently reclaimed VAT) and I have no other means of estimating the size of the group based on publicly available information. While it seems unlikely that all SMEs taking SFV services were VAT registered given the applicable revenue threshold for VAT registration,<sup>276</sup> I have no reasonable basis on which to make the necessary adjustment at this stage or to assess its total impact on my interim estimate.

382. However, I provide below the methodology which I will use to make this adjustment once that information is disclosed by BT.

383. In particular, as list prices include 20% VAT, the damage for VAT-registered customers will need to be estimated by comparing:

383.1. the price paid excluding VAT; with

383.2. the competitive benchmark, also excluding VAT.

384. In order to make this adjustment, I can therefore simply exclude VAT from the total damage figure in each period. The effect of making these adjustments is a reduction in damages for each VAT registered Class Member of 16.67%<sup>277</sup> for each relevant month.<sup>278</sup>

### Eligibility

385. Finally, if any BT Voice Only Customers were businesses, they would not have been eligible for the price cut in the BT Commitments: “*The price reduction will not apply to business customers. BT will exclude any standalone voice customers from the price reduction that it has reason to believe are business customers. Such customers will be provided with an opportunity to opt back in if BT’s information is incorrect.*”<sup>279</sup>

<sup>276</sup> £85,000 p.a. to be precise. <https://www.gov.uk/vat-registration/when-to-register#:~:text=You%20must%20register%20for%20VAT,that%20is%20not%20VAT%20exempt>.

<sup>277</sup> This figure is calculated as follows. To remove the 20% VAT rate, I multiply the overcharge figure by a factor of  $1 / (1 + 20\%)$ , which yields 83.33%. The effective percentage reduction is therefore  $1 - 83.33\% = 16.67\%$ .

<sup>278</sup> This approach assumes that a) all such customers in fact claimed the VAT back and b) they claimed back the VAT on the full purchase price (rather than a proportion, which may be relevant if the phone line was used for both residential and business services).

<sup>279</sup> Ofcom Statement, Annex 1 A1 “BT’s Voluntary Proposal” i.e. the BT Commitments (para. 2.2.3)

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386. Thus, my estimates of the number of BT Voice Only Customers and the damage accruing to them might include some (business) customers that did not in fact receive the discount. For those customers, the overcharge will have continued even after 1 April 2018. However, as I do not know the number of business customers that were excluded from the discount, I am unable to adjust my quantum estimate at this stage.

387. I will be able to more accurately identify business customers and estimate their damage upon access to data from BT. As can be seen above, BT identified which of its BT Voice Only Customers were businesses for the purposes of applying the commitments. Depending on the methodology BT employed used, the same approach could potentially be applied to identify businesses which were BT Split Purchase Customers, although I will need to revisit this once the methodology is known.

### 9.1.2 Methodology for distribution purposes

388. I intend to estimate aggregate damages on a top-down basis (rather than a bottom-up basis, building up from individual damage assessments). I would intend to take the following approach to the distribution of damages to individual members of the Class. To estimate the damage incurred by a hypothetical Ms. X:

388.1. BT would be able to identify if she was a Voice Only or Split Purchase Customer;

388.2. BT would also know the specific access offering she took and the specific months that she was billed for the offering;

388.3. Thus, her individual damage could be calculated by multiplying the overcharge element of the excessive price for her offering in the month she was billed for it (which will have been estimated as per paragraph 369.3 above), and adding across the months that she was taking the offering.

388.4. In respect of VAT, this will apply to a small subset of the Proposed Class and can be calculated as I explain above.

388.5. In respect of pass-on, if this is raised by BT, at this stage I think it is unlikely that it would be proportionate to try to identify the exact level of pass-on for individual business customers. My current view is that it would be sensible to endeavour to find an approach that is reasonable on an aggregate basis and apply this to all (relevant) members of the Proposed

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Class. I have provided some initial thoughts at paragraphs 377 to 379 above.

388.6. Similarly, in respect of interest rates, at this stage I think it is unlikely that it would be proportionate to try to identify the exact rate relevant to each individual, and would again suggest an aggregate approach, for example identifying a single rate reflecting the interest rates typically available to this demographic, and applying it to each individual's overcharge as determined above.

## 9.2 Estimate of damage based on public domain data

389. In the section above, I set out the methodology which I intend to use to calculate damages suffered by the Proposed Class if I am given access to the necessary data.

390. For the purposes of this preliminary report, I have estimated the number of BT Voice Only and BT Split Purchase Customers *in total* since I do not at present have access to customer numbers for each type of access offering *i.e.* Standard Line Rental, Line Rental Saver and Line Rental Plus. This allows me to give an approximation of aggregate damages owed to the Proposed Class at this stage.

391. I therefore set out below my methodology for giving a preliminary estimate of the amount of aggregate damages, based on publicly available information which involves the following three elements.

391.1. The duration for which damage was suffered by each Proposed Sub-class, namely:

391.1.1. from 01/10/2015 until 31/03/2018 for BT Voice Only Customers,<sup>280</sup> and

391.1.2. from 01/10/2015 to present day for BT Split Purchase Customers. (For the purpose of my interim estimates, I calculate damages until 31/10/2020 for this Proposed Subclass).

391.2. *Estimates* of the number of BT Voice Only and Split Purchase Customers in each month of the Claim Period (explained further in Section 9.2.1).

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<sup>280</sup> With the potential exception of Voice-only business customers for some of whom the relevant duration may to the present day, as set out in Section 9.1.1.

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391.3. The level of excessive price/overcharge in each month for the Standard Line Rental offering only, which I assume applies across all three offerings (explained further in Section 9.2.2).

### 9.2.1 Number of customers at a given point in time

392. As mentioned above, I do not have customer numbers at an access component offering level. However, the data published by Ofcom as part of its 2017 review allows me to estimate, on a monthly basis, the total number of BT Voice Only and BT Split Purchase Customers between 01/10/2015 and 31/10/2020.

393. I have estimated the number of BT Voice Only and Split Purchase Customers relevant to the Claim in each month using monthly estimates for two basic inputs:

393.1. Ofcom’s estimate of the number of BT Voice Only and Split Purchase Customers; and

393.2. an adjustment to remove customers who are excluded from the Class (namely customers who take the Home Phone Saver product, as I understand that BT Basic customers are already excluded from the source data – I discuss this further below).

394. The key source for my calculations is Ofcom’s Evidence supporting the Statement.<sup>281</sup>

#### Ofcom’s estimates of BT’s Voice Only and Split Purchase Customers

395. The raw data for market size was sourced from Ofcom’s Evidence supporting the Statement. Ofcom reports data on Voice Only and Split Purchase Customers in the form of charts depicting quarterly time-series of the number of Voice Only and Split Purchaser Customers for the period Q1 2013 to Q1 2017, both for BT and the UK overall.<sup>282,283</sup> These are shown below in Figure 24 and Figure 25 further below.

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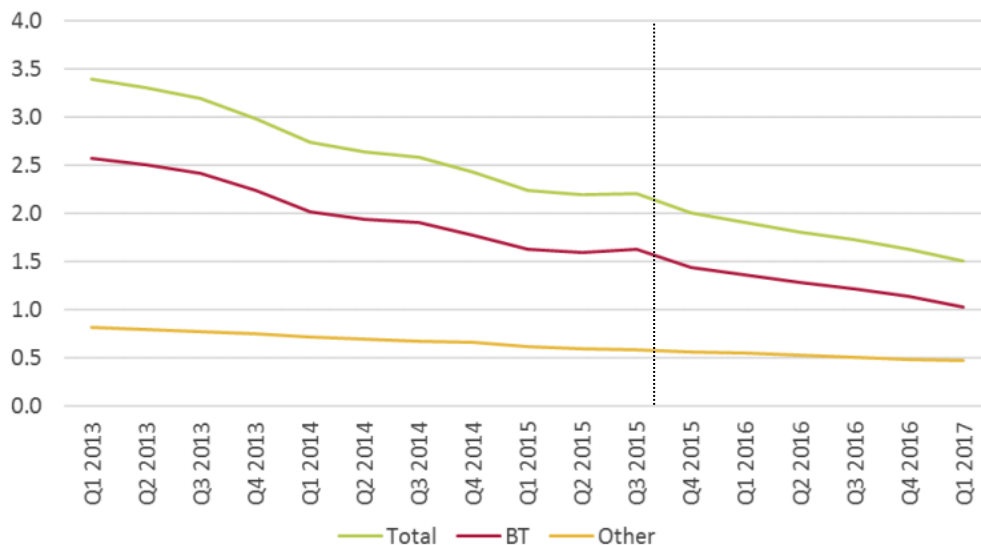
<sup>281</sup> [https://www.ofcom.org.uk/data/assets/pdf\\_file/0014/107321/standalone-landline-evidence.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0014/107321/standalone-landline-evidence.pdf)

<sup>282</sup> *Ibid.*, Figure 1.4

<sup>283</sup> *Ibid.*, Figure 1.6

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**Figure 24 Number of Voice Only Customers in the UK (millions)**



Source: Frontier Economics and Ofcom data.

Notes: 1) The vertical dotted line approximately represents the beginning of the Claim Period i.e. 1 October 2015 (one month after the end of Q3 2015). 2) Ofcom erroneously describes the units as thousands, rather than millions of lines. However, Ofcom clarifies in the text that the figures shown are indeed in millions.

**Figure 25 Number of Split Purchase Customers in the UK (millions)**



Source: Frontier Economics and Ofcom data.

Notes: 1) The vertical dotted line approximately represents the beginning of the Claim Period i.e. 1 October 2015 (one month after the end of Q3 2015). 2) Ofcom erroneously describes the units as thousands, rather than millions of lines. However, Ofcom clarifies in the text that the figures shown are indeed in millions.

396. As the data underlying these figures was not presented, the charts themselves represented the best available information. I estimate the monthly number of Voice Only and Split Purchase Customers during the Claim Period as follows:

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- 396.1. Up to and including Q1 2017, I use the numbers implied by the lines shown in Figure 24 and Figure 25 above as my starting point for estimating the number of BT Voice Only and Split Purchase Customers. As Ofcom data is presented on a quarterly basis,<sup>284</sup> I derive monthly estimates by assuming that the customer numbers change at a linear rate between quarters.
- 396.2. From Q2 2017 until the end of October 2020, I have projected customer numbers by relying on the average monthly rate of change implied by estimates derived for Q1 2013 to Q1 2017.

### Exclusions

397. I need to exclude customers of BT Basic and BT Home Phone Saver from the data I rely on.
398. Based on Ofcom's Statement and Evidence supporting the Statement, I infer that:
- 398.1. Ofcom has already excluded BT Basic customers from the Voice Only and Split Purchase Customer numbers. This is because BT Basic Customers are identified as not being eligible for the price cut in the Commitments<sup>285</sup> and have been excluded from Ofcom's analysis of market shares,<sup>286</sup> and
- 398.2. Home Phone Saver customers have been included in the Voice Only and Split Purchase Customer numbers. This is because Ofcom refers to one million Voice Only Customers being eligible for BT's voluntary price cut of which 200,000 are Home Phone Saver customers.<sup>287</sup> I also assume that Ofcom estimate of BT's Split Purchase Customer numbers includes Home Phone Saver customers as I have not seen evidence to the contrary.
399. I therefore adjust Ofcom's data on customer numbers in each month to exclude Home Phone Saver customers, on the following basis.
- 399.1. Ofcom states in the Statement (of October 2017) that there were c. 200,000 Home Phone Saver customers who "*could also receive the price cut*".<sup>288</sup> My understanding is that all these customers were Voice Only Customers and I therefore exclude these 200,000 customers from my

<sup>284</sup> Periodicity is important because both retail and wholesale prices change periodically. Therefore, estimating damages on a monthly basis means that prices are broadly accurate at any given time, which allows a more accurate damage estimate. I therefore also rely on monthly estimates of customer numbers.

<sup>285</sup> Statement, (Footnote 8)

<sup>286</sup> Evidence Supporting the Statement, (para 1.25)

<sup>287</sup> Statement, (para 1.18 and Footnote 6)

<sup>288</sup> Statement (Footnote 6)

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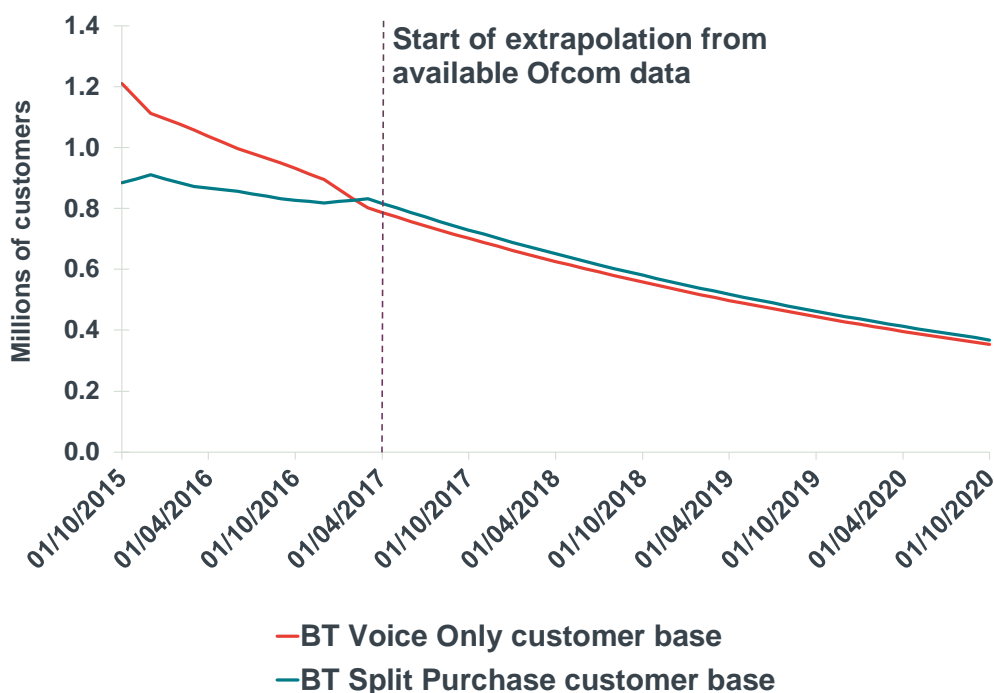
estimate of Voice Only Customers for October 2017. These customers represented 22% of BT’s Voice Only Customers in October 2017.

399.2. For the other months in the Claim Period, I assume that the proportion of BT’s Voice Only Customers who took Home Phone Saver remains the same as that in October 2017 (i.e. 22%), and exclude these customers.

399.3. In the absence of information relating to Home Phone Saver take-up among Split Purchase Customers, I also assume that the proportion of BT’s Split Purchase Customers who took Home Phone Saver in any month is the same as that for Voice Only Customers (22%) and exclude these customers.

400. The following figure presents my best estimate of BT Voice Only and BT Split Purchase Customers for the relevant BT line rental products.

**Figure 26 Estimate of the customer base: BT’s SFV customers adjusted to exclude Home Phone Saver customers**



Source: Frontier Economics and Ofcom data

Note: The vertical dotted line represents the end of the part of the Claim Period which is covered by the Ofcom data and the figures after that are estimated as set out above.

401. I will refine this estimate when I have access to better data as set out in Section 9.1.



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## 9.2.2 Level of overcharge

402. As set out above, I am currently unable to estimate the level of overcharge for each access offering. For the purposes of an initial assessment, I have assumed that the absolute level of excessive pricing is the same across Standard Line Rental, Line Rental Plus, and Line Rental Saver.
403. I consider this a reasonable assumption – at this stage – as the price differences between the products likely represent cost differences, as I explain in Section 8.3. The fact that the BT Commitments introduced a £7 monthly discount across the three relevant access components of BT SFV Services<sup>289</sup> supports a preliminary view that the degree of overcharge is sufficiently similar to proceed on this basis.
404. Thus, I estimate the level of overcharge in each month by comparing (in nominal terms)<sup>290</sup> the BT Standard Line Rental price over time with my best estimate of the competitive benchmark, which is the BT Standard Line Rental price on 01/11/2009 adjusted for WLR price changes (as discussed in Section 8.2.1 and 8.3). I apply this across all BT Voice Only and Split Purchase Customers. This is set out in Figure 27.

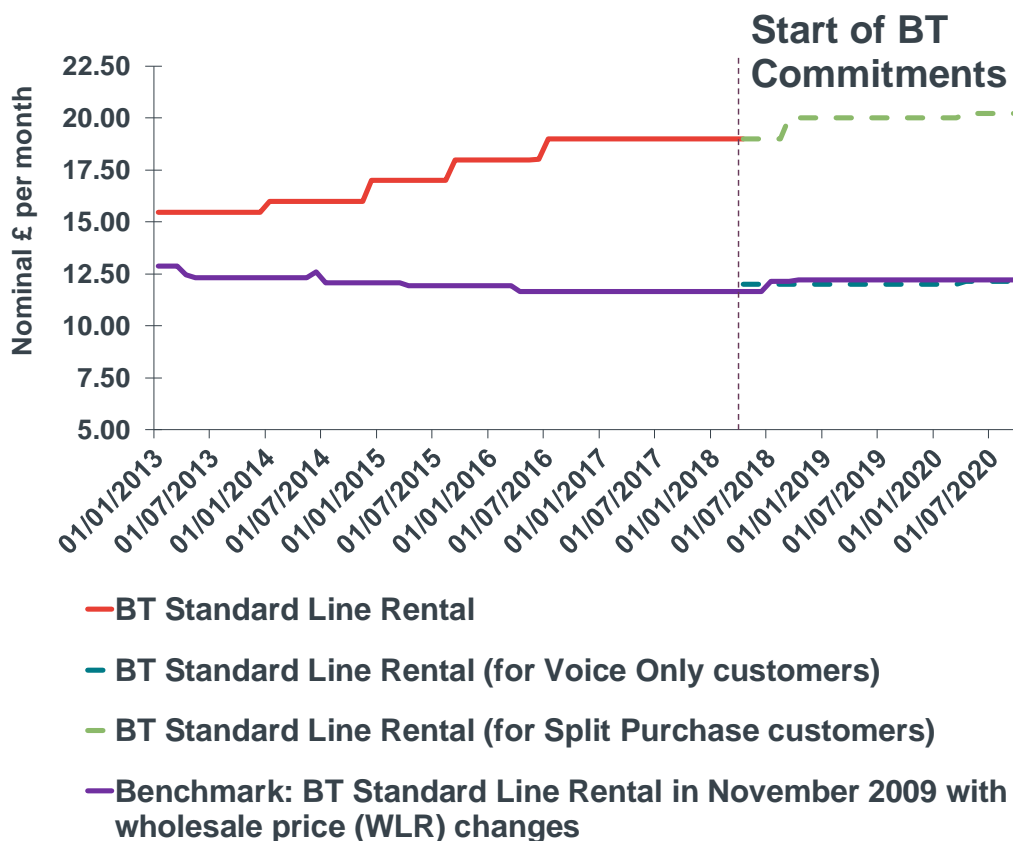
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<sup>289</sup> Statement, Annex 1 “A1 BT’s Voluntary Proposal” (paras. 2.1.1, 2.1.2)

<sup>290</sup> All my calculations have been carried out in nominal terms so as to calculate the amount by which a customer overpaid for their Line Rental product at any given point in time – an interest rate can then be applied to estimate the opportunity cost of this forgone amount.

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**Figure 27 Comparing Standard Line Rental prices with my estimate of the competitive benchmark**



Source: Frontier Economics estimate based on publicly available data

Note: 1) Prices include VAT and are presented in nominal terms. 2) The y-axis begins at £5 for presentational clarity.

405. I have set out in Section 9.1 the additional data I will need and the approach I will take to estimating the damage for customers of each individual access offering.

### 9.2.3 Interim estimate of the quantum of damages

406. As set out above, I estimate the damage for BT Voice Only Customers and another for BT Split Purchase Customers separately. The methodology for the assessment of the damage for the two Proposed Sub-classes is identical, with the only difference being that damage is incurred over different time periods. I then add the damage for the two Proposed Sub-classes together to form the aggregate damage estimate.

407. My methodology for estimating total damage for BT Voice Only Customers is set out below:

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- 407.1. For each month between (and including) 01/10/15 and 31/03/18, I multiply the number of BT Voice Only Customers in that month with the estimate of overcharge paid in that month. This gives me the total overcharge for the BT Voice Only Customers each month.
- 407.2. For the purposes of this preliminary estimate, I have been instructed to model aggregate damages with a simple interest rate of 8% per annum, and with a compound interest rate of 8%. I add the monthly equivalent rate of interest to the overcharge in each month of the Claim Period.
- 407.3. Adding these monthly damage estimates across the relevant period allows me to arrive at the estimated quantum of damages for the BT Voice Only Sub-class.
408. The methodology for estimating the total damage to BT Split Purchase Customers is identical, except that the damage period for these customers runs until the present day. As a result, I estimate the monthly damage for Split Purchase Customers for each month between (and including) 01/10/15 and 31/10/20 as per the steps set out above, and add across these monthly estimates to arrive at the damage to the Split Purchase Sub-class.

### Preliminary estimate of total damage

409. My preliminary estimate of aggregate damages for the Class, inclusive of VAT but before interest, is **£469 million**.<sup>291</sup> This comprises the following damage for the Proposed Sub-classes:
- 409.1. £182 million for the BT Voice Only Customer Sub-class; and
- 409.2. £287 million for the BT Split Purchase Sub-class.
410. My preliminary estimate of aggregate damages for the Class, inclusive of VAT and *simple* interest at 8%, is **£589 million**. This comprises the following damage for the Proposed Sub-classes:
- 410.1. £238 million for the BT Voice Only Sub-class; and
- 410.2. £351 million for the BT Split Purchase Sub-class.

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<sup>291</sup> All estimates have been rounded.

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411. My preliminary estimate of aggregate damages for the Class, inclusive of VAT and *compound* interest at 8%, is **£608 million**. This comprises the following damage for the Proposed Sub-classes:

411.1. £248 million for the BT Voice Only Sub-class; and

411.2. £360 million for the BT Split Purchase Sub-class.

412. Given the estimated number of unique customers in each Proposed Sub-class, this implies the following average quantum of damage per unique customer:

412.1. £148/£193/£201 per unique BT Voice Only Customer, on a no interest/8% simple interest/8% compound interest basis respectively; and

412.2. £265/£324/£333 per unique BT Split Purchase Customer, on a no interest/8% simple interest/8% compound interest basis respectively.

## 10 CLASS SIZE

413. Mischon have referred me to the CAT Rules which state that the Claim Form “shall” include “*an estimate of the number of class and any sub-class members and the basis for that estimate*” (emphasis added).<sup>292</sup> The CAT Guide adds: “*although the claim form must give an evidence based estimate of the size of the class, it is not necessary to identify each class member (in an opt-out claim) or specify exactly how many persons are within the class*” (emphasis added).<sup>293</sup>

414. To this end, I have estimated the size of the Proposed Class and the Proposed Sub-classes below, based on public domain information. I set out in Section 10.2 the data I would need from BT to more accurately estimate Class size post-Certification. I also provide a view on the likely geographic distribution of Proposed Class Members, as per my instructions.

### 10.1 Interim estimate of Proposed Class Size

415. As mentioned above, I have estimated Proposed Class and Proposed Sub-class sizes based on information available in the public domain. These estimates are distinct from my estimate of the number of BT Voice Only and Split Purchase Customers of BT SFV Services in each month (which I had set out in Section 9.2.1) for the following reasons.

415.1. The estimate of customer numbers in Section 9.2.1 for the purposes of assessing aggregate damages captures the overall number of BT Voice Only and BT Split Purchase Customers in each month during in the Claim Period, with differences in customer numbers from month to month reflecting the net effect of customers leaving and joining.

415.2. By contrast, in order to estimate total Proposed Class size it is necessary to capture the total number of individual customers that purchased the relevant services during the Claim Period. Thus, as new customers will have joined the class over time, the number of individual customers in the class will be greater than the highest number of customers buying BT SFV Services at any one time.

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<sup>292</sup> CAT Rules, (para. 75 (3) (c))

<sup>293</sup> CAT Guide, p.75

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416. I estimate that the size of the Proposed Class is 2.31 million, of which:<sup>294</sup>

416.1. 1.23 million members are in the Voice Only Sub-class; and

416.2. 1.08 million members are in the Split Purchase Sub-class.

417. I explain the basis for this calculation below.

### Methodology

418. My estimate of the Proposed Sub-class sizes for BT Voice Only and BT Split Purchase Customers uses two basic inputs:

418.1. the estimated number of BT customers in the relevant SFV customer group at the beginning of the Claim Period (as per my explanation in Section 9.2.1)<sup>295</sup>; and

418.2. an adjustment to reflect the estimated number of customers who joined the relevant customer group since the beginning of the Claim Period.

419. I have taken as a starting point my estimate of the number of relevant customers as at 1 October 2015, as set out in Figure 26. These are as follows:

419.1. 1.21 million BT Voice Only Customers; and

419.2. 0.88 million BT Split Purchase Customers.

420. In the absence of data on the number of new joiners over time, I need to estimate the rate at which customers have taken up BT's SFV services in each period. To do so I employ available information pertaining to annual switching rates in Ofcom's Evidence supporting the Statement.

420.1. For Voice Only Customers, 1% of BT's Voice Only Customers switched landline provider in the 12-month period preceding the survey.<sup>296</sup>

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<sup>294</sup> The class size, as estimated above, may also include members that have passed away either during or since the period of infringement. I understand that claims can be made on their behalf by their estates, so I have not adjusted the class size to reflect deaths. Note that small discrepancies between the figures are the result of rounding.

<sup>295</sup> This therefore excludes customers of Home Phone Saver and BT Basic, as explained in Section 9.3.

<sup>296</sup> Ofcom's Evidence, (Figure 1.58)

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- 420.2. For Split Purchase Customers<sup>297</sup> 6% of all split supplier customers switched landline provider during the same period (a switching rate for only BT Split Purchase Customers was not provided).<sup>298</sup>
421. In the absence of better information, I use these rates to assume a percentage of customers that joined the relevant customer group in each period.
422. Converting this to a monthly rate allows me to develop an estimate, separately for each Proposed Sub-class, of the number of customers in each month who were not previously BT SFV customers and were therefore not included in the number of customers on 1 October 2015.<sup>299</sup>
423. I estimate the additional unique customers in each month during the Claim Period by applying the relevant average monthly switching rate to the number of subscribers in each month. This results in an estimate of new customers in each month who would form part of the Proposed Class. I add the estimates of the number of new customers for each month of the Claim Period to the number of customers as at 1 October 2015.
424. This approach results in estimated Proposed Sub-class sizes as follows:
- 424.1. 1.23 million BT Voice Only Customers; and
- 424.2. 1.07 million BT Split Purchase Customers.

## 10.2 Data needed to estimate Class Size post-Certification

425. BT will hold the precise number of customers that belong to the Proposed Class and Proposed Sub-classes. Accordingly, I would need the following information.

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<sup>297</sup> Ofcom survey evidence relates to just split-supplier customers rather than both split-supplier and split-service customers as they had difficulty isolating/identifying split-service customers. However, Ofcom considers that survey evidence from split-supplier customers is reasonable proxy for Split Purchasers as it estimates that split-supply customers account for around 80% of Split Purchasers, with the remaining 20% being split-service customers. See Ofcom's Evidence, (paras 1.103 to 1.107)

<sup>298</sup> Ofcom's Evidence, (Figure 1.57).

<sup>299</sup> In converting annual switching rates to monthly switching rates, I have assumed that switching rates do not vary significantly, either seasonally or across the Claim Period more generally, as I do not have better information available to me.

I have also assumed that customers who switched to BT's SFV products following 1 October 2015 had not previously switched away from BT's SFV products during the Claim Period. Although some customers may have done so, the low switching rates observed for BT's SFV customers and SFV customers of other providers suggest that the impact of being able to identify these customers is negligible. In any case, this would impact only my estimates of the class size, and not my estimate of the quantum of damages.

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### Voice Only Sub-class

426. The total number of **unique Voice Only Customers** that purchased the following BT access offerings between 01/10/2015 up till 31/03/2018 (both inclusive):

- 426.1. Standard Line Rental;
- 426.2. Line Rental Plus; and
- 426.3. Line Rental Saver.

427. Adding across the number of unique Voice Only Customers purchasing each of these offerings during the Claim Period would give me the Voice Only Sub-class size.

### Split Purchase Sub-class

428. The total number of **unique Split Purchase Customers** that purchased the following BT access offerings product from 01/10/2015 to date:

- 428.1. Standard Line Rental;
- 428.2. Line Rental Plus; and
- 428.3. Line Rental Saver.

429. Adding across the number of unique Split Purchase Customers purchasing each of these offerings during the Claim Period would give me the Split Purchase Sub-class size.

## 10.3 Geographic distribution of Proposed Class Members

430. I understand that the geographic distribution of Proposed Class Members needs to be ascertained for the purposes of determining the appropriate location of the proceedings.

431. While Ofcom does not provide a geographic distribution of these customers, I observe that the majority of the population resides in England and Wales – 59.4 million (89%) of the UK's total population of 66.8 million in 2019.<sup>300</sup> This is true across the age distribution – for instance, 89.3% of those over 75 lived in

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<sup>300</sup> ONS population estimates, available at: <https://www.ons.gov.uk/peoplepopulationandcommunity/populationandmigration/populationestimates/datasets/populationestimatesforukenglandandwaleslesscotlandandnorthernireland>



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England and Wales in 2019. These proportions do not vary significantly across the Claim Period, as shown below.

**Figure 28 Geographic distribution of customers, 2015 – 2019**

Benchmark	2015	2016	2017	2018	2019
% UK total population living in England and Wales	88.9%	88.9%	89.0%	89.0%	89.0%
% UK over-75 population living in England and Wales	89.2%	89.2%	89.2%	89.2%	89.3%

Source: Frontier Economics based on ONS data

432. I have no reason to believe that the geographic distribution of the Proposed Class Members would deviate significantly from the population distribution. I therefore consider that it is highly likely that the majority of Proposed Class Members are located in England and Wales.<sup>301</sup>

<sup>301</sup> As will be seen above, I define the geographic market to be the UK excluding the Hull Area. While this may reduce the share of customers in England relative to the averages set out above, given the size of the population of Hull (at around 260,000 people in 2019, see ([http://109.228.11.121/IAS\\_Live/](http://109.228.11.121/IAS_Live/)), I do not consider any such reduction to be sufficient to change the conclusion that it is highly likely that the majority of class members are located in England and Wales.

## 11 STATEMENT OF TRUTH

433. I, David Parker, declare that:
434. I understand that my duty in providing written reports and giving evidence is to help the Tribunal on matters within my expertise and that this duty overrides any obligation to the party by whom I am engaged or the person who has paid or is liable to pay me (as set out in paragraph 7.67 of the Guide to Proceedings). I confirm that I have complied and will continue to comply with my duty.
435. I confirm that I have not entered into any arrangement where the amount or payment of my fees is in any way dependent on the outcome of the case.
436. I know of no conflict of interest of any kind.
437. I will advise the party by whom I am instructed if, between the date of my report and the hearing of the CPO application, there is any change in circumstances which affect my opinions expressed above.
438. I have shown the sources of all information I have used.
439. I have exercised reasonable care and skill in order to be accurate and complete in preparing this report.
440. I have identified any facts or matters relating to my opinions that fall outside my expertise.
441. I have endeavoured to include in my report those matters, of which I have knowledge or of which I have been made aware, that might adversely affect the validity of my opinion. I have clearly stated any qualifications to my opinion.
442. Where my opinion relies on assumptions or evidence, I have identified these, and explained why I consider them to be reasonable.
443. Where my opinion is provisional because relevant data is not available to me, I have identified that this is the case and specified what data I will require in order to advance the analysis.
444. I have not, without forming an independent view, included or excluded anything which has been suggested to me by others, including my instructing lawyers.
445. I will notify those instructing me immediately and confirm in writing if, due to any change in circumstances or for any other reason, my report requires any correction or qualification.
446. I understand that:
- 446.1. my report will form evidence to be given under oath or affirmation;

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- 446.2. questions may be put to me in writing for the purposes of clarifying my report and that my answers shall be treated as part of my report and covered by my statement of truth;
- 446.3. I may be required to attend Court to be cross examined on my report; and
- 446.4. I am likely to be the subject of public adverse criticism by the Tribunal if it concludes that I have not taken reasonable care in trying to meet the standards set out above.
447. I have read part 35 of the Civil Procedure Rules and the accompanying practice direction and the Civil Justice Council Guidance for the instruction of experts in civil claims and I have complied with their requirements.
448. I believe that the facts stated in the report are true, and that the opinions expressed are correct.

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**Signed**

**Dated**

*D Parker*

13<sup>th</sup> January 2021

## ANNEX A ESTIMATING ACCESS PRICES AND COMPETITIVE BENCHMARKS

449. In this section I set out the methodology I have used to estimate the prices charged by BT for the access component of its SFV services, specifically its Standard Line Rental, Line Rental Saver and Line Rental Plus offerings, during the Claim Period.

450. I also set out how I estimate the competitive benchmark level for Standard Line Rental during that period, including the assumptions and sources on which I have relied.

### A.1 Estimating the time-series of prices for the relevant access offerings

451. I have estimated the time-series of prices for the relevant access offerings in each month, in nominal terms, using the following inputs:

451.1. Ofcom monthly time-series price data for BT's Standard Line Rental products, in real terms, covering the period January 2013 to June 2019;<sup>302</sup>

451.2. BT's Consumer Price Guides, which provide information on the price of BT's Standard Line Rental product for the period following June 2019, and information on the prices of BT's Line Rental Saver and Line Rental Plus products for the duration of the Claim Period;<sup>303</sup> and

451.3. Information relating to the price reductions offered by BT under the Commitments,<sup>304</sup> from 1 April 2018.

452. For each access component offering, I combined the information available to produce a time-series for the duration of the Claim Period. The prices paid by each Proposed Sub-class for a given offering were identical until 1 April 2018, when BT introduced its voluntary commitment to reduce prices for some customers. Thereafter, the prices paid by the different Proposed Sub-classes

<sup>302</sup> Available at <https://data.gov.uk/dataset/f1425d4d-61f4-4596-a06a-8ff2522d8a46/pricing-trends-for-communications-services>

<sup>303</sup> Available at [https://www.bt.com/assets/pdf/BT\\_PhoneTariff\\_Residential.pdf](https://www.bt.com/assets/pdf/BT_PhoneTariff_Residential.pdf) and <https://www.bt.com/mobile/pdf/bt-consumer-price-guide-15.pdf>. Archived editions of the price guide used to obtain historical data available at [https://web.archive.org/web/\\*/https://www.bt.com/assets/pdf/BT\\_PhoneTariff\\_Residential.pdf](https://web.archive.org/web/*/https://www.bt.com/assets/pdf/BT_PhoneTariff_Residential.pdf)

<sup>304</sup> Statement, Annex A1

## EXPERT REPORT OF DAVID PARKER

varied depending on whether the discount applied to that Proposed Sub-class or not.

### A.1.1 Conversion of Ofcom price data into nominal terms

453. The starting point for my estimate of the price time series for BT's Standard Line Rental offering is Ofcom's monthly time series price data, which covers BT's prices for the period January 2013 to June 2019. This data is provided in real terms, adjusted for CPI inflation. I therefore convert this to a nominal price series for Standard Line Rental by removing the inflation adjustment.

### A.1.2 Incorporating additional pricing data

454. The Ofcom pricing dataset has two key limitations:

454.1. The time series of Standard Line Rental do not cover the entire Claim Period as BT's prices were unavailable after June 2019.

454.2. Prices for BT Line Rental Saver and BT Line Rental Plus were not provided (for any period).

455. I have therefore had to employ additional sources of pricing data to complement the Ofcom dataset.

#### Incorporating additional Standard Line Rental price data

456. As set out above, I sourced BT's Standard Line Rental prices after June 2019 from BT's Consumer Price Guides. The Consumer Price Guides show that the price of £19.99 per month recorded in Ofcom's pricing dataset for June 2019 did not change until BT increased prices to £20.20 per month from 31 March 2020 (in nominal terms and inclusive of VAT).<sup>305,306</sup> This price had not increased in BT's revised price guide as of 1 August 2020.<sup>307</sup> I append this information to the Ofcom pricing dataset in order to produce a time-series of BT's residential Standard Line Rental prices for the entire Claim Period.

<sup>305</sup> The price available on BT's website in January 2020 was still £19.99, as shown here: [https://web.archive.org/web/20200104185720/https://www.bt.com/assets/pdf/BT\\_PhoneTariff\\_Residential.pdf](https://web.archive.org/web/20200104185720/https://www.bt.com/assets/pdf/BT_PhoneTariff_Residential.pdf)

<sup>306</sup> The higher price of £20.20, applicable from 31 March 2020, is shown here: [https://web.archive.org/web/20200401010720/https://www.bt.com/assets/pdf/BT\\_PhoneTariff\\_Residential.pdf](https://web.archive.org/web/20200401010720/https://www.bt.com/assets/pdf/BT_PhoneTariff_Residential.pdf)

<sup>307</sup> [https://web.archive.org/web/20200805141248/https://www.bt.com/assets/pdf/BT\\_PhoneTariff\\_Residential.pdf](https://web.archive.org/web/20200805141248/https://www.bt.com/assets/pdf/BT_PhoneTariff_Residential.pdf)

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Estimating prices for Line Rental Saver and Line Rental Plus

**Line Rental Saver**

457. BT Line Rental Saver is offered at a discount to BT Standard Line Rental, in exchange for payment for a whole year being made up-front. As discussed above, Ofcom’s pricing dataset did not include prices for BT Line Rental Saver or BT Line Rental Plus. However, using BT’s Consumer Price Guides<sup>308</sup> I am able to determine the price differentials for the two products, relative to Standard Line Rental, during the Claim Period:

457.1. before 1<sup>st</sup> August 2017, Line Rental Saver was 10% cheaper than Standard Line Rental; and

457.2. thereafter, Line Rental Saver included 12 months for the price of 11 months (a discount of 1/12, or 8.3%).<sup>309</sup>

458. Using this information alongside the monthly time-series data for BT’s Standard Line Rental product described above, I have been able to calculate the equivalent monthly<sup>310</sup> price of Line Rental Saver in each month during the Claim Period.

**Line Rental Plus**

459. As far as I have been able to determine from BT’s Consumer Price Guides, BT has charged a premium for Line Rental Plus of £2 per month (nominal and inclusive of VAT) above the Standard Line Rental price throughout the Claim Period.<sup>311</sup> I have therefore applied this differential in each month of the Claim Period in order to construct a monthly time series of prices for the Line Rental Plus product.

<sup>308</sup> I used archived historical editions of BT’s Consumer Price Guides, which are available here: [https://web.archive.org/web/\\*/https://www.bt.com/assets/pdf/BT\\_PhoneTariff\\_Residential.pdf](https://web.archive.org/web/*/https://www.bt.com/assets/pdf/BT_PhoneTariff_Residential.pdf)

<sup>309</sup> BT’s Consumer Price Guide for October 2016 reports that Line Rental Saver represented a 10% discount to Standard Line Rental at that time (see here: <https://www.bt.com/mobile/pdf/bt-consumer-price-guide-15.pdf>). By the time Ofcom published its supporting evidence document in October 2017 (referenced earlier), the “free month” pricing for Line Rental Saver was described by Ofcom as being new. I understand that BT introduced price changes in April and August of 2017, although a Consumer Price Guide is unavailable for those periods. The only evidence I was able to find in relation to the specific timing of this price change was on a BT community forum, where discussions suggest that the pricing of Line Rental Saver increased in August 2017 (see here: <https://community.bt.com/t5/Landline/Line-Rental-Saver/m-p/1768306>). I have therefore assumed that the price change took effect on 1<sup>st</sup> August 2017.

<sup>310</sup> Although Line Rental Saver is payable on an annual basis, I have divided this by 12 to calculate an equivalent monthly price which can be compared to the price of the Standard Line Rental product.

<sup>311</sup> I have based this on an analysis of BT’s archived price guides, which all present a price difference between the two products of £2 per month.

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### A.1.3 Reflecting the BT Commitments

460. The BT Commitments reduced the price of some of its line rental offerings from 1<sup>st</sup> April 2018, and as could be seen in Figure 23 there does not appear to be evidence of a contemporaneous increase in calls prices.

461. For ease of reference, the key details of the price reductions (to the extent that they are explained in the Commitments) are as follows:

*“BT will:*

*2.1.1 apply on 1 April 2018 a £7 (seven) reduction (including VAT) to the monthly price of standard line rental and line rental plus (Line Rental services) for Fixed Voice-Only Customers (as defined in paragraph 2.2 below);*

*2.1.2 apply on 1 April 2018 an analogous adjustment to the annual charge for Line Rental Saver and ensure that those customers who paid the annual charge before 1 April 2018 benefit from the monthly discount for the remainder of their contract period after 1 April 2018;*

*2.1.3 not increase the price of its line rental products for Fixed Voice-Only Customers before 1 April 2019 and limit increases for the remaining two years of the commitment period to CPI+2.5%;*

*2.1.4 cap future price increases of a basket of Line Rental services and call products for Fixed Voice-Only Customers at CPI (up to and including 31 March 2021);*

*2.1.5 not increase the charges for Home Phone Saver customers before 1 April 2021.”<sup>312</sup>*

462. I have reflected the way in which the BT Commitments affected specific customer groups in my analysis.

### A.1.4 Estimate of prices paid for the relevant products

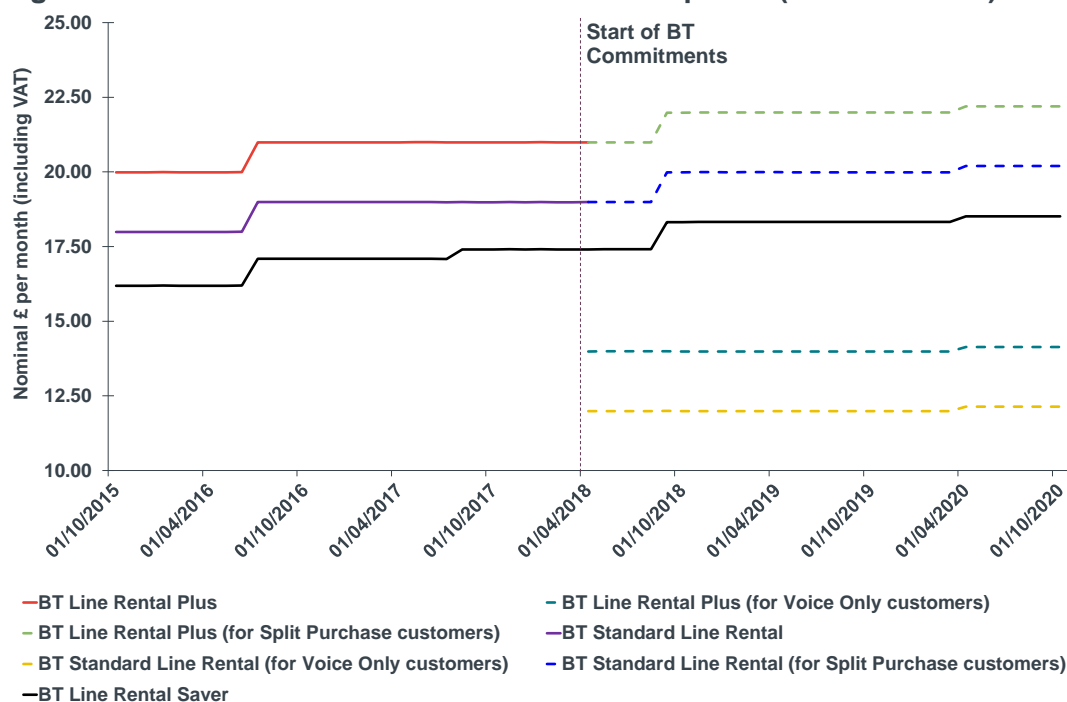
463. Based on the analysis I have described in the preceding subsections, the time series of prices paid by BT customers for the three relevant products throughout the Claim Period is shown in Figure 29.

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<sup>312</sup> Statement, Annex A1

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**Figure 29 Evolution of BT Line Rental Product prices (nominal terms)**



Source: Frontier Economics, Ofcom data and BT Consumer Price Guide data, prices presented in nominal terms, estimated based on a combination of a price index and nominal prices.

Notes: 1) Prices are presented in nominal terms and include VAT. 2) The y-axis begins at £10 for presentational clarity. 3) It was not possible to calculate a reduced price paid by Line Rental Saver customers after 1 April 2018 as the discount they received would have depended on when they first took the Line Rental Saver product. In any case, the Line Rental Saver product is no longer available to Voice Only Customers. 4) The vertical dotted line represents the introduction of the BT Commitments on 1 April 2018. 5) Until 1 August 2017 (note: this is an estimate and is explained in Annex A), the discounted Line Rental Saver price represented a free month in each year versus the Standard Line Rental price, i.e. 11 months for the price of 12 (a c.8.3% discount). Thereafter, customers instead received a reduction of 10% relative to the Standard Line Rental price.

## A.2 Estimating the time-series of estimates of the competitive benchmark

464. I have estimated three competitive benchmarks for the Standard Line Rental product. These are:

464.1. BT's Standard Line Rental price in November 2009, adjusted to reflect changes in wholesale (WLR) charges – which I consider to be the most appropriate competitive benchmark;

464.2. BT's Standard Line Rental price in November 2009 (with no adjustments to reflect changes in wholesale charges); and

464.3. BT's Standard Line Rental price (for Voice Only Customers) after BT's voluntary commitment price reduction.

465. I rely on the following basic inputs to estimate these benchmarks:

465.1. BT's Standard Line Rental price in November 2009;



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465.2. An adjustment to reflect cost changes during the Claim Period, based on the evolution of Openreach’s WLR price; and

465.3. BT’s Consumer Price Guide.<sup>313</sup>

466. All of the required inputs are available in nominal terms, so I do not need to make any adjustment for inflation.

### A.2.1 BT’s Residential Line Rental price in November 2009, adjusted to reflect changes in wholesale charges

467. Ofcom’s Q2 2009 Telecommunications Market Data Update reports that the relevant price is £12.50 per month (nominal, inclusive of VAT).<sup>314</sup> This is then adjusted to reflect differences in the price of WLR over time.

468. Openreach’s historical WLR pricing information contains the price of WLR, among other wholesale inputs, from 2006 to present.<sup>315,316</sup> Using this, I adjust BT’s Residential Line Rental price in November 2009 (£12.50 per month) in each month to reflect the difference in WLR prices in any given month relative to the WLR price in November 2009.

469. Since wholesale charges exclude VAT, I also make an adjustment to ensure VAT is reflected the competitive benchmark as this is consistent with prices that would be faced by retail customers.

### A.2.2 BT’s Residential Line Rental price in November 2009

470. Ofcom’s Q2 2009 Telecommunications Market Data Update reports that the relevant price is £12.50 per month (nominal, inclusive of VAT).<sup>317</sup> For this particular estimate of the competitive benchmark, this is the price in each month of the Claim Period.

### A.2.3 BT’s Residential Line Rental price (Voice-only) after the BT Commitments price reduction

471. This competitive benchmark relates to the line rental price paid by BT’s Voice Only Customers following the April 2018 price reduction under the BT

<sup>313</sup> Available at: [https://www.bt.com/assets/pdf/BT\\_PhoneTariff\\_Residential.pdf](https://www.bt.com/assets/pdf/BT_PhoneTariff_Residential.pdf)

<sup>314</sup> [https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates/q2\\_2009](https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates/q2_2009)

<sup>315</sup> WLR Pricing | Wholesale Access (Analogue Lines) | Line Rental Prices. Available at <https://www.openreach.co.uk/org/home/products/pricing/loadProductPrices.do?data=63iUyYbpRV%2Fdw36mtxo4r1nqs1m6Ockz301sgolk8P2FdiaKKEfrCsJCb3sZkzJ>

<sup>316</sup> Openreach’s WLR prices are presented on an annual basis and so I calculate the monthly equivalent.

<sup>317</sup> [https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates/q2\\_2009](https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates/q2_2009)

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Commitments.<sup>318</sup> Prior to 1<sup>st</sup> April 2018, I consider the competitive benchmark to be the price as at 1<sup>st</sup> April 2018. Since the commitment itself allows for some increases after 1<sup>st</sup> April 2019, I take account of any price changes implemented by BT thereafter based on BT's Consumer Price Guides.<sup>319</sup>

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<sup>318</sup> The line rental price in question is specific to Voice Only Customers as these were the only customers eligible for the automatic price reduction.

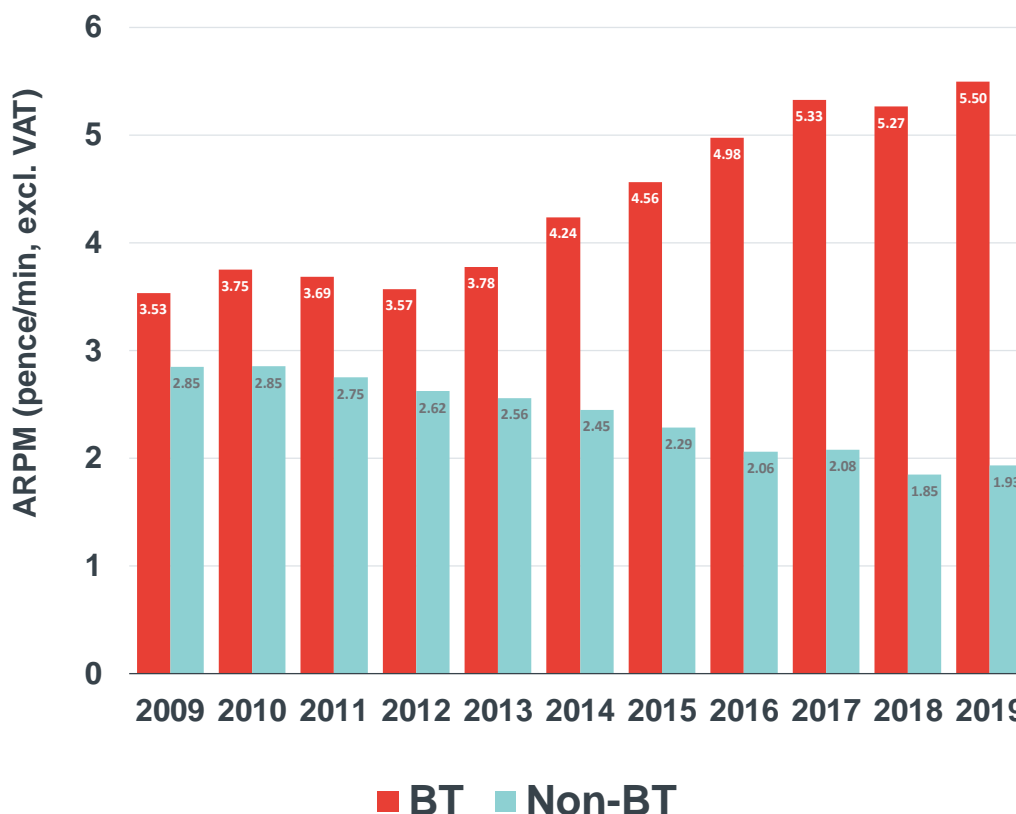
<sup>319</sup> I have relied on archived historical Consumer Price Guides for this information.

## ANNEX B AVERAGE REVENUE PER MINUTE ANALYSIS

472. I have examined the difference in calls ARPMS paid by BT and non-BT customers reflect higher average unit call prices. In order to conduct this analysis, I have relied upon data from Ofcom’s Q4 2019 Telecommunications Market Data Update.<sup>320</sup>

473. Figure 13 and Figure 23 in 7.2.3 and Section 8.4.1 respectively set out an analysis of the ARPM for calls. This showed that BT’s customers paid more for calls than non-BT customers on a weighted per-minute basis across all call types (i.e. a higher average unit call price). This data is repeated in Figure 30 below for ease of reference.

Figure 30 BT vs. non-BT calls ARPMS, 2009 – 2019



Source: Frontier Economics and Ofcom data.

Note: ARPMS do not control for differences in the distribution of call types made by different customers.

<sup>320</sup> See <https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates/telecommunications-market-data-update-q4-2019>

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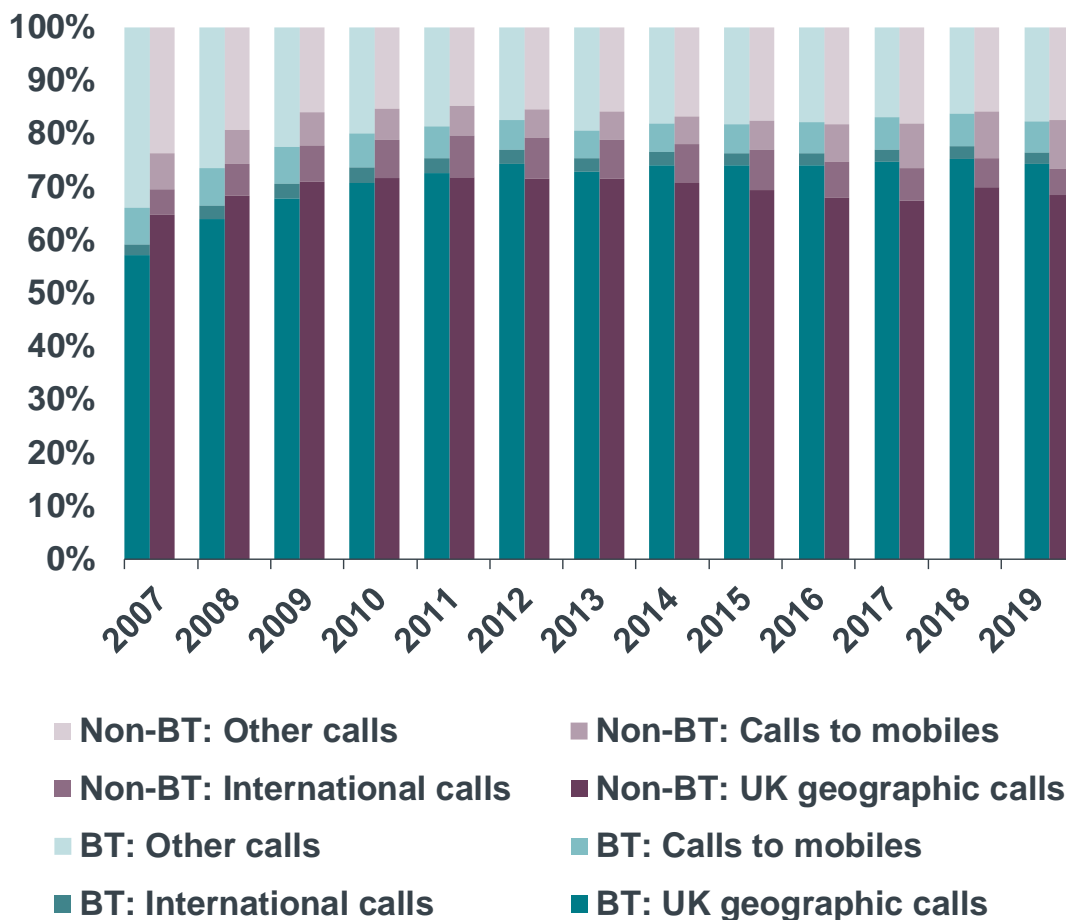
474. The average unit call prices were calculated by dividing total call revenues by total call volumes (in minutes), since no information was available to me regarding the revenues split by call types for different providers.
475. In the absence of further analysis, it is not possible to rule out that at least some of this difference in average unit call prices is explained by differences in the respective call distributions for those customer groups. In other words, if BT customers had, on average, made a higher share of more expensive calls than non-BT customers,<sup>321</sup> that may have been a contributing factor to an overall higher average unit call price.
476. However, the information on the distribution of call types made by voice customers, split between BT and non-BT, over time (Figure 31 below) suggests that this is not the case.

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<sup>321</sup> For example, BT customers may have made far more calls on average to premium rate/international numbers, or more peak rather than off-peak calls.

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**Figure 31 Types of calls made by BT and non-BT operators, 2007 – 2019**



Source: Frontier based on Ofcom data

477. As can be seen in Figure 31 above, the mix of calls made by users is similar for BT and non-BT providers, and has remained so across time.

478. My analysis therefore suggests that BT’s higher ARPMs were likely to have been a result of BT’s call prices being higher than the call prices charged by non-BT providers throughout the Claim Period, rather than due to a distributional effect relating to different usage of different calls types.

## ANNEX C INSTRUCTIONS

### Project Anthony - Instructions for Frontier

1. Mishcon de Reya LLP ("**Mishcon**") has been instructed by Justin Le Patourel (the "**Proposed Class Representative**") to commence opt-out collective proceedings against BT as described below.
2. The Proposed Class Representative will apply for a collective proceedings order ("**CPO**") in respect of claims seeking damages for losses suffered by individual customers of BT Group Plc ("**BT**") (the "**Proposed Class**")<sup>1</sup> as a result of excessive prices charged to them by BT in relation to landline telephony services known as 'standalone fixed voice ("**SFV**") services' in breach of s.18 of the Competition Act 1998 (the "**Chapter II Prohibition**") (the "**Claim**"). The period in respect of which losses are claimed begins on 1 October 2015.
3. The Proposed Class Representative has engaged you to act as an expert adviser with the intention that you shall (a) provide an initial report in support of his application for a CPO and, if the CPO is granted, (b) act as an expert throughout the case, including by producing a final report or reports and potentially giving evidence at trial. The scope of the instructions is set out below.

<sup>1</sup> A detailed definition of the Proposed Class is provided under separate cover.

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4. In summary, this letter sets out instructions for you to provide an expert economic report to the Proposed Class Representative in relation to an application for a CPO to be filed pursuant to Rule 75 of the Competition Appeal Tribunal Rules (the "**Rules**"), to commence opt-out collective proceedings under section 47B of the Competition Act 1998 (the "**CA98**").

### Background

5. In 2017, Ofcom undertook a review of the market for standalone landline telephone services (also referred to as SFV services), directed at residential customers who do not also purchase other non-voice services (such as broadband) in a bundle with their SFV services. The review was undertaken because:

*"Telephone line rental prices have risen between 25-49% between December 2009 and 2016 while the actual cost of providing these services has fallen by up to 26%. As a result, there was concern that Standalone Voice Customers may not be benefitting from competition and paying significantly above cost."*

6. In its final report, published in October 2017, Ofcom found that:

(a) there are two types of customers:

(i) voice-only: customers who bought a SFV service but did not, at the same time, buy a broadband service, either from BT or any other provider; and

(ii) split purchasers: customers who, at the same time, bought both (i) a SFV service; and (ii) a broadband service, either from BT or any other provider;

(b) it had concerns about prices charged to customers in each group;

(c) a significant price cut was important to alleviate the detriment suffered by voice only customers; and

(d) while split purchase customers had suffered increases in line rental charges in recent years without significant offsetting benefits, Ofcom decided to allow time for them to become more actively engaged.

7. In response to Ofcom's findings, BT offered voluntary commitments to Ofcom for a three-year period from April 2018 to reduce the prices it charged to voice only customers.

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### Conflicts

8. You have confirmed that you have no conflicts in acting against BT.

### Your duties

9. You are reminded that it is the duty of the expert to help the Competition Appeal Tribunal ("**CAT**") on matters within your expertise: that duty overrides any obligation to the person from whom you have received instructions or by whom you are paid. Your report should be addressed to the CAT and provide an unbiased, objective opinion as an independent witness in relation to those matters which are within your expertise.

10. Please read carefully the attached documents which further describe your duties to the CAT and the requirements for your Initial Report (as defined below):

(a) The Rules (as defined above), especially rule 4;

(b) The Competition Appeal Tribunal Guide to Proceedings 2015, especially paragraphs 7.65 to 7.70 (which provide guidance on giving expert evidence in the CAT);

(c) The Civil Procedure Rules Part 35;

(d) Practice Direction 35; and

(e) Civil Justice Council, Guidance for the instruction of experts in civil claims, August 2014.

### The CPO application: legal background

11. The CAT will make a CPO under section 47B of the CA98 in respect of claims which are "eligible for inclusion in collective proceedings".

12. According to subsection (6) of that section, claims are eligible for inclusion in collective proceedings "only if the Tribunal considers that they raise the same, similar or related issues of fact or law and are suitable to be brought in collective proceedings."

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13. Rule 79 of the Rules (to which we refer you) sets out three requirements which must be satisfied in order for claims to be certified as eligible for inclusion in collective proceedings, namely:

- (a) the claims must be brought on behalf of an identifiable class of persons (Rule 79(1)(a));
- (b) the claims must raise common issues (Rule 79(1)(b)); and
- (c) the claims must be suitable to be brought in collective proceedings (Rule 79(1)(c)).

14. We also draw your attention to Rule 73(2) which defines:

*“common issues” as meaning “the same, similar or related issues of fact or law”; and “aggregate award of damages” as meaning “an award of damages made by the Tribunal in collective proceedings without undertaking an assessment of the amount of damages recoverable in respect of each represented person”.*

15. We also refer you to Section 6 of the Competition Appeal Tribunal Guide to Proceedings 2015 which elaborates upon the requirements in the Rules; and judgments in respect of previous CPO applications, which address the relevant tests and standards as applied by the CAT: see in particular: *Gibson v Pride Mobility Products Limited* [2017] CAT 9; and *Mastercard Incorporated and others v Walter Hugh Merricks CBE* [2020] UKSC 51 ("**MasterCard v Walter Merricks**"). The Courts also had regard to the judgment of the Canadian Supreme Court in *Pro-Sys Consultants Ltd v Microsoft Corp.* [2013] SCC 57.

### Scope of instructions

16. In the first instance, we are seeking from you an expert report to be filed in support of the Proposed Class Representative’s application for a CPO (the "**Initial Report**").

17. In the Initial Report, we are seeking your views on whether, on the information currently available to you, BT’s prices were excessive and caused harm to the Proposed Class.

18. In particular, your Initial Report should address the following questions in relation to the infringement:

- (a) the scope of the relevant product and geographic markets concerned;

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(b) whether BT held a dominant position within the meaning of the Chapter II Prohibition on the markets which you have identified as relevant; and

(c) whether any of the prices charged by BT to the Proposed Class Members on any relevant market(s) were excessive (based on your understanding of that concept from an economic perspective) and therefore abusive within the meaning of the Chapter II Prohibition. If so, your Initial Report should also identify the amount of any overcharge.

19. In addressing the above, please identify which products provided by BT to Proposed Class Members have been subject to any overcharge(s) which you identify.

20. In relation to the Proposed Class and loss, please give:

(a) an estimate of the total number of persons within the Proposed Class and each sub-class (i.e. voice only customers and split purchaser customers);

(b) an estimate of the proportion of Proposed Class Members resident in England and Wales; and

(c) a preliminary estimate of the total aggregate loss suffered by Proposed Class Members as a result of the infringement.

21. Please indicate, where appropriate, if particular issues which you have identified as material to your economic analysis are common to Proposed Class Members.

22. In giving your views on the above issues, please:

(a) set out your methodology, the evidence relied on and the source of that evidence;

(b) indicate how you would extend this analysis to time periods beyond the date of this report, the evidence required in order to do so, and whether you anticipate any changes in your conclusions for such future periods; and

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## EXPERT REPORT OF DAVID PARKER

(c) set out a detailed methodology of how you intend to advance the analysis in preparation for trial in the event that the CPO is granted, including details of the evidence necessary and desirable in order to do so, and the likelihood that such evidence will be available. This should include the proposed methodology in relation to calculating aggregate damages (for example, whether a 'top-down' or 'bottom-up' approach will be employed).

23. In addition to the preparation of the Initial Report, your work for the CPO application may include:

- (a) reviewing documents provided by us;
- (b) reviewing and potentially providing a report in reply to any expert evidence produced by BT in response to the CPO application;
- (c) potentially giving oral evidence at a hearing of the CPO application; and
- (d) carrying out any other duties appropriate to the role of an expert witness, as directed by the CAT or instructed by us.

24. Furthermore, if the CAT grants a CPO and the Claim proceeds to trial, we will seek to instruct you to provide expert evidence for the trial and any relevant interlocutory applications.

### **Materials supplied**

25. In giving your views on the above issues, please consider the following documents which we have already provided to you:

- (a) “The review of the market for standalone landline telephone services, Provisional conclusions”, Consultation, Ofcom, February 2017 (non-confidential version);
- (b) “The review of the market for standalone landline telephone services – Annexes Provisional conclusions”, Consultation, Ofcom, February 2017 (non-confidential version);
- (c) “Review of the market for standalone landline telephone services”, Statement, Ofcom, October 2017 (non-confidential version);

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(d) “Review of the market for standalone landline telephone services, Evidence supporting the Statement”, Ofcom, October 2017 (non-confidential version); and

(e) Judgment of the Supreme Court in *MasterCard v Walter Merricks*.

**Next Steps**

26. The deadline for sending the Initial Report to the Proposed Class Representative is 7 January 2021.

27. Please let us know if you require any clarification in relation to our instructions, or if you have any questions in relation to your role as an expert in this matter. We look forward to working with you.

Yours sincerely

**Mishcon de Reya LLP**

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**Class definition**

1. The Proposed Class is defined as:
 

“all persons domiciled in the United Kingdom (except in the **Hull Area**) who, during the **Claim Period**, bought a **BT Standalone Fixed Voice Service** except for the **Excluded Services**” (referred to below as “**the Proposed Class**” or “**Proposed Class Members**” as appropriate).
2. For these purposes:
  - (a) **BT Standalone Fixed Voice service** (referred to below as a “**BT SFV Service**”) means any residential landline calling plan service provided by BT, except for the Excluded Services, which (i) includes landline line rental and (ii) has not been sold as part of a bundle with broadband. For these purposes, a bundle refers to a contract, or two or more closely related, linked or interdependent contracts which, individually or together, include and require the purchase of broadband, or other non-voice services, as well as the landline calling plan service.
  - (b) **Excluded Services** means BT Basic and BT Home Phone Saver.
  - (c) **Hull Area** means the area defined as the Licence Area in the licence granted on 30 November 1987 by the Secretary of State under Section 7 of the Telecommunications Act 1984 to Kingston upon Hull City Council and Kingston Communications (Hull) plc.
3. The Proposed Class is split into two Proposed Sub-classes, namely:
  - (a) **BT Voice Only Customers:** Members of the Proposed Class who, during the applicable Claim Period as defined below, bought a BT SFV Service but did not, at the same time, buy a broadband service, either from BT or any other provider.
  - (b) **BT Split Purchase Customers:** Members of the Proposed Class who, during the applicable Claim Period as defined below, have bought at the

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same time both (i) a BT SFV Service; and (ii) a broadband service, either from BT or any other provider.

4. The **Claim Period** means:
- (a) for residential BT Voice Only Customers, between 1 October 2015 and 1 April 2018 inclusive;
  - (b) for business BT Voice Only Customers, between 1 October 2015 and the date of the Tribunal's final determination of the Claims made by the Sub-class of BT Voice Only Customers or their earlier settlement (or settlement of any part thereof); and
  - (c) for BT Split Purchase Customers, between 1 October 2015 and the date of the Tribunal's final determination of the Claims by the Sub-class of BT Split Purchase Customers or their earlier settlement (or settlement of any part thereof).

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## **ANNEX D CURRICULUM VITAE**

### David Parker



Director

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David advises companies facing competition investigations in relation to agreements, abuses of dominance, market studies and investigations and mergers, across many national and supra-national jurisdictions, and in relation to state aid. He has led Frontier's work on a large number of detailed market studies and investigations across many different areas.

His expertise covers an extremely wide range of sectors, including financial services, retailing, energy, transport, telecoms, media, online platforms and retailers, agricultural products, FMCG products, chemicals, petrochemicals, health services, pharmaceuticals, and postal services.

David provides expert advice in litigation and arbitration cases, in particular in relation to standalone and follow-on damages cases arising from breaches of competition law and appeals against regulatory decisions. He has given expert evidence in several courts and tribunals, including the England and Wales High Court, the Competition Appeal Tribunal, the Northern Ireland High Court, the Ireland High Court, the First Tier Tax Tribunal, the London Court of International Arbitration and the Milan Court of Appeal.

David was recognised as one of Who's Who Legal's "Global Elite Thought Leaders" for Competition Economics in 2019.

### Experience

#### Competition

#### UK competition inquiries

Selected experience includes:

- Facebook/GIPHY (CMA, 2020)
- Amazon/Deliveroo (CMA, 2020)
- Credit reference agency market study (FCA, 2019-)
- Digital advertising market study (CMA, 2019-2020)
- Quidco/TopCashback (CMA, 2019)

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- Funerals (CMA, 2019-)
- Sainsbury's/Asda (CMA, 2018-19)
- Meadow Foods/Roilvest (CMA, 2018)
- Experian/ClearScore (CMA, 2018-19)
- SSE/npower (CMA, 2018)
- Investment consulting market study (CMA, 2017-18)
- Zoopla Property Group/Money.co.uk (CMA, 2017)
- Zoopla Property Group/Expert Agent (CMA, 2017)
- FirstGroup, acquisition of South West Trains rail franchise (CMA, 2017)
- Tesco/Booker (CMA, 2016-2017)
- Just Eat/Hungryhouse (CMA, 2016-2017)
- AMC Cinemas/Odeon (CMA, 2016)
- Asset management (FCA, 2016)
- FirstGroup, acquisition of TransPennine Express rail franchise (CMA, 2015-2016)
- FirstGroup, review of SBH undertakings (CMA, 2015-2016)
- Implications of Plevin judgment (FCA, 2015)
- Payment systems infrastructure (PSR, 2015)
- Indirect access to payment systems (PSR, 2015)
- Booker/Musgrave (CMA, 2015)
- Stagecoach/ InterCity East Coast (CMA, 2015)
- Poundland/99p Stores (CMA, 2015)
- Stepstone/Evenbase (CMA, 2014)
- Eurotunnel remittal (CMA, 2014)
- Micronclean/Guardline (CMA, 2014)
- FirstGroup/Essex Thameside rail franchising bid (CMA, 2014)
- FirstGroup/Caledonian Sleeper rail franchising bid (CMA, 2014)
- FirstGroup/Thameslink, Southern and Great Northern rail franchising bid (CMA, 2014)
- FirstGroup/Scotrail rail franchising bid (CMA, 2014)
- FirstGroup/InterCity East Coast rail franchising bid (CMA, 2014)
- TNT Post (Whistl) vs. Royal Mail (Ofcom, 2014-18)
- Retail energy market investigation (CMA 2014-)
- Retail banking market investigation (CMA 2014-)



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- Landmark/DIIG (OFT, 2013)
- ICT services to UK Government (OFT, 2013)
- Consultation on consumer credit regulations (FCA, 2013)
- Review of divestment of TSB from Lloyds (OFT, 2013)
- Web Reservations International/Hostelbookers (OFT, 2013)
- Tesco/Spar (OFT, 2013)
- Vion/2SFG merger (OFT, 2013)
- Private healthcare investigation (CC, 2012-13)
- Motor insurance investigation (CC, 2012-13)
- Booker/Makro merger (OFT/CC, 2012-13)
- Review of First Group/SBH Undertakings (OFT, 2012)
- Aggregates/cement/ready mix concrete investigation (CC, 2012)
- DPG/Zoopla (OFT, 2011-2012)
- Electruepart/eSpares merger (OFT, 2011)
- Review of waste electrical equipment regulations (Private client, 2011)
- Mortgage Brain/Trigoldcrystal merger (OFT, 2011)
- Movies Pay TV investigation (CC, 2010-11)
- Local bus services market investigation (CC, 2010-2012)
- Tesco Onestop – Mills acquisition (OFT, 2010)
- Assessment of dominant position of Royal Mail (Postcomm, 2009)
- Brightsolid/Friends Reunited (CC, 2009-10)
- Local bus services market study (OFT, 2009-10)
- Grocery retailing – remittal following successful appeal (CC, 2009)
- Tesco Barnstaple acquisition (OFT, 2008)
- Tesco Slough acquisition (CC, 2007)
- Grocery retailing (CC, 2006-08)
- Grocery retailing (OFT, 2005-06)
- Somerfield/Morrisons (CC, 2005)
- Home credit (CC, 2005-06)
- Capital Radio/GWR (OFT, 2004)
- Home Credit Supercomplaint (OFT, 2004)
- Domestic bulk liquified petroleum gas (CC, 2004)

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- Drager/AirShields (CC, 2004)
- Landmark/EA Chapter 2 complaint (OFT, 2003)
- Landmark/Sitescope merger (OFT, 2003)
- Asda/Morrisons/Sainsbury/Tesco/Safeway mergers (CC, 2003)
- Mobile termination charges (CC, 2003)
- Tesco/T&S merger (OFT, 2002)
- Extended warranties (CC, 2002)
- Pharmacy Investigation (OFT, 2002)
- Competition Assessment Guidelines (OFT, 2001)
- Neopost/Ascom (CC, 2001)
- Kodak/ColourCare (CC, 2001)
- BSkyB Review (OFT, 2001)
- Napp Pharmaceuticals (OFT, 2001)
- Banking services to Small and Medium Enterprises (CC, 2000)
- Supermarkets (CC, 1999)

### EU and other competition inquiries

Selected experience includes:

- Facebook/Reliance Jio merger (Competition Commission of India, 2020)
- Investigation of Criteo complaint against Facebook (French Competition Authority, 2020-)
- Investigation of Facebook Marketplace (EC, 2020-)
- Link/Pepper (Irish Competition and Consumer Protection Commission, 2020)
- Berendsen/Kings Laundry (Irish Competition and Consumer Protection Commission, 2018-19)
- KMV/Pepsi (Czech Anti-Monopoly Office, 2018)
- Tesco – allegation of hub and spoke behaviour (Hungarian Competition Authority, 2017)
- Kraft/certain sauce brands of Mondelez (Bundeskartellamt, 2017)
- Valero/Topaz (Irish Competition and Consumer Protection Commission, 2016)
- Grocery retailer – supplier relationships (Czech Anti-Monopoly Office)
- Grocery retailer - RPM Allegations (Slovak Anti-Monopoly Office)
- Topaz/Esso (Irish Competition and Consumer Protection Commission, 2015)

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- Holcim/Lafarge merger (EC, 2014-2015)
- Sale of Elverys (Irish High Court, 2014)
- Cyprus LNG public procurement exemption (EC, 2013-)
- Advent/Cytec resins business (EC, 2012-13)
- Caterpillar/MWM (EC, 2010-11)
- Advice on market definition and dominance in Hong Kong TV sectors (Hong Kong Broadcasting Authority, 2011)
- Yara/Terra (EC, 2010)
- Potential retail acquisition (Private client, Polish Competition Authority)
- TNS/GfK merger (EC, 2008)
- Samsung Tesco/Homever (Korean Competition Authority, 2008)
- Mars/Wrigley merger (EC, 2008)
- Advice on digital TV licence applications (BCI, 2008)
- Tesco-Carrefour (Slovakian Competition Authority, 2005)
- GE/Honeywell merger (EC, 2001)
- UPM-Kymmene/Haindl merger (EC, 2001)
- HP/Compaq merger (EC, 2001)
- Merloni/GDA merger (EC, 2001)
- Italian exhibition sector (IAA, 2001)

### Litigation and dispute support

- Facebook vs. Federal Cartel Office (Federal Court of Justice, 2020-)
- Ofcom vs. Royal Mail (Court of Appeal, 2020-)
- Ryanair vs. LastMinute ( Milan Court of Appeal, 2020-)
- Ryanair vs. Viaggiare (Milan Court of Appeal, 2020-)
- Ryanair vs. Skyscanner (Ireland High Court, 2020-)
- Justin Gutmann vs. FirstGroup (Competition Appeal Tribunal, 2019-)
- Achilles vs. Network Rail (Competition Appeal Tribunal, 2019)
- Ofcom vs. Royal Mail (Competition Appeal Tribunal, 2019)
- Durham Company vs HMRC (Upper Tribunal, 2017-)
- Tesco vs. Visa (Competition Appeal Tribunal, 2017)
- Pride Mobility Scooters vs. Dorothy Gibson (Competition Appeal Tribunal, 2016)
- Choice vs. Post Office Limited (High Court, 2016)

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- Dunnes Stores Ltd. Vs. Peninsula Securities Ltd (NI High Court, 2016)
- Gascoigne Halman vs. Agents' Mutual (E&W High Court/Competition Appeal Tribunal, 2016-2017)
- Lloyds Banking Group vs. Inara (E&W High Court, 2016)
- Tesco vs. High Peak (E&W High Court/Competition Appeal Tribunal, 2016)
- Cool Milk vs. Department of Health (E&W High Court, 2014)
- Begas vs. Sonatrach (International Court of Arbitration, 2013-14)
- Avon vs. HMRC (First Tier Tax Tribunal, 2013)
- Recolight et al vs. CEF/EWRG (E&W High Court, 2011-12)
- Appeal of Ofcom's decision on Sky Sports (Premier League, Competition Appeals Tribunal, 2011)
- Secretary of State for Health and Others vs. Servier (E&W High Court, 2010-)
- Follow-on damages assessment from a finding of abuse of dominant position (EWS, Competition Appeals Tribunal, 2009)
- Appeal of Irish Competition Authority Decision (Kerry/Breeo, Irish High Court, 2009)
- Support for potential action of likely damages following OFT abuse finding (Private client, E&W High Court, 2008-09)
- Support for assessment of likely damages following potential cartel finding (Private client, E&W High Court, 2008-09)
- Secretary of State for Health and Others vs. Reckitt Benckiser (E&W High Court, 2008-2010)
- Groceries sector appeal (Tesco, Competition Appeals Tribunal, 2008)
- Follow-on damages assessment from a finding of abuse of dominant position (Competition Appeals Tribunal, 2008)
- The economics of lotteries (International Court of Arbitration, 2004-2008)
- Vitamins cartel – damages assessment (Competition Appeals Tribunal, 2004)
- Generic pharmaceuticals – assessment of cartel damages (High Court, 2004)
- GE/Honeywell appeal (Court of First Instance/Court of Justice of the European Union, 2002-04)
- Supermarket loyalty schemes – assessment of damages (High Court, 2002-03)
- Abolition of Resale Price Maintenance on Medicaments (OFT, 2000)

### UK regulatory reviews

- Manchester Bus Franchising (Private Client, 2019)
- Review of competition issues in rail franchising bids (Rail Delivery Group, 2015)

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- Revision of WEEE regulations (BIS, 2014)
- Response to consultation on consumer credit (FCA, 2013)
- MailSort Lite (Postcomm, 2009)
- Isle of Grain change of use application (Ofgem, 2004)
- Review of charge controls for mobiles (OFTEL, 2001)
- UK rolling stock market (ORR 1998)
- Application for a gaming licence for the Ritz casino (GBGB 1998)
- Options for a value for money assessment of the ORR (NAO 1997)

### Other regulatory reviews

- Training course in assessing significant market power (EETT, 2002)
- Assessment of SMP (National telecoms operator, 2002)

### State aid

- Circle/Rushcliffe CCG (E&W High Court, 2020)
- Siemens/Alstom (European Commission 2003, private client)

## Career

2012 – present	Director, Frontier Economics
2010 – 2011	Associate Director, Frontier Economics
2003 – 2009	Manager, Frontier Economics
1999 – 2002	Consultant, Frontier Economics
1997 – 1998	Consultant, London Economics

## Education/ academic background

1995 – 1997	MPhil Economics, Oxford University
1992 – 1995	BA Economics, 1 <sup>st</sup> Class, University of Exeter

## Publications

- F. Bruni and D. Parker, “Attention Oligopoly: Comments on the paper by Prat and Valletti”, Competition Policy International Antitrust Chronicle, April 2019.

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- J. Hausman and D. Parker, “Margin-Concentration Analysis In The UK Groceries Inquiry”, *Journal of Competition Law and Economics*, 2010, Volume 6 Issue 3, p687-704
- D. Parker, “Illustrative Price Rises from Mergers in Differentiated Products Markets”, *Global Competition Policy*, April 2009
- R. O’Donoghue and D. Parker, “The Final Piece in the Jigsaw: An Analysis of the Draft European Commission Guidelines on Non-Horizontal Mergers”, *eSapience Center for Competition Policy*, March 2007.
- D. Parker “A screening device for tacit collusion concerns”, *European Competition Law Review*, 2006, Issue 8, p424-433,
- Z. Biro and D. Parker “A new EC merger test? Dominance v Substantial Lessening of Competition”, *Competition Law Journal*, Volume 1 Issue 2, 2002, p157-166.

## ANNEX E DATA REQUIREMENTS AND AVAILABILITY

479. This annex consolidates the additional data needed to:
- 479.1. further refine the assessment of dominance and abuse; and/or
  - 479.2. more accurately estimate class size, the quantum of total damage, and the damage for individual Class and Proposed Sub-class members.
480. My current assessment of damage is from 1 October 2015 to 31 October 2020. However, given that the damage is on-going for some Proposed Sub-class members, this assessment will subsequently need to be updated depending on the timing of these proceedings. While my methodology will be largely the same even as the time period is extended, the data needs will expand as time progresses.
481. Accordingly, while the time-period for which I would need the data has been indicated, it will only be possible able to identify the exact period for which data is required subsequently.
482. At present, the data is restricted to the data BT is expected to hold, either because it relates to BT information, may be available to BT Group through market or competitor research undertaken by BT Retail, or available to BT Group through the wholesale activities of Openreach. Given that it serves the vast majority of this market, I anticipate that the data BT will likely be able to provide should be sufficient to refine the relevant analysis. If this expectation is not correct, third party requests may need to be considered.

### E.1 Data relevant to factual background

483. Full, monthly, price lists for the following BT offerings offered to **Voice Only Customers** – BT Standard Line Rental, BT Line Rental Plus and BT Line Rental Saver. The price lists should cover each month in the Claim Period.<sup>322</sup>
484. Full, monthly, price lists for the following BT SFV access products offered to **Split Purchase Customers** – BT Standard Line Rental, BT Line Rental Plus and BT Line Rental Saver. The price lists should cover each month during the Claim Period.<sup>323</sup>

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<sup>322</sup> Para. 63.1

<sup>323</sup> Para. 63.2

## E.2 Data relevant to the dominance assessment

### E.2.1 Market for SFV services to Voice Only Customers

#### Market shares – access component

485. Data to estimate monthly BT market shares by volume for SFV access from Q2 2017. In particular:<sup>324</sup>

485.1. Monthly volume of the access component of SFV services i.e. number of lines (specifically for Standard Line Rental, Line Rental Saver, Line Rental Plus and Home Phone Saver ) sold to Voice Only Customers by BT from 1 April 2017 to 1 April 2018.

485.2. Monthly volume of the access component of SFV services i.e. number of lines sold to Voice Only Customers by rivals from 1 April 2017 to 1 April 2018, or estimates thereof.

486. Data to estimate BT market shares by revenue for SFV access (excluding BT Basic):

486.1. Annual revenues from BT Voice Only Customers for the SFV access component (excluding BT Basic) from 2015 to 2018.<sup>325</sup>

486.2. Annual revenues from rivals' Voice Only Customers for the SFV access component from 2015 to 2018.<sup>326</sup>

#### Market shares – calls component

487. Data to estimate monthly BT market shares by volume for SFV calls by Voice Only Customers (excluding customers of BT Basic) from 2015 to 2018:

487.1. Annual volume (number of minutes) of calls made by BT Voice Only Customers (excluding customers of BT Basic) from 2015 to 2018.<sup>327</sup>

487.2. Annual volume (number of minutes) of calls made by Voice Only Customers of rivals from 2015 to 2018.<sup>328</sup>

488. Data to estimate BT market shares by revenue for Voice-only SFV calls from 2015 to 2018 (excluding calls by BT Basic customers):

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<sup>324</sup> Para. 208

<sup>325</sup> Para. 217.3

<sup>326</sup> Para. 217.4

<sup>327</sup> Para. 217.1

<sup>328</sup> Para. 217.2



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- 488.1. Annual revenues from BT Voice Only- Customers for the SFV calls component (excluding BT Basic) from 2015 to 2018.<sup>329</sup>
- 488.2. Annual revenues from rivals' Voice Only Customers for the SFV access component from 2015 to 2018.<sup>330</sup>

### Pricing and profitability

489. Total revenues and total volumes of calls made by Voice Only Customers of SFV services for each year between 2015 to 2018, for both BT (excluding BT Basic) and rivals.<sup>331</sup>
490. BT's annual gross margins from 2015 to 2018 for:<sup>332</sup>
- 490.1. the access component of SFV services sold to Voice Only Customers by product (excluding BT Basic); and
- 490.2. the calls component of SFV services for Voice Only Customers by product (excluding BT Basic).

## E.2.2 Market for SFV services to Split Purchase Customers

### Market shares – access component

491. Data to estimate monthly BT market shares by volume for the access component of SFV services:<sup>333</sup>
- 491.1. Volumes (as measured by the number of lines) for the access component of SFV services by product (specifically, for Standard Line Rental, Line Rental Saver, Line Rental Plus and Home Phone Saver) sold to Split Purchase Customers by BT from 1 April 2017 to 1 April 2018, on a monthly basis.
- 491.2. Volumes (as measured by the number of lines) of the access component of SFV services sold to Split Purchase Customers by rivals from 1 April 2017 to 1 April 2018, on a monthly basis.
492. Data to estimate BT market shares by revenue for SFV access products sold to Split Purchase Customers from 2015 (excluding BT Basic):

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<sup>329</sup> Para. 217.5

<sup>330</sup> Para. 217.6

<sup>331</sup> Para. 238

<sup>332</sup> Para. 243

<sup>333</sup> Para. 253

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492.1. Annual revenues from BT Split Purchase Customers of the SFV access component (excluding BT Basic) from 2015 to 2020.<sup>334</sup>

492.2. Annual revenues from rivals' Split Purchase Customers of the SFV access component from 2015 to 2020.<sup>335</sup>

### Market shares – calls

493. Annual volume (number of minutes) of calls made by BT Split Purchase Customers (excluding customers of BT Basic) from 2015 to 2020.<sup>336</sup>

494. Annual volume (number of minutes) of calls made by Split Purchase Customers of rivals from 2015 to 2020.<sup>337</sup>

495. Annual revenues from BT Split Purchase Customers of the SFV calls component (excluding BT Basic) from 2015 to 2020.<sup>338</sup>

496. Annual revenues from rivals' Split Purchase Customers of the SFV access component from 2015 to 2020.<sup>339</sup>

### Pricing and profitability

497. Total revenues and volumes of calls made by BT Split Purchase Customers of SFV services (excluding BT Basic) for each year between 2015 to 2020.<sup>340</sup>

498. BT's annual gross margins from 2015 to 2020 for:<sup>341</sup>

498.1. SFV access component options sold to Split Purchase Customers (excluding BT Basic)

498.2. the calls components of SFV services for the Split Purchase Customers (excluding BT Basic).

## E.3 Data relevant to abuse and overcharge

### Price data

499. Full, monthly, price lists for 2008 and 2009 for the following BT offerings offered to **Voice Only Customers** – BT Standard Line Rental, BT Line Rental

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<sup>334</sup> Para. 259.3

<sup>335</sup> Para. 259.4

<sup>336</sup> Para. 259.1

<sup>337</sup> Para. 259.2

<sup>338</sup> Para. 259.5

<sup>339</sup> Para. 259.6

<sup>340</sup> Para. 268

<sup>341</sup> Para. 269

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Plus and BT Line Rental Saver. The price lists should cover each month during the Claim Period.<sup>342</sup>

500. Full, monthly, price lists for 2008 and 2009 for the following BT SFV access products offered to **Split Purchase Customers** – BT Standard Line Rental, BT Line Rental Plus and BT Line Rental Saver. The price lists should cover each month during the Claim Period.<sup>343</sup>

### Cost data

501. Estimates for the non-WLR variable cost per line, on a robust and verifiable methodology, for provision of the following BT Residential SFV access offerings:<sup>344</sup>

- 501.1. Standard Line Rental;
- 501.2. Line Rental Saver; and
- 501.3. Line Rental Plus

This data should be provided on a monthly basis for 2008 and 2009, and from 1 October 2015 to date.<sup>345</sup>

502. Gross margin for the above products in 2008 and 2009. The data should be provided separately for Voice Only and Split Purchase Customers if the costs of provision to the two groups differ.<sup>346</sup>

### Potential rebalancing between access and calls

503. Data on revenues and volumes of calls made by BT Voice Only Customers of Standard Line Rental, Line Rental Saver and Line Rental Plus for each year between 2015 to 2018.<sup>347</sup>

504. Data on revenues and volumes of calls made by BT Split Purchase Customers of Standard Line Rental, Line Rental Saver and Line Rental Plus for each year between 2015 to 2020.<sup>348</sup>

505. BT's annual gross margins from 2015 to 2018 for:<sup>349</sup>

- 505.1. SFV access offerings sold to Voice Only Customers, in particular:

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<sup>342</sup> Para. 293.1

<sup>343</sup> Para. 293.2

<sup>344</sup> Para. 298

<sup>345</sup> Para. 299

<sup>346</sup> Para. 300

<sup>347</sup> Para. 345.1

<sup>348</sup> Para. 345.2

<sup>349</sup> Para. 345.3

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- 505.1.1. Standard Line Rental;
- 505.1.2. Line Rental Saver; and
- 505.1.3. Line Rental Plus
- 505.2. the calls components of SFV services for the Voice Only Customers of the above offerings.
- 506. BT's annual gross margins from 2015 to 2020 for: <sup>350</sup>
  - 506.1. SFV access offerings sold to Split Purchase Customers, in particular:
    - 506.1.1. Standard Line Rental;
    - 506.1.2. Line Rental Saver; and
    - 506.1.3. Line Rental Plus
  - 506.2. the calls components of SFV services for the Split Purchase Customers of the above offerings.

### E.4 Data relevant to damage assessment

- 507. For each month between October 2015 and March 2018 (both inclusive), the number of BT **Voice Only** Customers on each of the following BT SFV access component offerings: <sup>351</sup>
  - 507.1. Standard Line Rental;
  - 507.2. Line Rental Plus; and
  - 507.3. Line Rental Saver.

For each offering, the number of known business users of these offering should be provided separately for each month. To the extent that BT has any information on whether these customers were VAT registered, this should be provided as well.

- 508. For each month from (and including) October 2015 to date, the number of **Split Purchase Customers** on each of the following BT SFV access component offerings: <sup>352</sup>
  - 508.1. Standard Line Rental;
  - 508.2. Line Rental Plus; and
  - 508.3. Line Rental Saver.

Again, for each offering, the number of known business users of these offerings should be provided separately for each month. To the extent that

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<sup>350</sup> Para. 345.4

<sup>351</sup> Para. 374.1

<sup>352</sup> Para. 374.2

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BT has any information on whether these customers were VAT registered, this should be provided as well.

### E.5 Data relevant to class size

509. Voice Only Sub-class –The total number of **unique Voice Only Customers** that purchased the following BT access offerings between 01/10/2015 up till 31/03/2018 (both inclusive):<sup>353</sup>

- 509.1. Standard Line Rental;
- 509.2. Line Rental Plus; and
- 509.3. Line Rental Saver.

510. Split Purchase Sub-Class – The total number of **unique Split Purchase Customers** that purchased the following BT access offerings product from 01/10/2015 to date: <sup>354</sup>

- 510.1. Standard Line Rental;
- 510.2. Line Rental Plus; and
- 510.3. Line Rental Saver.

### E.6 Additional data

511. I also need the following additional information to assess and verify the initial conclusions as set out in this report. <sup>355</sup>

- 511.1. BT confidential versions of the key Ofcom documents;
  - 511.1.1. “The review of the market for standalone landline telephone services, Provisional conclusions”, Consultation, Ofcom, February 2017 (non-confidential version);
  - 511.1.2. “The review of the market for standalone landline telephone services – Annexes Provisional conclusions”, Consultation, Ofcom, February 2017 (non-confidential version);
  - 511.1.3. “Review of the market for standalone landline telephone services”, Statement, Ofcom, October 2017 (non-confidential version); and

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<sup>353</sup> Para. 426

<sup>354</sup> Para. 428

<sup>355</sup> Para. 219

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511.1.4. “Review of the market for standalone landline telephone services, Evidence supporting the Statement”, Ofcom, October 2017 (non-confidential version).

511.1.5. “Consultation: Protecting voice-only landline telephone customers”, Ofcom, December 2020.

511.2. BT’s s.135 submissions referred to by Ofcom in the above documents;

511.3. Any correspondence relating to BT seeking to alter the Commitments; and

511.4. BT unredacted Consultation responses and correspondence with Ofcom.



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**ANNEX 3**

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# Review of the market for standalone landline telephone services

## Statement

Redacted [X] for publication

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Publication Date: 26 October 2017

## About this document

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This document sets out our conclusions for the market for standalone landline telephone services following our consultation in February.

We had concerns about consumers that buy landline services in a standalone contract and not as part of a bundle with other services such as broadband or pay-TV. In particular, we were concerned about consumers who do not buy fixed broadband, as the market appeared not to be serving them well. We observed that these consumers were experiencing rising prices for line rental, despite falling wholesale costs.

In our February consultation, we proposed regulated price reductions and a requirement for BT to work with us to encourage their customers to consider what better deals were available.

We have now received an offer from BT that matches our proposed regulation for voice-only consumers. Here we set out our consideration of BT's offer.

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# 1. Executive summary

## Strategic context

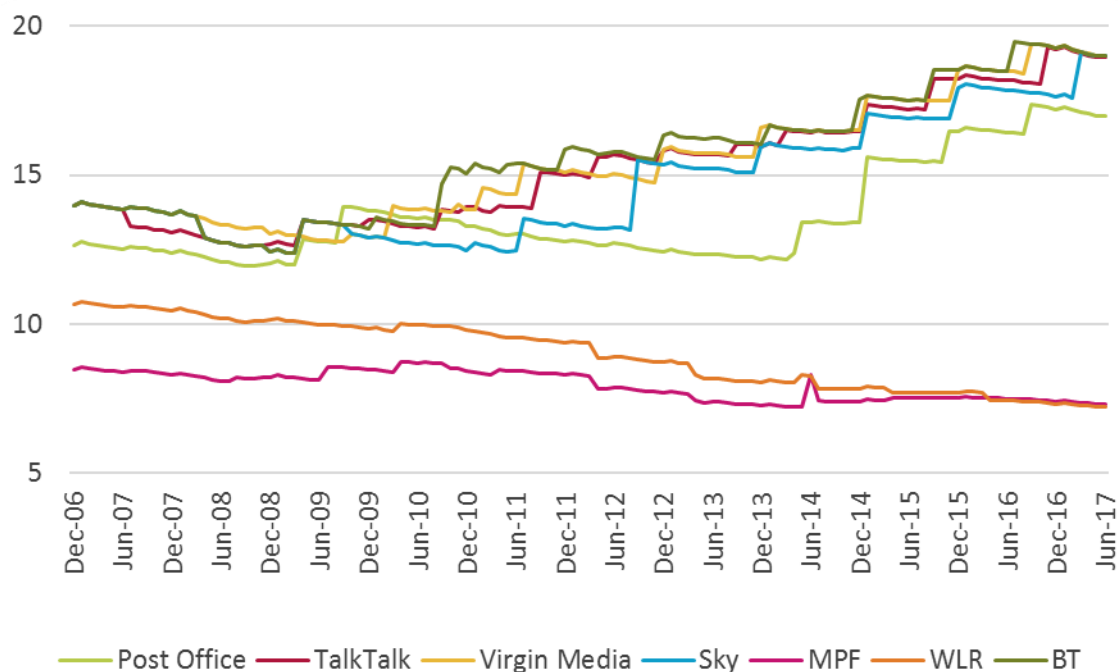
- 1.1 Over the past decade, the landscape for fixed-line telecommunications in the UK has been transformed. Competition has brought new services, increased choice and delivered benefits to consumers.
- 1.2 While there remains a need to continue driving the industry to meet increasing demands for greater quality and reliability, on the whole customers who buy bundled services are getting more for their money than ever before. However, customers that do not take bundled services have not benefited from competition in the same way. In particular, customers purchasing voice-only services – often elderly people who have remained with the same provider for many years – are getting poor value for money. These consumers have less choice of suppliers and are not benefiting from strong price competition or promotional offers. Their loyalty to their provider is not being rewarded but is instead leading to ever higher prices.
- 1.3 As shown in Figure 1 below, line rental prices have increased significantly since 2009. From December 2009 to June 2017, line rental prices rose by between 23% and 47% in real terms. At the same time, the wholesale cost of providing landline services fell by about 27% in real terms.<sup>1</sup>
- 1.4 This fall in wholesale costs has allowed more competitive pricing in the bundled market but voice-only customers have faced price increases without receiving any significant corresponding benefits.

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<sup>1</sup> Wholesale costs are represented by the WLR and MPF lines in Figure 1. These two wholesale products are used by providers to offer retail line rental services to consumers. WLR price fell by 27%.

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Figure 1: Wholesale and retail line rental price movements (£/month at June 2017 prices)



## Our February consultation

- 1.5 On 28 February 2017, we set out our proposals to address the concerns we had identified in the standalone landline telephone services market (February Consultation). This was the first stage in a review process to determine whether or not competition is working well for consumers in the retail market.
- 1.6 We identified two categories of consumers who buy standalone telephone services: voice-only (those who only buy a telephone service and not broadband) and split purchasers (those who buy a telephone service and a broadband service, but not as a bundle). On the basis that telephone providers could not distinguish between these customers we considered it was appropriate to include them all in a single market. We provisionally concluded that BT has significant market power in the provision of services to customers who purchase landline telephone services on a standalone basis.
- 1.7 To address the concerns we identified, we proposed to regulate BT's standalone telephony services through a retail price control, with an initial price cut of between £5 and £7 in monthly line rental, and a basket cap on prices of line rental and calls to limit future price increases to no more than the rate of inflation.
- 1.8 We also proposed to require BT to work with us to trial – and, if appropriate, deliver – consumer information to encourage its standalone telephony customers to look for better value deals in order to promote competition.

## Assessment of markets and measures to address consumer detriment

- 1.9 We have carefully considered both the responses to the February Consultation, and further market research that we published in July 2017.<sup>2</sup>
- 1.10 Since the February Consultation, we have been made aware that providers of standalone telephony services on Openreach's network are in fact able to identify which of their customers are voice-only and which are split purchasers.<sup>3</sup> Therefore, while providers have not so far set different prices (or other terms and conditions) between these two customer groups, they could do so if they wished. Accordingly, we are no longer of the view that voice-only and split-purchase customers should be considered part of the same market.
- 1.11 While we have concerns about the current outcomes for both customer groups, our concerns are more acute for voice-only customers. Voice-only customers generally do not engage with the market: 77% of voice-only customers have never switched provider or considered doing so.<sup>4</sup> They tend to be older and less likely to shop around for a better deal. Over 40% of voice-only customers are at least 75 years old, and 40% live in DE socio-economic group households (for comparison, 55% of dual-play customers are 75 or over, and 20% are in DE group households).<sup>5</sup> Moreover there are now relatively few providers of landline only services for these consumers to choose from.
- 1.12 Even if measures to promote engagement and competition for voice-only customers are successful, they are likely to take time to have an impact (and there are challenges to them being successful, which requires both that voice-only customers engage more actively and also that this stimulates a growth in the existing, limited competition). BT currently holds a dominant position in the market for voice-only customers and the lack of competition enables it to maintain prices above the competitive level.
- 1.13 We therefore consider that a significant price cut is important to alleviate the detriment suffered by voice-only customers. We are also in favour of providing information to consumers, because of the potential benefits in encouraging their engagement in the market and greater competition.
- 1.14 Like voice-only customers, split purchasers have suffered increases in line rental charges in recent years without significant offsetting benefits. However, split purchasers are typically younger and more technologically literate, and, by definition, have internet access which allows them to access alternative offers more easily. Unlike voice-only customers, split purchasers have a wide range of choices available to them, such as dual-play (telephone

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<sup>2</sup> Available at: [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0016/105307/Enriching-understanding-of-Standalone-Voice-Customers.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0016/105307/Enriching-understanding-of-Standalone-Voice-Customers.pdf)

<sup>3</sup> BT has told us that it can seek information from Openreach on a monthly basis to confirm which of their lines are voice-only.

<sup>4</sup> Ofcom switching tracker 2016. Available at: [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0025/95524/Switching-Tracker-2016-Data-tables.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0025/95524/Switching-Tracker-2016-Data-tables.pdf)

<sup>5</sup> Ofcom technology tracker H1 2017. Available at: [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0015/101292/technology-tracker-data-tables-h1-2017.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0015/101292/technology-tracker-data-tables-h1-2017.pdf)

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and broadband) bundles, which should allow them to seek better value for money from providers if they increase their levels of engagement.

- 1.15 To address the detriment faced by split purchasers we have decided that it is more appropriate to allow time for split purchasers to become more actively engaged and potentially switch to dual-play bundles where that is a better option for them, than to include them in a price control at this stage. Split purchasers may benefit from being informed that, in many cases, they are not obtaining good value for money and can find themselves a better deal.

## BT's voluntary proposal

- 1.16 On 24 October 2017 BT put forward a voluntary proposal seeking to address some of the concerns identified in the February Consultation. BT's proposal involves the following commitments for a three-year period in respect of its voice-only customers:
- a) A line rental price reduction of £7 per month (inclusive of VAT) effective from April 2018;
  - b) Raising prices of calls and line rental by no more than inflation (CPI) each year;
  - c) Provision of reporting information to allow Ofcom to monitor its compliance with the voluntary undertaking; and
  - d) A commitment to improve the information available to ensure voice-only customers are aware of possible savings available to them in this market.
- 1.17 BT also proposed to further stimulate engagement by split-purchase customers by issuing an annual statement detailing the total spend of these customers which should help them to consider what alternatives are available for voice alone and in conjunction with their broadband service.
- 1.18 Approximately one million BT voice-only customers will be eligible for the price cut. Around 800,000<sup>6</sup> will receive the price cut automatically on 1 April 2018.<sup>7</sup>
- 1.19 These commitments from BT are in addition to the continued provision of BT Basic, the social tariff for those receiving benefit support.<sup>8</sup>

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<sup>6</sup> Roughly 200,000 customers on BT's 'Home Phone Saver' package could also receive the price cut. Those that don't take broadband (i.e. not split purchasers) can choose to stay on their current package, or move to the standard product being cut, depending on which is the best deal for them.

<sup>7</sup> Home Phone Saver tariff bundles line rental, calls and additional features together in a package and offers a discount of up to £30 against compared to purchasing the features individually at standard prices.

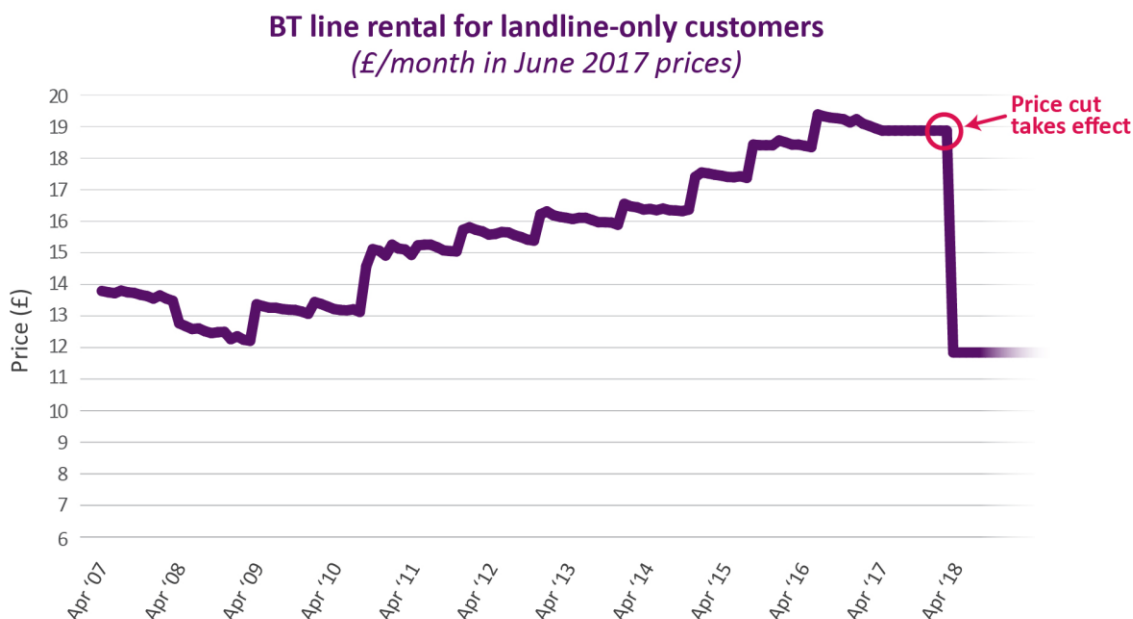
<sup>8</sup> There will be no change to the price of BT's social tariff – BT Basic. This will remain a requirement on BT to provide low-income households on certain benefits access to BT's network at a much reduced price relative to that of standard line rental. It is available to those on Income Support, Income-based Jobseeker's Allowance, Pension Credit, Employment and Support Allowance and those with zero earnings on Universal Credit.

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## Accepting BT's voluntary proposal

- 1.20 We consider that BT's voluntary proposal addresses our concerns over the prices offered to voice-only customers. It brings line rental prices back down to levels last seen in 2009 in real terms, as shown in Figure 2 below. It reverses the trend of recent years for ever higher prices and goes further to ensure that prices are constrained by CPI for the next three years.
- 1.21 BT has also agreed to improve its communications with its voice-only customers to provide information on potential savings and the switching process.
- 1.22 For split-purchase customers, the focus of BT's proposal is now solely on encouraging engagement through an annual statement. We consider that this, plus the absence of a price cut, might encourage them to engage more actively with the deals available in the market for dual-play and other bundles. Additionally, we will be exploring other types of prompts or tools for consumers more generally in our consumer engagement project. We launched this project in July 2017 through a call for inputs.<sup>9</sup>
- 1.23 We therefore consider that BT's voluntary proposal is sufficient to address our concerns in relation to this review. Accordingly, we have decided against the imposition of formal regulation at this time.

Figure 2: BT's line rental prices for voice-only customers: 2007-2018



Source: Ofcom/PurePricing UK Broadband Updates

<sup>9</sup> Available at: <https://www.ofcom.org.uk/consultations-and-statements/category-2/helping-consumers-engage-communications-markets>



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## Next steps

- 1.24 We will monitor closely BT's implementation of its voluntary proposal to cap prices for voice-only customers. If BT fails to deliver on its commitments, we will consider imposing regulatory remedies.
- 1.25 We will work with BT on measures to improve customer engagement in the market for voice-only customers and monitor progress.
- 1.26 We will also monitor the overall impact of BT's voluntary proposal for consumers. Should our monitoring show that consumer detriment remains unaddressed, we will consider intervening in the market.

## 2. Introduction and background

2.1 Our Review of the market for Standalone Landline Telephone Services arose from concerns over the extent to which consumers buying landline telephone services on a standalone basis were missing out on the benefits of competition. Retail prices were rising despite wholesale prices falling in real terms and our review sought, in particular, to investigate whether or not measures were needed to address rising retail prices. We consulted in February on our proposals to impose regulation in relevant retail markets.

### Our concerns leading to this review

2.2 Since 2009, when we removed all regulation on BT in the retail voice telephony markets, many consumers have moved towards buying services in bundles, and this is where we have seen the focus of competition. In 2017, 88% of households reported buying at least two of their communication services in a bundle, with dual-play packages of landline and broadband triple-play packages of landline, broadband and pay-TV being the most popular.<sup>10</sup> This percentage continues to rise.

2.3 Consumers purchasing bundled products have benefitted from competition in terms of prices and choice of products available. Whilst they have, in the past, paid a line rental charge in addition to charges for voice and broadband services, in October 2016, the Advertising Standards Authority (the ASA) issued a ruling requiring communications providers to no longer separate out line rental for bundles.<sup>11</sup> Broadband suppliers' price claims must therefore now show all-inclusive, up-front and monthly costs. Consumers purchasing bundled products including voice services therefore no longer pay a separate line rental charge.

2.4 As part of the Strategic Review of Digital Communications (Strategic Review) we set out our concerns that standalone landline customers have experienced real-terms price increases over the last few years. We also expressed our concerns about the levels of engagement for this market.<sup>12</sup>

2.5 We have gathered evidence that shows competition is not benefiting customers purchasing landline telephone services on a standalone basis (i.e. those that do not purchase bundled products) to the same extent. There are currently 2.6 million households which take landline telephone services outside a bundle, representing 10% of all residential landline users. While the number of such customers is declining over time, it is nevertheless likely to remain significant for the foreseeable future.

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<sup>10</sup> Ofcom technology tracker H1 2017. Available at:

[https://www.ofcom.org.uk/data/assets/pdf\\_file/0015/101292/technology-tracker-data-tables-h1-2017.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0015/101292/technology-tracker-data-tables-h1-2017.pdf)

<sup>11</sup> Advertising Standards Authority, 2016. "Changes to broadband price claims in ads comes into force today",

<https://www.asa.org.uk/news/changes-to-broadband-price-claims-in-ads-comes-into-force-today.html>

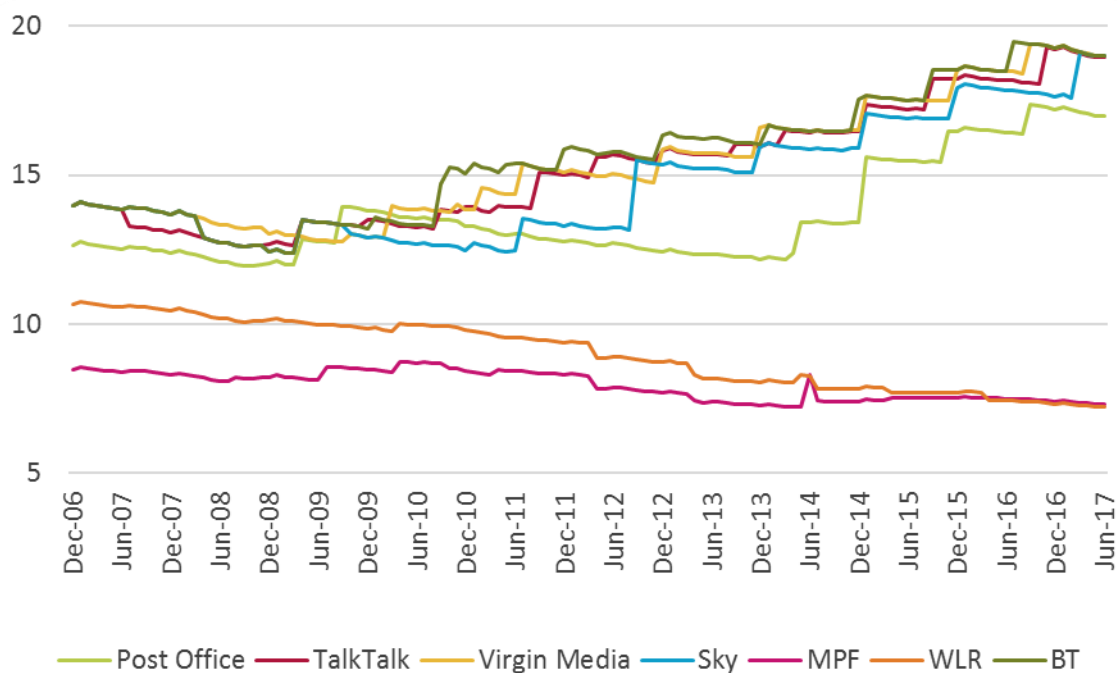
<sup>12</sup> Ofcom Strategic review 2016, Paragraphs 7.9-7.10. Available at:

[https://www.ofcom.org.uk/data/assets/pdf\\_file/0016/50416/dcr-statement.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0016/50416/dcr-statement.pdf)

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2.6 As Figure 3 shows, these customers have been progressively exposed to increasing line rental prices since 2009. This has been occurring despite wholesale charges for products used to provide line rental falling by up to 27% in real terms. Wholesale costs are represented by the WLR (wholesale line rental) and MPF (metallic path facility) lines in Figure 3. These two wholesale products are used by providers to offer retail line rental services to consumers.

**Figure 3: Wholesale and retail line rental price movements (£/month at June 2017 prices)**



Source: Ofcom/Pure Pricing UK Broadband Updates (adjusted for CPI; excludes line rental saver pre-payment tariffs)

- 2.7 Some of the price increases may be due to a rebalancing of prices between line rental and calls as fixed voice call revenues fall due to people making fewer calls, using instead texts, email etc. However, the declining wholesale costs suggest that the price increases are generally not justified by cost increases and communications providers serving this market have been increasing their profitability.
- 2.8 The effect of the increase in line rental prices has a particular impact on elderly consumers. As Figure 4 shows, over 40% of voice-only consumers are over 75.<sup>13</sup> Moreover, this group of consumers is generally more disengaged. Ofcom research has shown that 77% of voice-only customers have never switched providers or considered doing so.<sup>14</sup> These customers are receiving poor value for money given the rising line rental charges which they face.

<sup>13</sup> Ofcom Technology Tracker, H1 2017. Available at:

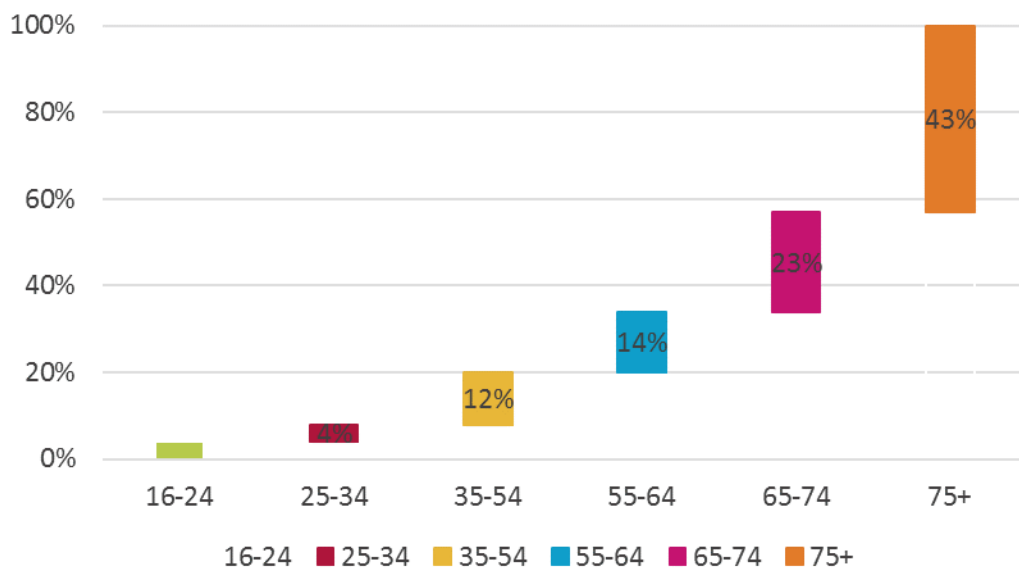
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<sup>14</sup> Ofcom, 2016. *The Consumer Experience 2015*, Research Annex,

[https://www.ofcom.org.uk/data/assets/pdf\\_file/0023/38543/annex.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0023/38543/annex.pdf)

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Figure 4: Residential voice-only consumers by age group



Source: Ofcom Technology Tracker, H1 2017

## Background to this statement

### Retail regulation

- 2.9 Up until 2006, BT was subject to retail price regulation. In 2006, Ofcom<sup>15</sup> decided not to maintain retail price controls.<sup>16</sup> In doing so we recognised, however, that certain groups of vulnerable consumers might require more protection than the average consumer who could switch easily.<sup>17</sup> In particular, we acknowledged that there may be some consumers for whom competition was weaker, leaving them vulnerable to price rises.
- 2.10 In 2009, we concluded that relevant retail markets were effectively competitive and BT no longer held a position of significant market power in those markets. In light of that conclusion, we removed the remaining regulation which applied. We indicated that we would continue to monitor consumers' experience of these services and would intervene, if appropriate in the future.

### Wholesale regulation

- 2.11 Whilst regulation at the retail level has been removed, Ofcom continues to impose regulation requiring BT to offer wholesale products to its competitors to allow them to compete effectively at the retail level. BT has been required to provide wholesale line

<sup>15</sup> Ofcom replaced Oftel as the regulator with responsibility for electronic communications markets from 29 December 2003.

<sup>16</sup> Ofcom, 2006. *Retail Price Controls: Explanatory statement* ("2006 Retail Price Control Statement"), [https://www.ofcom.org.uk/data/assets/pdf\\_file/0012/42114/rpcstatement.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0012/42114/rpcstatement.pdf)

<sup>17</sup> 2006 Retail Price Control Statement, paragraph 1.13.

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rental and wholesale call origination on regulated terms for a number of years and that remains the case.

**February consultation**

- 2.12 In February 2017, we published a consultation on our initial conclusions for this market review (the February Consultation). We provisionally identified a market for standalone fixed voice access and a market for standalone fixed voice calls, both UK-wide excluding the Hull area. We also provisionally concluded that BT held significant market power in both of these markets. To address the consumer detriment we had identified arising from a lack of competition in the markets, we proposed several options for regulation in this market. These included our preferred option of a one-off price cut of between £5-7 on BT's retail line rental price, an ongoing charge control for line rental and calls as well as engagement remedies designed to help customers in this market to be more aware of their options and to potentially switch to better deals in order to stimulate increased competition.
- 2.13 Our consultation ran from 28 February until 9 May. We received 47 responses to this consultation, including 10 responses from organisations and 37 from individuals.

## 3. Market assessment

### Introduction

3.1 In this section we set out the provisional conclusions we reached in the February Consultation and the responses we received. We set out our consideration of the responses and our subsequent position.

### Provisional conclusions in the February Consultation

3.2 Our market review process involves defining markets, assessing whether or not one or more providers holds a position of significant market power in those markets and deciding what regulation, if any is required.

3.3 In the February Consultation, we started by identifying voice-only customers, i.e. those who did not purchase a fixed broadband service at all, as our focal product. 1.5 million customers fall within this group and they are generally older and less likely to shop around for a better deal. Over 40% of voice-only consumers are over-75, and over one-third live in DE socio-economic group households.<sup>18</sup> After identifying the focal product we conducted an analysis of market conditions to determine whether the relevant market should encompass a broader group of customers.

3.4 We went on to consider the position of “split-purchase” customers (i.e. those that purchase landline telephone and broadband services separately, not as part of a bundle). We provisionally found that the market we were interested in included both voice-only customers and split purchasers, primarily on the basis that communications providers have not, to date, price discriminated between them.

3.5 In our consultation, we therefore identified relevant markets for:

- a) The provision of standalone fixed voice access in the UK, excluding the Hull Area. This included sales to voice-only customers and split purchasers and was limited to residential services.
- b) The provision of standalone fixed voice calls in the UK, excluding the Hull Area. As for access, this included sales to voice-only customers and split purchasers and was limited to residential services.

3.6 We provisionally concluded that BT had significant market power in the markets we identified, based on our analysis of market shares, barriers to entry and expansion, pricing, profitability and countervailing buyer power. A significant market power finding meant that we considered that BT can set the terms and conditions of sales without facing significant competitive constraint from other providers.

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<sup>18</sup> Ofcom technology tracker H1 2017. Available at:

[https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0015/101292/technology-tracker-data-tables-h1-2017.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0015/101292/technology-tracker-data-tables-h1-2017.pdf)

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- 3.7 Several stakeholders commented on our provisional conclusions on market definition. TalkTalk agreed with our assessment, while BT, Virgin Media and Post Office disagreed with our assessment in part or entirely.
- 3.8 SSE, Telefonica, Vodafone, TalkTalk, Post Office and the consumer group Which? agreed with our provisional conclusion that BT had SMP in the relevant markets. BT disagreed with our assessment. Stakeholder responses are set out in full on our website.<sup>19</sup>
- 3.9 We address the main points made by stakeholders in the sections below.

**Market assessment****Product market definition**

- 3.10 In light of the comments we received from stakeholders, further information gathering and research we have revised our view of the market.
- 3.11 We no longer consider that it is appropriate to define markets around the purchase of standalone fixed voice access and calls. Rather, we consider that there are separate markets for the purchase of each of access and calls by voice-only customers.
- 3.12 We address separately at the end of this section our views on the position of split purchasers.

**Split-purchase customers are not in the same market as voice-only customers**

- 3.13 BT and Virgin Media did not agree that split-purchase customers were part of the same market as voice-only.
- 3.14 BT argued that if a separate market existed for standalone fixed voice, split-purchase customers should not be part of it. It argued that split purchasers should be in the same market as dual-play as the two groups consumed functionally equivalent services and had similar characteristics in terms of demographics, engagement levels and switching activity.<sup>20</sup> BT also argued that suppliers have strong incentives to attract split-purchase customers to take up their dual play offers.<sup>21</sup>
- 3.15 Virgin Media argued that voice-only and split-purchase customers should be defined in separate markets, as the evidence demonstrates significantly different demographic characteristics, they purchase different communications services and have different levels of engagement.<sup>22</sup>
- 3.16 Both Virgin Media and BT argued that there may be rational reasons why split purchasers choose not to buy a bundle. BT argued that there may be "non-specific price benefits" to

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<sup>19</sup> <https://www.ofcom.org.uk/consultations-and-statements/category-1/review-of-landline-telephone-services>

<sup>20</sup> BT response to February Consultation, 19 May 2017, page 33, paragraph 129.

<sup>21</sup> BT response to February Consultation, 19 May 2017, page 34 paragraph 131 to 134.

<sup>22</sup> Virgin Media response to February Consultation, 17 May 2017, page 4 to 5.

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- consumers, for example the availability of Pay-TV with the broadband supplier.<sup>23</sup> Similarly, Virgin Media explained that services available from two different providers are not identical, for example that a consumer might be satisfied with their fixed voice line provider but switch broadband supplier to achieve a better quality of service.<sup>24</sup>
- 3.17 In the February Consultation, we provisionally concluded that the relevant market included the provision of standalone fixed voice services to both voice-only and split-purchase customers. We noted that up to that point, even where communications providers could easily distinguish between voice-only and split-purchase consumer (in the case where they provided both the standalone broadband and standalone telephone services), they had not done so in terms of the services they offered and there was no obvious intent by communications providers to seek to differentiate services.
- 3.18 Since the February Consultation, we have been made aware that providers of standalone telephone services on Openreach's network are in fact able to distinguish which of their customers take voice-only and which are split purchasers. BT has told us that it can seek information from Openreach, on a monthly basis, to confirm which of its lines are voice-only, and we understand that other providers could obtain similar information from Openreach.
- 3.19 In addition, as noted in paragraph 4.9 below, BT has offered to reduce line rental prices to its voice-only customers but not to split-purchase customers who are buying standalone fixed voice services from BT and broadband from another provider. BT has therefore indicated that not only can it identify which customers are voice-only customers and which customers are not, but it is also able to, and is prepared to, set different prices for voice-only and split-purchase customers.
- 3.20 As we set out in the February Consultation, if there was price discrimination between voice-only and split-purchase customers, it might imply two narrower, separate markets for standalone fixed voice access services, one for voice-only and the other for split purchasers.<sup>25</sup> The OFT market definition guidelines mention that:
- “Where a hypothetical monopolist would (or would be likely to) price discriminate significantly between groups of customers, each of these groups may form a separate market. If so, a relevant market might be defined as sales of the relevant product in the relevant geographic area to a particular customer group”.*<sup>26</sup>
- 3.21 In such circumstances of price discrimination, the two groups of customers would not face a common pricing constraint.
- 3.22 On balance we therefore consider it appropriate to identify a market for standalone fixed voice services to voice-only customers, separate from the provision of standalone fixed

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<sup>23</sup> BT response to February Consultation, 19 May 2017, page 31, paragraph 125 to 128.

<sup>24</sup> Virgin Media response to February Consultation, 17 May 2017, page 8.

<sup>25</sup> February Consultation, paragraph 3.48, footnote 48.

<sup>26</sup> OFT, 2004, Market Definition,

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voice services to split purchasers. In view of communications providers' ability to price discriminate, we no longer consider that voice-only customers and split-purchase customers face a common pricing constraint and, consequently, the two customer groups should no longer be considered as falling within the same relevant market.

### Dual-play services are also not in the same market as standalone fixed voice services bought by voice-only customers

3.23 BT did not agree with our view that dual-play services did not act as a competitive constraint on standalone fixed voice services. It considered that standalone fixed voice services were part of a broader market including dual-play services. In its response to the February Consultation it stated:

*"BT does not agree that there are separate markets for standalone fixed voice services, whether for access or calls; rather there is a wider market for voice services in which BT does not hold SMP.*

*Within this wider market there are pro-competitive explanations for the pricing structure which Ofcom is concerned about. The incremental broadband price has historically been the focus of competitive activity reflecting the significant uptake of bundles ...*

*Firms have therefore prioritised keeping the incremental broadband prices low in order to be able to compete effectively for customers of bundles (which, at 90%, is by far the largest customer segment) rather than using line rental reductions as a means of competing for voice-only customers (which are a much smaller and dwindling group)".<sup>27</sup>*

3.24 BT also said:

*"As the market has evolved to almost ubiquitous take up of bundles, incremental broadband prices have been forced down by competitive pressure. All providers have chosen to offset this, to some degree, through line rental price increases".<sup>28</sup>*

3.25 The Advertising Standards Agency (ASA) has ruled that from 31 October 2016 broadband suppliers' price claims must show all-inclusive, up-front and monthly costs. BT argued that in the future, the ASA ruling will reduce incentives to raise line rental prices, and might also mean providers consider reducing line rental charges to compete for voice-only customers.

3.26 The standard test for whether a product or service constitutes a separate market is whether a hypothetical monopolist supplier of the service could impose a small but significant non-transitory increase in price (SSNIP) above the competitive level without losing sales to such a degree as to make this price rise unprofitable. In the February

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<sup>27</sup> BT response to February Consultation, 19 May 2017, page 4.

<sup>28</sup> BT response to February Consultation, 19 May 2017, page 11.

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Consultation we set out our view that standalone fixed voice access prices are substantially above competitive levels, as they have increased in recent years while costs have fallen.<sup>29</sup>

- 3.27 We also explained that we thought standalone fixed voice services have been highly, and increasingly, profitable. We also noted that the average price of these services has generally been increasing at a faster rate than those of dual-play services (specifically ADSL services).<sup>30</sup> We provisionally concluded that dual-play services are not in the same market as standalone fixed voice services bought by voice-only customers, as standalone fixed voice access prices (and profits) are substantially above competitive levels, which would not be sustainable if they were constrained by competition from dual-play.<sup>31</sup>
- 3.28 While BT argued that price increases for standalone fixed voice services were driven by the nature of dual-play pricing, it did not provide any evidence to contradict our assessment that the presence of dual-play offers had not constrained standalone fixed voice prices to competitive levels. We have updated our analysis of price trends for standalone fixed voice and ADSL services, and the updated figures continue to support our position.<sup>32</sup>
- 3.29 We have considered BT's argument that the ASA ruling will reduce incentives to raise line rental prices, and may lead to lower prices. The ASA announced its intention to introduce its new rules in May 2016 and implemented this in October 2016. After the ASA's announcement BT, Plusnet, TalkTalk, Post Office and Virgin Media each raised the price of line rental by approximately £1. Since implementation, none of the main providers has decreased its price, and Plusnet has increased its price.<sup>33</sup> We consider that the evidence to date does not demonstrate that that, as BT has suggested, the price of standalone fixed voice services would fall materially as a competitive response to the ASA ruling.

**Separate markets for access and calls for voice-only customers**

- 3.30 Post Office did not agree that there were separate markets for standalone fixed voice access and calls. It argued that customers could not easily purchase landline access without calls, as very few providers offered contracts for access only, and neither Post Office or BT did so.<sup>34</sup>
- 3.31 We agree with the Post Office that consumers cannot easily purchase landline access without calls, and that consumers typically purchase a bundle of access and calls. However, on the basis set out in the February Consultation, we remain of the view that there is scope for differences in the competitive conditions between the two, and that for this reason it is appropriate to define them as separate markets.<sup>35</sup>

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<sup>29</sup> February Consultation, paragraph 3.32.

<sup>30</sup> February Consultation, paragraph 3.34.

<sup>31</sup> February Consultation, paragraph 3.38.

<sup>32</sup> Evidence supporting this statement, paragraphs 1.84 - 1.87.

<sup>33</sup> Evidence supporting this statement, Figure 1.26. SSE has also increased its price but it is unclear what proportion is an increase in line rental.

<sup>34</sup> Post Office response to February Consultation, 28 March 2017, page 1.

<sup>35</sup> February Consultation, paragraphs 3.13 – 3.20.

**Review of the market for standalone landline telephone services - statement**

3.32 In any event, whether access and calls are treated as separate markets or as a single market does not fundamentally change our competition assessment.

**Geographic market**

3.33 As set out in our February Consultation, in the UK excluding the Hull Area, we consider that competitive conditions are broadly similar and there is a clear national dimension in competition for standalone fixed voice services. Evidence shows that price is the main mode of competition and communications providers have national uniform pricing policies. Further, we do not have evidence that communications providers compete on non-price elements of voice-only services. Accordingly, we remain of the view that the market for voice-only services is that for the UK excluding the Hull Area.<sup>36</sup>

**Assessment of competition for voice-only customers**

3.34 In its consultation response BT stated that it did not consider that it had significant market power. BT argued that it faces significant competitive pressure and is not able to set the terms and conditions for standalone fixed voice services independently of competitors. It argued that it has responded to competition by investing to improve its products and customer service. For example it launched Home Phone Saver in 2014 – a product that offers a variety of calls and other ancillary services in addition to line rental.<sup>37</sup>

3.35 BT did not consider that market shares provided a good indicator of market power because it considered that there was a wider market in which its market share was much lower, and in that market it did not have significant market power. It argued that Ofcom should have captured standalone fixed voice customers who had switched to dual-play or multi-play in its estimates.<sup>38</sup>

3.36 BT also argued that the standalone fixed voice market segment is rapidly declining due to the migration to dual play bundles. It argued this should be taken into account, and so it was not proportionate to regulate the provision of these services.<sup>39</sup>

3.37 BT's claims about market shares and dual-play bundles mirror its similar arguments on market definition. We have explained above why we disagree with those arguments.

3.38 BT has had a market share of over 70% in the market for standalone fixed voice access to voice-only customers based on number of lines, until 2016 as shown in Figure 3 below. It also a high market share of over 70% for standalone fixed voice calls based on volume.<sup>40 41</sup>

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<sup>36</sup> February Consultation, paragraphs 3.110 to 3.113.

<sup>37</sup> BT response to February Consultation, 19 May 2017, page 5 (paragraphs 16 to 18).

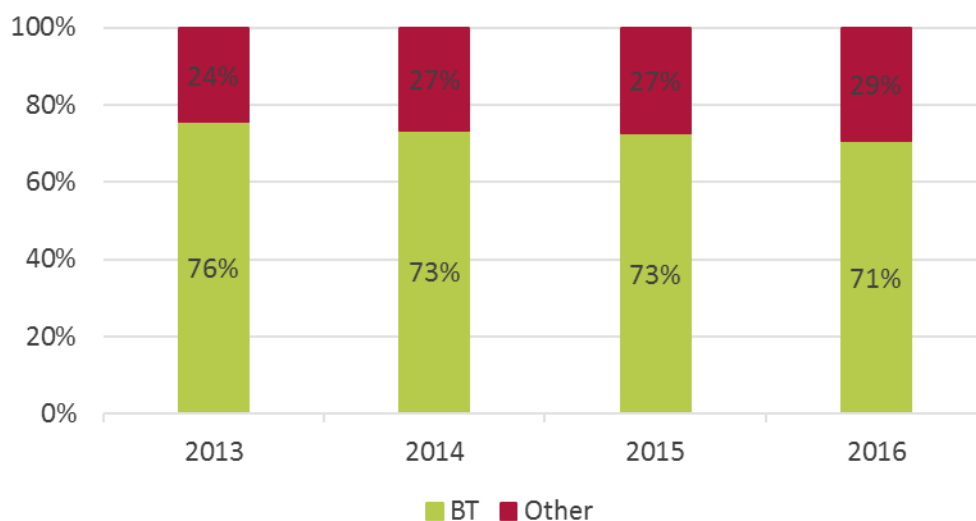
<sup>38</sup> BT response to February Consultation, 19 May 2017, page 17 (paragraph 67).

<sup>39</sup> BT response to February Consultation, 19 May 2017, page 18 (paragraph 69).

<sup>40</sup> Calls market share refers to all standalone fixed voice customers because we do not have any evidence on which to break down standalone fixed voice calls into calls made by voice-only customers and those made by split-purchase customers.

<sup>41</sup> Evidence supporting this statement, table 1.10 and table 1.18.

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**Figure 3: Market shares of voice-only lines by BT and other communications providers**

Source: s.135 responses

- 3.39 Any entrant or smaller player faces high barriers to acquiring customers, limiting its ability to compete effectively. Voice-only customers typically show low levels of engagement and low willingness to switch supplier. There is also evidence that voice-only customers with BT are more brand loyal and less engaged compared to customers of other communications providers.<sup>42</sup> In addition, the relatively small size of the market makes it harder to run an efficient marketing campaign, while online marketing channels are also unlikely to be an effective way of targeting these consumers.
- 3.40 Communications providers expressed similar views on the barriers to entry and expansion in our discussions with them, in their responses to the February Consultation and in evidence provided following the February Consultation. [3] no longer offers standalone fixed voice services to new customers and does not intend to re-enter the market. Others expressed interest in winning more standalone fixed voice customers but noted the high acquisition costs.<sup>43</sup>
- 3.41 BT said that Home Phone Saver was launched in response to competitive pressure from Post Office and other providers. However, in the February Consultation we noted that it enables BT to target more engaged customers that were likely to switch without having to reduce standard prices, which would reduce the revenue it earns from less engaged customers.<sup>44</sup>
- 3.42 BT said that because the market was rapidly declining it would not be proportionate for Ofcom to intervene. However, as the market shrinks acquisition costs are likely to increase, making entry and expansion by other communications providers even more difficult which makes the need for a response more acute.

<sup>42</sup> Evidence supporting this statement, paragraphs 1.123 – 1.142.

<sup>43</sup> Evidence supporting this statement, paragraphs 1.54.

<sup>44</sup> February Consultation, paragraphs 4.63 to 4.66.

**Review of the market for standalone landline telephone services - statement**

- 3.43 As we set out in the February Consultation, despite its decline, we still consider the market material in size and it is not going to disappear in the near future.
- 3.44 Average line rental prices have increased by between 23% and 47% in real terms between December 2009 and June 2017, while the wholesale price of WLR has fallen by 27%.
- 3.45 BT's line rental prices have also generally been higher than those of other communications providers since 2009 [§]. Fixed call volumes have decreased by 55% between Q3 2010 and Q4 2016 and therefore it is possible some of the increase in line rental prices and revenue could be attributed to a rebalancing between line rental and calls. However, across standalone fixed voice customers total revenue per line has increased over the past four years and therefore we do not think that the increase in line rental can be attributed only to rebalancing of access and calls. In the February Consultation, we considered whether the changes in line rental or calls prices could be justified by changes in costs. We provisionally concluded that the cost changes could not explain the price increases.<sup>45</sup>
- 3.46 Additionally, we said there was evidence that BT acted as a price leader. We noted [§].<sup>46</sup>
- 3.47 Our analysis for the February Consultation indicated that BT's profitability per standalone fixed voice line was high and had increased over the period 2007/08 to 2015/16. We estimated that BT's net margin per standalone fixed voice line increased from £[§] per month to £[§] in real terms over the period (based on December 2016 prices).<sup>47</sup> Using the same methodology, we estimate that BT's net margin per standalone fixed voice line in 2016/17 was £[§] per month.<sup>48</sup>
- 3.48 Overall, BT enjoys a significant market share within the markets for voice-only access and calls which have persisted over time. While competition was more intense in the early part of the century. With the movement of the focus of the market to bundles the market has become significantly more static. Competitors face significant barriers to expansion within the market and BT has been able to increase prices above the competitive level. In these circumstances, we do not consider that BT faces any significant constraints on its ability to act independently within the markets for the purchase of voice-only access and calls.

**Split-purchase customers**

- 3.49 As we discussed above, we no longer consider split-purchase customers to be in the same market as voice-only customers. For the reasons set out below, we consider that the consumer detriment identified in the February Consultation in respect of split-purchase customers may be addressed on a different basis to that for voice-only customers. In light of that conclusion, and the position set out in BT's voluntary proposal, we do not consider

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<sup>45</sup> February Consultation, paragraphs 4.60 to 4.62.

<sup>46</sup> February Consultation, paragraph 4.52 and 4.67.

<sup>47</sup> February Consultation, paragraph 4.68.

<sup>48</sup> Additional information provided by BT since the February Consultation suggests that it might be appropriate for us to reduce our estimates of the retail costs per standalone fixed voice line. We estimate that this would increase BT's net margin by £[§] per month.

**Review of the market for standalone landline telephone services - statement**

it necessary to proceed with a more formal market definition exercise in respect of these customers.

- 3.50 In the February Consultation we noted that the availability of competitively-priced dual-play services had not prevented split-purchase customers from experiencing price rises well above costs for standalone fixed voice services. We also took account of differences in demographics and engagement levels of split purchase compared to voice-only customers.<sup>49</sup>
- 3.51 Split-purchase customers pay materially more, for standalone voice and standalone broadband services, than they would pay for functionally equivalent dual-play services.<sup>50</sup>
- 3.52 These customers have also been highly profitable.<sup>51</sup> We explained the outcomes and evidence supported our provisional conclusion that dual-play bundles do not competitively constrain standalone fixed voice prices to split purchasers. Therefore, we did not consider that standalone fixed voice services bought by split purchasers were in the same market as dual-play services. Consultation responses have not provided evidence or arguments to lead us to change our view.
- 3.53 BT also accounts for a very high market share, 97%, of split-purchase lines.<sup>52</sup> We also note that, as for voice-only customers, the declining and relatively small size of the market can make it difficult for communications providers of standalone fixed voice services (both voice-only and split purchase) to target them to encourage them to switch provider. However, there is a much greater choice of dual-play packages which they could adopt. We discuss this further in the next section.

**Summary of conclusions**

- 3.54 Overall, BT's position in the markets for the purchase of voice-only access and calls is consistent with the position we set out in the February Consultation for standalone fixed voice services more generally. BT is the dominant provider of standalone fixed voice services to voice-only customers with around 70% of the market. We consider that the insufficiency of competition in these markets has led to customers being materially worse off and we consulted on a regulatory response to this concern.
- 3.55 However, in light of our concerns BT has agreed to implement voluntary proposals to address those concerns. As set out in the next section, in light of those proposals, we have decided not to proceed with the imposition of regulatory remedies and we therefore do not consider it necessary to reach a formal determination of significant market power with respect to the market for voice-only customers at this time.

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<sup>49</sup> February Consultation, paragraph 3.40.

<sup>50</sup> Evidence supporting this statement, paragraphs 1.88 - 1.93

<sup>51</sup> February Consultation, paragraph 3.41.

<sup>52</sup> Evidence supporting this statement, table 1.14

## 4. Addressing the consumer detriment

### Introduction

4.1 In this section, we set out our conclusions on the market for standalone landline telephone services in light of the market assessment we have made since the February Consultation. We summarise the concerns that we had about voice-only customers, and we set out why we consider that the voluntary proposal that BT has made addresses our concerns.

### Our concerns

- 4.2 Our concerns for this market stem from the fact that line rental prices have been increasing in real terms since 2010, despite falling wholesale charges for products used to provide line rental. Price increases may be due in part to communications providers rebalancing prices as fixed voice call volumes and revenues fall. However, our assessment indicates that the price increases are generally not justified by cost increases and the provision of standalone fixed voice services has become more profitable over this period. Our assessment also identifies a concern that the provision of standalone fixed voice services is not competitive.
- 4.3 In the February Consultation, we set out proposed remedies to address our concerns in respect of the markets for standalone fixed voice access and calls.
- 4.4 Our favoured remedy was a £5-7 monthly reduction to the price of line rental in addition to an obligation to encourage greater consumer engagement in the market through provision of better information to consumers. We considered the range of £5-7 would bring prices closer to cost and so mitigate the consumer detriment but would allow information remedies to encourage consumers to shop around for the best deal and promote competition.
- 4.5 As set out in Section 3 above, we no longer consider it appropriate to define a single market that includes both voice-only and split-purchase customers. We have established since the February Consultation that providers of standalone fixed voice services now have a way to distinguish which of their customers take voice-only and which are split purchasers. Whilst, to date, providers have not yet set different prices, terms or conditions between the two groups, we are now aware that they could do so if they wished.
- 4.6 Voice-only customers, as we discuss in Section 3, have a very limited set of competitive choices, are highly disengaged from the market and have a more limited range of tools, in any event, through which to compare service options (as they generally have less access to the internet).
- 4.7 Unlike voice-only customers, split purchasers have a clear range of choices available to them, such as dual-play bundles, which should allow them to seek better value for money from providers. Split purchasers are typically younger and more technologically literate, and, by definition, have internet access and thus should be better placed to make choices,

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particularly if given the right prompts. Addressing the detriment faced by split purchasers may therefore be most effectively addressed through empowering split purchasers to increase their engagement with offers available from providers. In particular, split purchasers could benefit from being prompted that, in many cases, they are not obtaining good value for money and can find themselves a better deal.

- 4.8 Accordingly, while we continue to view a price cut as essential to addressing our concerns related to voice-only customers, we consider our response to split purchasers should be more strongly focussed on encouraging a behavioural change.

**BT's voluntary proposal**

- 4.9 On 24 October 2017 BT wrote to us with a voluntary proposal to address our concerns in the standalone fixed voice market.
- 4.10 Annex 1 contains the letters exchanged between Ofcom and BT which detail the specifics of BT's voluntary proposal for this market. In summary, for a period of three years for its voice-only customers, BT has committed to:
- a) A line rental price reduction of £7 per month (including VAT);
  - b) Raising prices of calls and line rental by no more than inflation (CPI) each year;
  - c) Provision of reporting information to allow Ofcom to monitor its compliance with the voluntary undertaking; and
  - d) A commitment to work to improve the information available to ensure voice-only customers are aware of possible savings to them in this market.
- 4.11 BT has also proposed to further stimulate engagement by split-purchase customers by sending them an annual statement detailing their total spend which should assist them in considering what alternatives are available for voice alone and in conjunction with their broadband service.
- 4.12 Approximately one million BT voice-only customers will be eligible for the price cut. Around 800,000<sup>53</sup> will receive the price cut automatically on 1 April 2018.<sup>54</sup>
- 4.13 These commitments from BT are in addition to the continued provision of the BT Basic service, the social tariff for those receiving benefit support.<sup>55</sup>

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<sup>53</sup> Roughly 200,000 customers on BT's 'Home Phone Saver' package could also receive the price cut. Those that don't take broadband (i.e. not split purchasers) can choose to stay on their current package, or move to the standard product being cut, depending on which is the best deal for them.

<sup>54</sup> Home Phone Saver tariff bundles line rental, calls and additional features together in a package and offers a discount of up to £30 against compared to purchasing the features individually at standard prices.

<sup>55</sup> There will be no change to the price of BT's social tariff – BT Basic. This will remain a requirement on BT to provide low-income households on certain benefits access to BT's network at a much reduced price relative to that of standard line rental. It is available to those on Income Support, Income-based Jobseeker's Allowance, Pension Credit, Employment and Support Allowance and those with zero earnings on Universal Credit.



## Consideration of BT's voluntary proposal

### Mitigating the price detriment

- 4.14 In the February Consultation, we identified BT as having a position of significant market power in the standalone fixed voice market. We proposed a regulatory condition that a price cut on the standard line rental of between £5-£7 per month would immediately reduce the gap between wholesale costs and retail prices which we had seen emerge over the last few years.
- 4.15 The £7 per month one-off reduction to the line rental charge levied by BT is at the top of that range. This reduction would result in a voice-only customer being £84 better off per year.
- 4.16 We also proposed a regulatory basket price control structure which would limit the ability of BT to increase its charges for line rental and calls beyond the rate of inflation. BT has committed to a basket structure that is almost identical to the remedy we defined in the February Consultation, and has agreed to limit the increases to charges in this basket to no more than CPI in any given year. In addition, BT has committed not to increase the charges for its Home Phone Saver product.
- 4.17 We further note that BT is a price leader in this market. Although the price reduction will not apply to all voice-only customers, if other communications providers' prices are constrained by BT's we expect that BT's competitors will respond to this reduction in BT's line rental prices.

### Addressing low levels of consumer engagement

- 4.18 The evidence we have assessed as part of this project suggests very low levels of engagement for voice-only consumers. Indeed, as we have discussed above in Section 3, low consumer engagement is one of the factors that has contributed to cementing BT's position in the market. We therefore proposed in the consultation to trial and implement engagement remedies to empower consumers and stimulate other providers to compete more vigorously within the market and to win customers.
- 4.19 BT's commitment to trial and deploy engagement remedies within this market takes account of the approach set out in the February Consultation. BT has provided specific commitments on the nature and format of these communications and has volunteered to share information as to their efficacy with Ofcom. We consider that BT's proposals in this area should enable the implementation of consumer information measures which promote competition for the benefit of consumers.
- 4.20 We will work with BT to develop and trial consumer communications for voice-only customers covering the areas we identified in consultation. These communications could act as a prompt to engage, provide information on potential savings and the switching process, and facilitate customers' response to this information. We remain of the view that there is some uncertainty as to the potential effectiveness of these remedies. However, we

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consider there is sufficient merit in further development and trialling to gather evidence on the effectiveness and optimal design of communications in these areas.

**Conclusions**

- 4.21 BT's proposals to cut the price of its line rental by £7 per month for a period of three years and capped at inflation closely meets the regulatory conditions we proposed in our February Consultation. We have therefore decided not to impose such conditions at this time. However, we will monitor BT's adherence to these commitments on price. In order to enable us to do so, BT has agreed to provide Ofcom with information that will allow us to ascertain its compliance with the basket. BT will provide to Ofcom an audited annual report within four months of the financial year end. This will enable Ofcom to monitor BT's compliance with the detail of the pricing commitments which it has made. If our monitoring shows any problems of implementation by BT of its price cut for voice-only customers, we will consider taking appropriate regulatory action.
- 4.22 We will also work with BT on measures it will take to improve customer engagement in the market to ensure voice-only customers. These communications could act as a prompt to engage, provide information on potential savings and the switching process, and facilitate customers' response to this information.
- 4.23 Generally, we will monitor the overall impact of BT's voluntary proposal for voice-only customers. Should our monitoring show that the detriment for those consumers remains unaddressed despite BT implementing these changes, we will consider whether we will need to intervene further in the market in the interests of these consumers.

**Split-purchase customers**

- 4.24 We recognise that split-purchase customers also suffer detriment arising from high prices for voice services, however it is clear that different supply-side conditions exist and there is greater scope for a positive outcome from encouraging this group to re-evaluate their buying choices than is the case with voice-only customers. In particular, the needs of many split-purchase customers could be met, at better value for money, by switching to dual-play packages. There are many communications providers offering competitive dual-play packages.
- 4.25 Following the February Consultation, we undertook some qualitative research to enrich our understanding of standalone fixed voice customers and their potential responses to engagement remedies. Though a small non-representative sample, it suggested a more effective trigger for split-purchase customers to increase their engagement could be through their broadband and/or TV package, rather than their landline.<sup>56</sup>
- 4.26 On balance we consider it is more appropriate to allow time for split purchasers to become more engaged, and potentially switch to dual play where that is a better option for them, rather than including them in a price control at this stage. Our overall intention in this

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<sup>56</sup> The research we commissioned is on our website at: <https://www.ofcom.org.uk/consultations-and-statements/category-1/review-of-landline-telephone-services>

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regard is to empower consumers to make well-informed choices. We recognise that some split purchasers may have specific reasons, such as quality of service, for preferring different providers for their landline and broadband services. Such consumers might make well-informed decisions to remain as split purchasers and not switch to a dual-play bundle. But we consider that there are many split purchasers who are not obtaining good value for money and can find themselves a better deal. For such consumers, three routes to encourage greater engagement and well-informed choices are:

- a) BT's voluntary proposal to provide more information on annual spend and alternatives available;
- b) The fact that they are excluded from the price cut potentially prompting them to re-evaluate; and
- c) Our broader work on improving consumer engagement.

4.27 For split-purchase customers, the focus of BT's proposal is on encouraging engagement through an annual statement. We consider this, plus the absence of a price cut, should encourage them to engage more actively with the deals available in the market for dual-play and other bundles. Additionally, we will also be exploring other types of prompts or tools for consumers more generally in our consumer engagement project. We launched this project in July 2017 through a call for inputs.<sup>57</sup>

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<sup>57</sup> Available at: <https://www.ofcom.org.uk/consultations-and-statements/category-2/helping-consumers-engage-communications-markets>

# A1. BT's voluntary proposal

**Letter from BT to Ofcom, 24 October 2017**



**Jonathan Oxley**  
Ofcom  
Riverside House  
2a Southwark Bridge Road  
London SE1 9HA

**BT Consumer**

Name Marc Allera  
E-Mail [redacted]

By email only to: [redacted]

24 October 2017

Dear Jonathan

**OFCOM'S REVIEW OF THE MARKET FOR STANDALONE FIXED VOICE TELEPHONY SERVICES**

Following recent discussions between BT and Ofcom, the attached document sets out the details of BT's voluntary commitment to reduce the monthly price of its line rental products by £7 (incl. VAT) for fixed voice-only customers from 1 April 2018 and to cap future price increases for these customers' basket of goods at CPI (until 31 March 2021).

BT is committed to assisting voice-only consumers in fully realising the benefits of competition and, indeed, digital inclusion. To this effect, we will work with Ofcom on measures that may work to improve our customers' engagement with the market.

Yours Sincerely,

A handwritten signature in black ink, appearing to read 'M. Allera', written over a light blue horizontal line.

**Marc Allera**  
CEO, BT Consumer

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## **BT's standalone fixed voice commitments**

## Standalone fixed voice: BT's voluntary commitments

### WHEREAS:

- (A) On 28 February 2017, Ofcom launched a consultation “The review of the market for standalone landline telephone services”.
- (B) BT now voluntarily provides the commitments set out below and, in particular, provides the greatest possible price reduction for our true voice only customers consistent with a competitive outcome, alongside measures to stimulate engagement for standalone fixed voice customers. Ofcom acknowledges that these commitments address the issues raised during its consultation process.
- (C) These commitments relate to residential line rental and calls products provided under the BT brand (they do not apply to EE, Plusnet, nor to BT's business products and/or services).

### NOW THEREFORE:

#### 1. General Provisions

- 1.1 BT plc gives Ofcom the commitments below (**BT's Commitments**).
- 1.2 The Annexes to these Commitments shall form part of these Commitments.
- 1.3 Words and expressions used in BT's Commitments shall be interpreted in accordance with Annex A.
- 1.4 References to paragraphs, sections and Annexes shall mean paragraphs and sections of, and Annexes to, these Commitments, unless otherwise stated.
- 1.5 These Commitments shall apply in respect of the whole of the United Kingdom.

#### 2. BT's Price Commitments:

- 2.1 As set out more particularly in Annex B, BT will:
  - 2.1.1 apply on 1 April 2018 a £7 (seven) reduction (including VAT<sup>1</sup>) to the monthly price of standard line rental and line rental plus (**Line Rental** services) for Fixed Voice-Only Customers (as defined in paragraph 2.2 below);
  - 2.1.2 apply on 1 April 2018 an analogous adjustment to the annual charge for Line Rental Saver and ensure that those customers who paid the annual charge before 1 April 2018 benefit from the monthly discount for the remainder of their contract period after 1 April 2018;
  - 2.1.3 not increase the price of its line rental products for Fixed Voice-Only Customers before 1 April 2019 and limit increases for the remaining two years of the commitment period to CPI+2.5%;
  - 2.1.4 cap future price increases of a basket of Line Rental services and call products for Fixed Voice-Only Customers at CPI (up to and including 31 March 2021);

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<sup>1</sup> If the rate of VAT changes, BT's Commitments will not preclude BT from making pricing changes to reflect any such VAT rate change.

2.1.5 not increase the charges for Home Phone Saver customers before 1 April 2021.

2.2 BT's price Commitments will apply to its **Fixed Voice-Only Customers**, which means: residential customers who purchase a Line Rental service under the BT brand<sup>2</sup> and who do not also have a fixed broadband service provided to them, whether by BT or another Communications Provider. BT will take reasonable steps to ensure that only Fixed Voice-Only Customers receive the discount and, in particular:

2.2.1 The price reduction will not apply to BT Basic or Home Phone Saver customers.

2.2.2 The price reduction will not apply to Split Purchase Customers. BT will exclude any standalone voice customers from the price reduction that it has reason to believe buy fixed broadband services, whether from a BT group company or another communications provider. Such customers will be provided with an opportunity to opt back in if BT's information is incorrect.

2.2.3 The price reduction will not apply to business customers. BT will exclude any standalone voice customers from the price reduction that it has reason to believe are business customers. Such customers will be provided with an opportunity to opt back in if BT's information is incorrect.

2.2.4 In respect of 2.2.2 and 2.2.3 above, BT will from time to time provide Ofcom with information relating to the volume of customers impacted and the volume who have received the discount.

### 3. BT's reporting Commitments

3.1 BT will complete and provide to Ofcom the three compliance statements (compliance summary, compliance detail and single change-service X) that were referenced in Ofcom's "Financial reporting for standalone landline telephone services" consultation of 25 April 2017 (template statements included at Annex C) (**Compliance Statements**). The Compliance Statements will be provided annually, within four months of the end of BT's financial year.

3.2 BT will work with Ofcom and the Auditor to agree a mutually acceptable procedure for audit that is proportionate. BT proposes allowing the Auditor to conduct 'agreed upon procedures' testing on the Compliance Statements, as follows:

3.2.1 Ofcom, the Auditor and BT to meet, create and agree the respective tests to be carried out regarding the Compliance Statements.

3.2.2 The Auditor will carry out the testing of the completed Compliance Statements at the end of BT's financial year in 2019, 2020 and 2021 respectively.

3.2.3 The Auditor will issue a letter and a report to Ofcom and BT stating they have carried out testing and provide the results of the tests.

3.2.4 BT will send the Compliance Statements to Ofcom. BT considers the Compliance Statements to be confidential and does not consent to their publication by Ofcom.

### 4. BT's Commitments to increase engagement

4.1 BT's Commitments in this section will apply up to and including 31 March 2021.

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<sup>2</sup> for the avoidance of doubt excluding EE and Plusnet and BT business customers



4.2 BT will provide its Split Purchase Customers (to the extent it has been able to identify such customers) with an annual statement in the form set out in Annex D to this letter.

4.2.1 BT's Split Purchase Customers will be divided into cohorts with the annual statements being distributed across the year.

4.3 For Fixed Voice-Only customers, BT will investigate, using a reasonable number of trials, the form of communication which has the best prospect of success in increasing engagement for these customers. BT commits to working with Ofcom to seek to achieve this.

4.4 BT will in good faith work with Ofcom to seek to finalise the details of trials to its Fixed Voice-Only Customers, subject to the provisions in paragraph 4.4.2 below, the following principles will apply to the trials:

4.4.1 BT commits to trialling and potentially implementing communications that may include:

- 4.4.1.1 Factual information on a customer's current tariff or previous spending;
- 4.4.1.2 Factual information on typical, average or "up to" savings for a given tariff type within the BT portfolio and market wide - provided that this is not inaccurate or misleading and if relevant given market conditions;
- 4.4.1.3 General statements about the switching process – ensuring that this is accurate and reflects the differences between switches occurring on the same and different platforms;
- 4.4.1.4 General calls to action and references to sources of advice, including suggesting contacting family or friends.

4.4.2 Save by the mutual agreement of BT and Ofcom, communications to BT's Fixed Voice-Only Customers will not:

- 4.4.2.1 Promote BT's competitors, their brands, products, offers or the potential savings that might be achieved through switching to a specific competitor;
- 4.4.2.2 Endorse individual digital comparison tools, including individual price comparison websites;
- 4.4.2.3 Denigrate BT's brand, for example in respect of information on customer service performance or inappropriately use BT's brand (including BT's logo);
- 4.4.2.4 Provide individual projections of a customer's future spending;
- 4.4.2.5 Provide information which is inaccurate, misleading or confusing about potential savings or the switching process;
- 4.4.2.6 Include any information, or be sent to any customers, in a manner that BT believes may breach law or regulation.

4.4.3 Metrics for measuring the success of the trials will reflect a range of criteria which may include, for example:

- 4.4.3.1 Actions to optimise use of BT products / services;
- 4.4.3.2 Interactions with third party advice service;
- 4.4.3.3 Movement outside of the Fixed Voice-Only base (e.g. to dual play)
- 4.4.3.4 Churn to competitors;
- 4.4.3.5 Increased likelihood to engage or seek advice;
- 4.4.3.6 Improved perceptions of switching.

## ANNEXES TO BT'S COMMITMENTS

### ANNEX A: DEFINITIONS AND INTERPRETATION

1. For the purposes of interpreting these Commitments:
  - 1.1 Unless otherwise defined herein, words or expressions have the meaning assigned to them in the Communications Act 2003 (as amended);
  - 1.2 Headings and titles shall be disregarded;
  - 1.3 Any word following the terms including, include, in particular, for example or any similar expression shall be construed as illustrative and shall not limit the sense of the words, description, definition, phrase or terms preceding those terms.
  
2. The following terms shall have the following meanings in BT's Commitments including Annexes:
  - 2.1 **Auditor** means the external auditors for BT's regulatory financial statement for the time being appointed by BT
  - 2.2 **Basket** means all Services listed in Annex B provided to Voice Only Customers in the First Relevant Period, the Second Relevant Period and the Third Relevant Period;
  - 2.3 **BT** means British Telecommunications plc, whose registered company number is 1800000, and any of its subsidiaries or holding companies, or any subsidiary of such holding companies, as defined by the Companies Act 2006.
  - 2.4 **CPI** means the index of consumer prices compiled, from time to time, by an agency or public body on behalf of Her Majesty's Government or a government department (which is the Office of National Statistics at this time);
  - 2.5 **Consumer Business Unit** means the business unit of British Telecommunications Plc that is responsible for providing, amongst other things, BT branded retail fixed voice, line and broadband services to residential customers and which, for the avoidance of doubt, does not include Plusnet Plc, EE and BT Business and Public Sector.
  - 2.6 **Controlling Percentage** is to be determined in accordance with paragraph 6 of Annex B part A;
  - 2.7 **Exchange Line** means an access connection between a customer's premises and a local exchange.
  - 2.8 **Exchange Line Service** means a service consisting in the provision by BT's Consumer Business Unit of an Exchange Line to a customer (for the avoidance of doubt excluding services provided by Plusnet, EE and BT Business and Public Sector).
  - 2.9 **Line Rental Charge** means any amount charged by BT's Consumer Business Unit to a Relevant Customer on a monthly basis for Standard Line Rental and Line Rental Plus, excluding:
    - 2.9.1 any incremental charge made for the provision of Voice-Call Services by BT
    - 2.9.2 any Exchange Line installation charges;
    - 2.9.3 the Home Phone Saver Charge and any element or variant thereof;
    - 2.9.4 Line Rental Saver Charge and any element thereof;
    - 2.9.5 BT Basic;
  - 2.10 **Line Rental Saver Charge** means any amount charged by BT at its commercial discretion to Relevant Customers for the provision of Exchange Line Services where such amount is subject to a discount related to the making of an upfront payment for the service;

- 2.11 **Line Rental Plus Charge** means any amount charged by BT at its commercial discretion to Relevant Customers for the provision of Exchange Line Services where customers choose not to pay by direct debit, which also includes additional features.
- 2.12 **Ofcom** means the Office of Communications as established pursuant to section 1(1) of the Office of Communications Act 2002.
- 2.13 **Percentage Change** is to be determined in accordance with paragraph 5 of Annex B, part A;
- 2.14 **Prior Period** means each of the following three periods:
- 2.14.1 in relation to the First Relevant Period, the period beginning on 31 March 2017 and ending on 1 April 2018;
  - 2.14.2 in relation to the Second Relevant Period, the First Relevant Period;
  - 2.14.3 in relation to the Third Relevant Period, the Second Relevant Period;
- 2.15 **Prior Period Weighted Average Charge** is to be determined in accordance with the relevant formula in paragraph 5 of Annex B, part A;
- 2.16 **Relevant Customers** means Fixed Voice-Only Customers as defined at paragraph 2.2;
- 2.17 **Relevant Period** means each of the following three periods:
- 2.17.1 the twelve-month period 1 April 2018 and ending on 31 March 2019 (the “**First Relevant Period**”)
  - 2.17.2 the twelve-month period beginning on 1 April 2019 and ending on 31 March 2020 (the “**Second Relevant Period**”)
  - 2.17.3 the twelve-month period beginning on 1 April 2020 and ending on 31 March 2021 (the “**Third Relevant Period**”);
- 2.18 **Relevant Period Weighted Average Charge** is to be determined in accordance with the relevant formula in paragraph 5 of Annex B, part A;
- 2.19 **Service** means any of the products and / or services listed in Annex B: part 2
- 2.20 **Split Purchase Customers** means customers who buy fixed voice services and also buy fixed broadband from the same or another supplier outside a bundle.
- 2.21 **Voice-Call Service** means a service that allows a customer to make voice calls using an Exchange Line.

**ANNEX B - PART 1: OPERATION OF PRICE COMMITMENTS**

1. BT shall ensure that in each **Relevant Period** its **Line Rental Charge** does not exceed the **Line Rental Charge Ceiling** for that period.
2. The **Line Rental Charge Ceiling** is:
  - a. £11.99 monthly (including VAT<sup>3</sup>) for the **First Relevant Period for Standard Line Rental**; **£13.99 monthly (including VAT<sup>4</sup>) for the First Relevant Period** for Line Rental Plus; and £131.89 annually (including VAT<sup>5</sup>) for the **First Relevant Period** for Line Rental Saver (the **Line Rental Saver Charge Ceiling**);
  - b. for each subsequent **Relevant Period**, an amount calculated by employing the following formula:

$$CC_t = CC_{t-1} * (1 + CPI_{t-1} + 2.5\%)$$

Where:

- $CC_t$  means the Line Rental Charge Ceiling for the Relevant Period;  
 $CC_{t-1}$  means the Line Rental Charge Ceiling for the Prior Period;  
 $CPI_{t-1}$  means the change in the CPI in the year of 12 months ending four months immediately before the end of the Prior Relevant Period expressed as a percentage, rounded to two decimal places;

3. Where a customer has paid a Line Rental Saver Charge for a Line Rental Saver Charge Year which has started, but not ended on 1 April 2018, BT will ensure that the Nominal Line Rental Saver Charge does not exceed the Controlling Line Rental Saver Charge for each full calendar month remaining until the completion of that Line Rental Saver Charge year

Where:

- a. **Line Rental Saver Charge Year** means the 12-month period covered by the Line Rental Saver Charge paid by the Customer;
- b. **Relevant Line Rental Saver Charge** means the **Line Rental Saver Charge** paid by the Customer divided by 12;
- c. **Controlling Line Rental Saver Charge** means the **Line Rental Saver Charge Ceiling** for the **First Relevant Period** divided by the number of the remaining full calendar months until completion of the Line Rental Saver Charge Year;

4. BT shall take all reasonable steps to secure that, at the end of each **Relevant Period**, the **Percentage Change**,  $C_t$  (determined in accordance with paragraph 5 below) in the aggregate of charges for all of the **Services** in the **Basket** is not more than the **Controlling Percentage**,  $CP_t$  (as determined in accordance with paragraph 6 below).
5. For the purposes of complying with paragraph 4 the **Percentage Change**,  $C_t$ , shall be specified by employing the following formula:

<sup>3</sup> If the rate of VAT changes, BT's Commitments will not preclude BT from making pricing changes to reflect any such VAT rate change.

<sup>4</sup> As above.

<sup>5</sup> As above.

$$C_t = \frac{\sum_{i=1}^n \left[ R_i \frac{(\bar{P}_{i,t} - \bar{P}_{i,t-1})}{\bar{P}_{i,t-1}} \right]}{\sum_{i=1}^n R_i}$$

$C_t$  is the **Percentage Change** in the aggregate of charges for the **Services** in the **Basket** for the **Relevant Period**,  $t$ ;

$n$  is the number of individual **Services** in the **Basket**;

$i$  is a number from 1 to  $n$  for each of the  $n$  individual **Services** in the **Basket**;

$R_i$  is the **Total Revenue** accrued during the 12 months up to 30<sup>th</sup> November of the **Prior Period** in respect of the individual **Service**  $i$  that forms part of the **Basket**;

$t$  refers to the **Relevant Period**;

$t-1$  refers to the **Prior Period**;

$\bar{P}_{i,t}$  is the **Relevant Period Weighted Average Charge** made by BT for the individual **Service**  $i$  that forms part of the **Basket** during the **Relevant Period**, excluding any discounts offered by BT;

Where such **Relevant Period Weighted Average Charge** shall be calculated by employing the following formula:

$$\bar{P}_{i,t} = \sum_{j=1}^m (W_{i,j,t} P_{i,j,t})$$

Where:

$m$  is the number of time periods for which there are distinct charges during the **Relevant Period**;

$j$  is a number from 1 to  $m$  for each of the  $m$  time periods during which a distinct charge is in effect;

$W_{i,j,t}$  is the proportion of the **Relevant Period** in which each charge,  $P_{i,j,t}$  is in effect, calculated by the number of days during which the charge is in effect and dividing by the number of days in each **Relevant Period**.

$P_{i,j,t}$  is the charge for the specified period,  $j$ , during the **Relevant Period**  $t$  for the individual Service,  $i$ ;

$\bar{P}_{i,t-1}$  is the **Prior Period Weighted Average Charge**, where:

for the purpose of calculating the Percentage Change for the First Relevant Period, for Standard Line Rental, Line Rental Saver and Line Rental Plus,  $\bar{P}_{i,t-1}$  will be taken as defined respectively in paragraph 2a, and for all other services  $\bar{P}_{i,t-1}$  is the **Prior Period Weighted Average Charge** made by BT for the individual **Service**  $i$  that forms part of the **Basket** during the **Prior Period**, excluding any discounts offered by BT;

for the purposes of calculating the **Percentage Change** for the **Second Relevant Period** and the **Third Relevant Period**,  $\bar{P}_{i,t-1}$  is the **Prior Period Weighted Average Charge** made by BT for the individual **Service**  $i$  that forms part of the **Basket** during the **Prior Period**, excluding any discounts offered by BT;

Where such **Prior Period Weighted Average Charge** shall be calculated by employing the following formula:

$$\bar{P}_{i,t-1} = \sum_{j=1}^m (W_{i,j,t-1} P_{i,j,t-1})$$

Where:

$m$  is the number of time periods for which there are distinct charges during the **Prior Period**;

$j$  is a number from 1 to  $m$  for each the  $m$  time periods during which a distinct charge is in effect;

$W_{i,j,t-1}$  is the proportion of the **Prior Period** in which each charge,  $P_{i,j,t-1}$ , is in effect, calculated by the number of days during which the charge is in effect and dividing by the number of days in the **Prior Period**; and

$P_{i,j,t-1}$  is the charge for the individual period,  $j$ , during the **Prior Year**,  $t-1$ , for the individual Service,  $i$ .

6. For the purposes of complying with paragraph 5, the **Controlling Percentage**,  $CP_t$ , shall be calculated by employing the following formula:

$$CP_t = CPI_t + 0$$

Where:

$CP_t$  is the **Percentage Change** in charges for the specific **Service** in the single charge category in question for the **Relevant Period**  $t$ ; and

$CPI_t$  means the change in the CPI in the year of 12 months ending four months immediately before the end of the **Prior Period** expressed as a percentage, rounded to two decimal places.

## ANNEX B – PART 2: PRODUCTS / SERVICES

### Line Rental

Standard Line Rental

Line Rental Saver

Line Rental Plus

### Calling Plans

All Calling plans taken by Relevant Customers except for BT Basic and Home Phone Saver

### Call charges and International

Calls to BT Mobile Consumer numbers

Calls to all other UK Mobile numbers

Calls to UK National and Local Numbers

Access charges to service numbers

Calls to International numbers

Friends & Family International

International Freedom

Calls to 070 / 076 / 055 / 056 number ranges

**Calling features / other**

Calling feature packs rental

BT call minder

BT answer 1571

Choose to Refuse

Anonymous Call Reject

BT Privacy with Caller Display

Call Barring

Call Diversion

Call Waiting

BT Smart Talk

BT Call Protect

Three Way Calling

Ring Back

Reminder Call

1471

1470

Call Return 1471

Call Return 1571

Timeline

Call Sign

**ANNEX C: COMPLIANCE STATEMENTS**

1. Compliance summary				
Basket total	Condition X.xx	Period		Notes
			20XX/20XX+1	
		CPI	X.XX%	
		X	X.XX%	
		Controlling percentage (CPI-X)	X.XX%	
		Prior year Revenue	£x,xxx	
		Weighted revenue change made	£x,xxx	
		Weighted % price change made	X.XX%	
		Complies	True/False	
Single charge category 1	Condition X.xx	CPI	X.XX%	
		X	X.XX%	
		Controlling percentage (CPI-X)	X.XX%	
		Price ceiling	X.XX%	
		Complies	True/False	
Single charge category 2	Condition X.xx	CPI	X.XX%	
		X	X.XX%	
		Controlling percentage (CPI-X)	X.XX%	
		Price ceiling	X.XX%	
		Complies	True/False	

2 Compliance Detail																
Period: 20XX/20XX+1																
<b>Basket 1</b>																
CPI X.XX%																
X X.XX%																
Controlling percentage (CPI-X) X.XX%																
Basket	Revenue weight			Prior period average price				Current period average price				Average Price Change	Average price change x Revenue weight			
	Average price	Volume	Revenue	Initial price	Price change 1	Price change 2	etc	Average price	Initial Price	Price change 1	Price change 2			etc	Average price	
Days in year				x	x	x	x		x	x	x	x				
Service 1	x.xx	x,xxx	£x,xxx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	£x,xxx	
Service 2	x.xx	x,xxx	£x,xxx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	£x,xxx	
etc	x.xx	x,xxx	£x,xxx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	x.xx	(B)£x,xxx	
Total			(A)£x,xxx													
Percentage Change			X.XX% (B/A)													



**Single change – service X**

	Period 1	Period 2	Period 3
CPI	X.XX%	X.XX%	X.XX%
X	X.XX%	X.XX%	X.XX%
Controlling percentage (CPI-X)	X.XX%	X.XX%	X.XX%
Price ceiling	X.XX	X.XX	X.XX
Prices charged during period:			
- start of period	X.XX	X.XX	X.XX
- price change 1 (date)	X.XX	X.XX	X.XX
- price change 2 (date)	X.XX	X.XX	X.XX
- etc	X.XX	X.XX	X.XX

Note 1:

Note 2:

Etc:

**ANNEX D: ANNUAL STATEMENT FOR BT'S SPLIT PURCHASE CUSTOMERS**

<b>Field</b>	<b>Description</b>	<b>Example Wording</b>
<b>Format</b>	Letter or extra page on relevant bill. Sent annually via email and on paper if paper billing has been requested. Also available to view on MyBT	n/a
<b>Summary Spend</b>	Last 12 months' monthly average spend on line rental, calls/calling plans and add-ons, shown in a simple format (e.g. using an infographic)	<i>Last year you spent £X per month on average on your phone service with BT. That was an average of £x per month on calls and calling plans; £x on line rental and £x on features (give examples of what these were)</i>
<b>Savings Information</b>	Presentation of BT bundles that could provide a cost saving. Full T&Cs on back of letter.	<i>Our records indicate that you currently buy landline and broadband services separately [from different companies]. Ofcom, the communications regulator, estimates that people like you could save [£150] per year by bundling landline and broadband in one package with the same provider. You could save money by taking up one of our combined offers. For example, package XX offers you the same phone service that you currently receive, with XX broadband [add in package and average speeds] for £XX per month. This would be subject to a contract period of XX months. All of our terms and conditions are set out on the back of this letter.</i>
<b>Customer Response</b>	Refer to BT.com	<i>If you would like to take up this offer, or to find out more about the packages available to you from BT, please visit BT.com. Should you wish to do so, you can then apply to change your home phone and broadband packages on MyBT.com. You will then have 14 days to cancel if you change your mind.</i>
<b>Switching Information</b>	Information on how to switch and where to get more advice on switching	<i>Switching is easy. Should you wish to switch your landline and broadband to another provider, you don't need to contact BT. Information about how to do this is available on the Ofcom website at: <a href="https://www.ofcom.org.uk/phones-telecoms-and-internet/advice-for-consumers/costs-and-billing/switching">https://www.ofcom.org.uk/phones-telecoms-and-internet/advice-for-consumers/costs-and-billing/switching</a></i>

Review of the market for standalone landline telephone services - statement

## **Letter from Ofcom to BT, 26 October 2017**

Marc Allera  
CEO, BT Consumer  
BT Group

Jonathan Oxley  
Group Director, Competition  
Tel: [redacted]  
Email:  
[redacted]

26 October 2017

Dear Marc,

### Standalone landline telephone services

Thank you for your letter of 24 October committing to make various changes to the pricing for voice-only customers together with various measures to stimulate engagement for standalone fixed voice customers.

We have considered your letter and on the basis of BT's commitments set out there which closely reflect the regulatory proposals set out in our February consultation, we have decided not to proceed to the imposition of formal regulation at this time.

We will monitor the implementation of BT's commitment to cut and cap the retail prices for voice-only customers as set out in your letter. Whilst we do not anticipate any issues, should BT for any reason fail to carry out this commitment we will need to re consider our decision not to impose regulatory remedies to this effect.

We will also monitor the impact of BT's commitments more generally on consumers including the engagement remedies on which we will work with you. Should our monitoring show that nonetheless the consumer detriment we have identified remains unaddressed, we will consider whether we need to intervene in future.

Yours sincerely,



Jonathan Oxley

## A2. Sources relied upon in this statement

### Evidence supporting this statement

A2.1 Alongside this statement, we have today published the supporting evidence on our website. This is available at: <https://www.ofcom.org.uk/consultations-and-statements/category-1/review-of-landline-telephone-services>

### Information obtained under formal powers

A2.2 In the production of this statement, we have relied on information gathered using our formal information gathering powers under section 135 of the Communications Act 2003. We obtained information under these powers from the following stakeholders:

- i) BT
- ii) Phone Co-op
- iii) Post Office
- iv) Sky
- v) SSE
- vi) TalkTalk
- vii) Virgin Media

A2.3 We also relied upon information provided in response to the Narrowband market review after seeking permission from information providers to do so.

### Researched commissioned for the purposes of this review

A2.4 We commissioned qualitative research to inform this review. We have published this research on our website and it is available at: [https://www.ofcom.org.uk/data/assets/pdf\\_file/0016/105307/Enriching-understanding-of-Standalone-Voice-Customers.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0016/105307/Enriching-understanding-of-Standalone-Voice-Customers.pdf)

### Other sources that we have used

A2.5 We have used information from the following Ofcom sources:

- i) Ofcom technology tracker
- ii) Ofcom switching tracker
- iii) Narrowband market review

### Consultation responses

A2.6 We received consultation responses from the following stakeholders:

**Review of the market for standalone landline telephone services - statement**

- i) SSE
- ii) Telefonica
- iii) Vodafone
- iv) TalkTalk
- v) Communications Consumer Panel/ACOD
- vi) Three
- vii) Virgin Media
- viii) Post Office
- ix) BT
- x) Which?
- xi) Vodafone
- xii) UKCTA

A2.7 We received consultation responses from 37 individuals.

A2.8 We published non-confidential versions of these responses (where we were able to do so) on our website, they are available at: <https://www.ofcom.org.uk/consultations-and-statements/category-1/review-of-landline-telephone-services>

## A3. Glossary

<b>2006 Retail Price Control Statement</b>	Ofcom, <i>Retail Price Controls</i> , July 2006. <a href="https://www.ofcom.org.uk/_data/assets/pdf_file/0012/42114/rpcstatement.pdf">https://www.ofcom.org.uk/_data/assets/pdf_file/0012/42114/rpcstatement.pdf</a>
<b>2007 EC Recommendation</b>	European Commission Recommendation (2007/879/EC) of 17 December 2007 on relevant product and service markets within the electronic communications sector susceptible to ex ante regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services. Published in the Official Journal of the European Union, 28.12.2007, L 344, pages 65-69 at <a href="http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32007H0879">http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32007H0879</a>
<b>2014 EC Recommendation</b>	European Commission Recommendation (2014/7174/EC) of 9 October 2014 on relevant product and service markets within the electronic communications sector susceptible to ex ante regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services. <a href="http://eur-lex.europa.eu/JOHtml.do?uri=OJ:L:2014:295:SOM:EN:HTML">http://eur-lex.europa.eu/JOHtml.do?uri=OJ:L:2014:295:SOM:EN:HTML</a>
<b>2016 NMR Consultation</b>	Ofcom, <i>Narrowband market review – Consultation</i> , December 2016. <a href="https://www.ofcom.org.uk/_data/assets/pdf_file/0016/95011/Narrowband-Market-Review.pdf">https://www.ofcom.org.uk/_data/assets/pdf_file/0016/95011/Narrowband-Market-Review.pdf</a>
<b>The Act</b>	Communications Act 2003
<b>ASA</b>	Advertising Standards Authority
<b>BT</b>	British Telecommunications plc.
<b>BT Basic</b>	BT Basic is a social telephony scheme sold by BT for customers who are recipients of specific means-tested Government benefits. See <a href="http://btplc.com/inclusion/ProductsAndServices/BTBasic/index.htm">http://btplc.com/inclusion/ProductsAndServices/BTBasic/index.htm</a>
<b>BT retail divisions</b>	Those BT business units that directly serve residential and/or business customers.
<b>Bundle</b>	A bundle refers to the purchase of landline services in addition to other services such as broadband, pay-TV, etc.
<b>Call plan</b>	An add-on to a line rental services which allow customers to make calls to a specified set of number types (UK geographic numbers, or UK mobile etc.) within a given period (weekend, evening, anytime etc.) for a fixed price. They may or may not come with time limitations or fair use policies.
<b>Consumer Price Index (CPI)</b>	The official measure of inflation of consumer prices in the UK.

## Review of the market for standalone landline telephone services - statement

<b>Dual-play</b>	Where CP offers two services as part of a package of services, for example fixed voice and fixed broadband services.
<b>Home Phone Saver</b>	Home Phone Saver is a BT telephone only line rental package which provides a number of additional services. The service cannot be taken in a bundle with such as broadband.  <a href="http://bt.custhelp.com/app/answers/detail/a_id/49402/~/home-phone-saver-2017">http://bt.custhelp.com/app/answers/detail/a_id/49402/~/home-phone-saver-2017</a>
<b>Hull Area</b>	The area defined as the 'Licensed Area' in the licence granted on 30 November 1987 by the Secretary of State under Section 7 of the Telecommunications Act 1984 to Kingston upon Hull City Council and Kingston Communications (Hull) plc (KCOM).
<b>NMR</b>	Narrowband market review.
<b>Ofcom</b>	The Office of Communications.
<b>Plusnet</b>	Plusnet plc.
<b>Post Office</b>	Post Office Limited.
<b>Price freeze</b>	A situation where the prevailing market price or any other price is then held constant, either in nominal or real terms.
<b>S135</b>	Section 135 of the Communications Act.
<b>Significant Market Power (SMP)</b>	A test set out in European Directives used by NRAs, such as Ofcom, to identify those TPs which must meet additional obligations under the relevant Directives.
<b>Sky</b>	British Sky Broadcasting Ltd.
<b>Split purchaser</b>	A customer that buys both a standalone fixed voice service and a standalone fixed broadband service, either from the same supplier or different suppliers, i.e. all split -service and split-supplier customers.
<b>Split-service customer</b>	A customer that buys both a standalone fixed voice service and a standalone fixed broadband service from the same supplier, but each service is bought separately (not in a bundle).
<b>Split-supplier customer</b>	A customer that buys both a standalone fixed voice service and a standalone fixed broadband service from two different suppliers.
<b>SSE</b>	SSE Energy Supply Limited.
<b>SSNIP</b>	Small but Significant Non-Transitory Increase in Price.
<b>Strategic review</b>	Strategic review of Digital Communications 2016. See <a href="https://www.ofcom.org.uk/_data/assets/pdf_file/0016/50416/dcr-statement.pdf">https://www.ofcom.org.uk/_data/assets/pdf_file/0016/50416/dcr-statement.pdf</a>
<b>Standalone fixed voice customers</b>	Customers that buy a fixed voice service from a CP but do not also buy a fixed broadband service from the same CP as part of a bundle.



## Review of the market for standalone landline telephone services - statement

<b>Standalone fixed voice services</b>	Landline services that are not sold as part of a bundle with non-voice service. This includes access (i.e. line rental) and calls.
<b>TalkTalk</b>	TalkTalk Telecoms Group plc.
<b>The Phone Co-op</b>	The Phone Co-op Limited.
<b>UK</b>	United Kingdom – when referring to the United Kingdom this excludes Hull except when referring to United Kingdom wide data.
<b>Virgin Media</b>	Virgin Media plc.
<b>Voice-only customer</b>	A customer that buys a standalone fixed voice service, but do not also buy a fixed broadband service from any CP.
<b>Wholesale Line Rental (WLR)</b>	The service offered by BT to other United Kingdom communications providers to enable them to offer retail line rental services in competition with BT’s own retail services. Line rental is offered along with calls (and other service elements, such as broadband) to retail customers.

**Review of the market for standalone landline telephone services - statement**

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**ANNEX 4**

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# **Review of the market for standalone landline telephone services**

Evidence supporting the Statement

Redacted [REDACTED] for publication

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Consumer characteristics	32

# 1. Evidence supporting this statement

- 1.1 This document sets out evidence we have drawn on in our review of the provision of residential standalone fixed voice (“SFV”) services in the UK (excluding Hull, unless otherwise stated). It updates evidence originally set out in our February Consultation<sup>1</sup>, and provides new evidence that has become available since then (e.g. the results from the NMR residential survey), which we have relied on in our Statement of 26 October 2017.

## An overview of fixed voice services

### Trends in the bundling of retail services

- 1.2 Consumers have largely shifted away from purchasing communications services separately and towards purchasing bundles of services. Bundling describes the process of combining multiple telecommunications services as a single package from one supplier.
- 1.3 Figure 1.1 shows the proportion of households that take bundled services. In 2017, 70% of households reported that they purchased at least landline and fixed broadband from the same provider, and 81% reported buying at least two of their communication services in a bundle.<sup>2</sup>

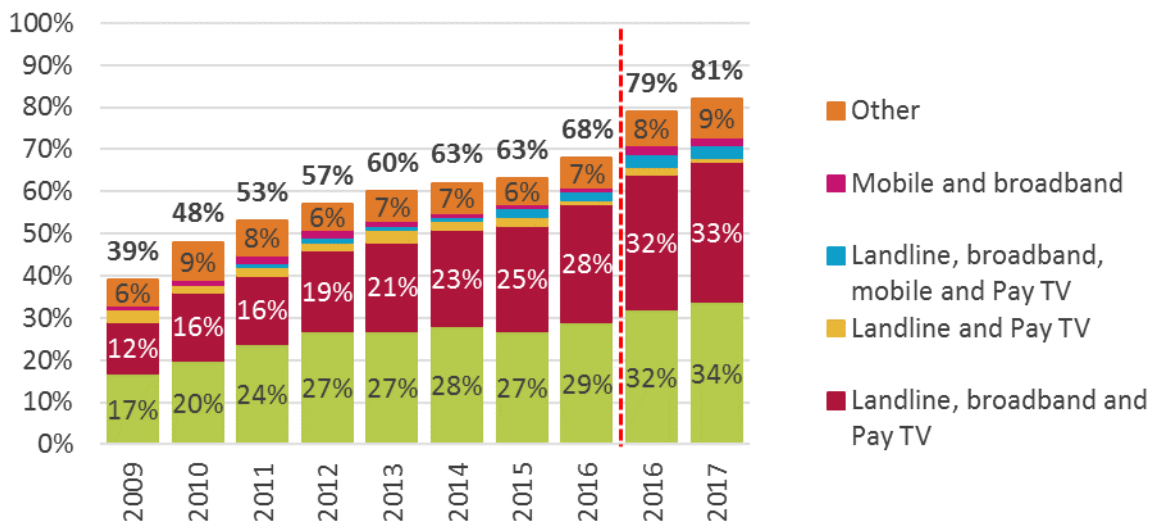
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<sup>1</sup> See Annex 8 (Supporting evidence), available here:

[https://www.ofcom.org.uk/data/assets/pdf\\_file/0027/97812/Annexes-Review-of-the-market-for-standalone-landline-telephone-services.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0027/97812/Annexes-Review-of-the-market-for-standalone-landline-telephone-services.pdf)

<sup>2</sup> The households not reflected on Figure 1.1 (approximately 19% of households in 2017) are made up of those who purchase their landline on a standalone basis and those who do not have a landline, some of whom live in a mobile-only home.

## Evidence supporting the review of the market for standalone landline telephone services

Figure 1.1: Take-up of bundled services<sup>3</sup>

Source: Ofcom, Technology Tracker. Data from Q1 of each year 2009 – 2014, then H1 2015-2017.

Notes: Revised methodology for 2016 data (right of the dotted line) as outlined in the footnote.

## Trends in the volume of residential lines and calls

### Line volumes

- 1.4 According to Ofcom's Quarterly Telecoms data updates, the total number of residential lines in the UK has increased by 13% since Q4 2009, from 23.4 million to 26.4 million in Q4 2016.<sup>4</sup> This increase reflects the growth in household numbers and the take-up of fixed telephony.<sup>5</sup>
- 1.5 Whilst the number of BT residential lines has decreased, this has been more than offset by an increase in the number of residential lines supplied by other operators. This has translated into a decrease in BT's share of residential lines from 57% in Q4 2009 to 36% in Q4 2016.

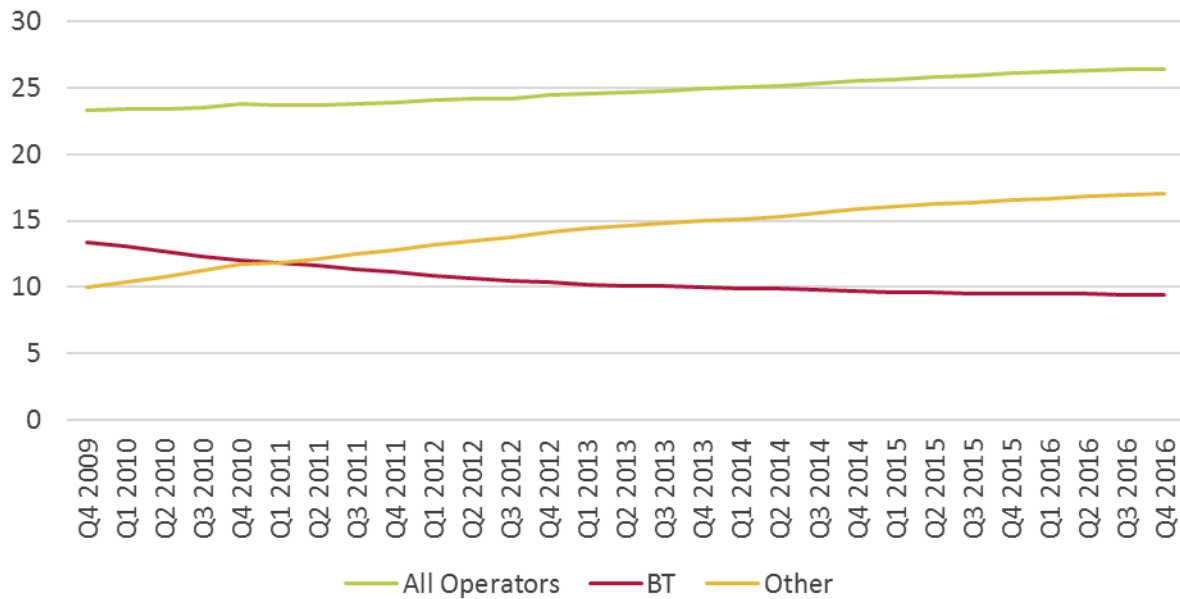
<sup>3</sup> The red dotted line marks a change in how we use Technology Tracker responses to estimate the proportion of households that bundle services. To the left of the dotted line, we report the proportion of respondents who indicated they bundle communications services. To the right of the dotted line, we report the proportion of respondents who indicated they purchase multiple services from a single provider. Analysis for 2016 and 2017 now includes those who pay line rental in addition to their broadband service as a bundle.

<sup>4</sup> We estimate that approximately 1.65 million residential lines in the UK are purchased by SMEs. This estimate is based on the fact that around 30% of SMEs reported not having a business-specific contract in 2016 (31% for those with 1-9 employees, 10% for those with 10-49 employees, and 5% for those with 50-249 employees. See Figure 103 from the Jigsaw report on *SME experience of communications services*, available here: [https://www.ofcom.org.uk/data/assets/pdf\\_file/0030/96348/Ofcom-SME-consumer-experience-research-2016-Report.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0030/96348/Ofcom-SME-consumer-experience-research-2016-Report.pdf)) and that there were approximately 5.5 million SMEs in the UK in 2016 (see Paragraph 4.33 from Ofcom's Connected Nations Report 2016, available here: [https://www.ofcom.org.uk/data/assets/pdf\\_file/0035/95876/CN-Report-2016.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0035/95876/CN-Report-2016.pdf)).

<sup>5</sup> The take-up of fixed telephony among households shows a fairly stable trend, fluctuating between 82% and 87% between 2009 to 2017.

## Evidence supporting the review of the market for standalone landline telephone services

Figure 1.2: Number of residential lines in the UK (millions)



Source: Ofcom/operators<sup>6</sup>

### Call volumes

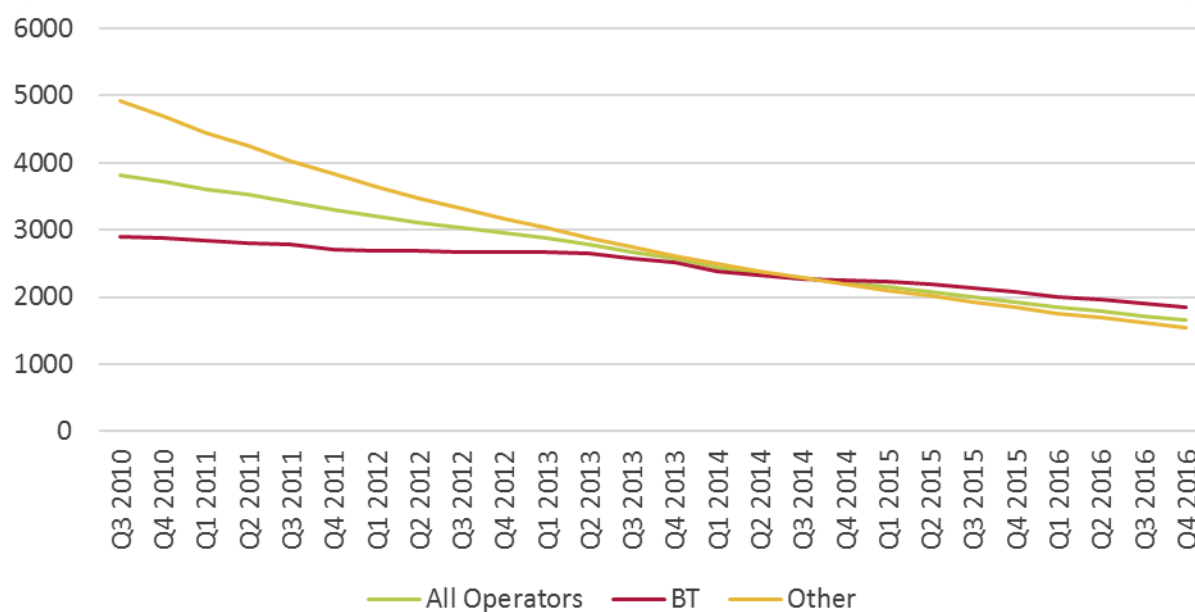
- 1.6 Call minutes per residential line, i.e. including both bundled lines and standalone landlines, have decreased since Q3 2010, from 3.8 thousand minutes per line in the year up to Q3 2010 to 1.7 thousand minutes per line in the year up to Q4 2016 (a 57% fall). BT customers historically made fewer call minutes on average than customers of other Communications Providers (“CPs”).

<sup>6</sup> See Ofcom’s Telecoms data updates here: <https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates>.



## Evidence supporting the review of the market for standalone landline telephone services

Figure 1.3: Call minutes per residential line per year in the UK (thousands)



Source: Ofcom/operators<sup>7</sup>

## An overview of the customer groups

1.7 Customers who purchase SFV services can be divided into two distinct customer groups:

- Voice-only customers: these customers purchase an SFV service but do not take fixed broadband from any supplier; and
- Split-purchase customers; these customers purchase an SFV service and a standalone fixed broadband service, i.e. they purchase these services separately and therefore do not derive any benefit from purchasing these services in tandem.

1.8 Split-purchase customers can be further divided into two sub-groups:

- Split-supply customers: these customers purchase an SFV service and a standalone fixed broadband service from two separate suppliers; and
- Split-service customers: these customers purchase an SFV service and a standalone fixed broadband service from the same supplier; i.e. they do not bundle these services.

1.9 In the February Consultation we defined a single market for SFV customers and, therefore, presented much of the evidence in a consolidated manner.<sup>8</sup> In light of our revised Statement position, we have presented the voice-only and split-purchaser groups independently where possible. We have also updated our analysis where new evidence is available.

<sup>7</sup> See Ofcom's Telecoms data updates here: <https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates>.

<sup>8</sup> Annex 8: [https://www.ofcom.org.uk/data/assets/pdf\\_file/0027/97812/Annexes-Review-of-the-market-for-standalone-landline-telephone-services.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0027/97812/Annexes-Review-of-the-market-for-standalone-landline-telephone-services.pdf)

## Evidence supporting the review of the market for standalone landline telephone services

- 1.10 We collected data from BT, Phone Co-op, Post Office, Sky, SSE, TalkTalk, and Virgin Media, have updated it since the February Consultation. We collected data on:
- the number of fixed voice lines purchased on a standalone basis (excluding lines purchased by split-service customers);
  - the number of fixed voice lines purchased by split-service customers, if any; and
  - the number of customers who purchase a standalone fixed broadband service.<sup>9</sup>
- 1.11 While BT and other providers could take steps to identify which of its SFV customers were voice-only, to date it has not done this. Therefore, communications providers were only able to provide the number of fixed voice lines they sell on a standalone basis (excluding lines purchased by split-service customers). This included both voice-only customers and split-supply customers.
- 1.12 We have used data on customers who purchase a standalone fixed broadband service in order to estimate the number of split-supplier customers. This is because the former will include all split-supply customers on the Openreach network (who need to pay a line rental in order to receive a broadband service). However, the number of customers who purchase a standalone fixed broadband service also includes customers on the Virgin Media network (who do not need to pay a line rental to receive a standalone fixed broadband service). Virgin Media advised that at the time of asking [X] of their customers purchased standalone broadband. We estimate that this means that [X] Virgin Media customers purchase a standalone fixed broadband service, and have no SFV service from any provider as at Q1 2017 given our estimate that [X] BT SFV customers are Virgin Media standalone broadband customers.
- 1.13 In addition to its own volumes, BT provided us with estimates of the number of its SFV customers who purchase a separate standalone fixed broadband service from other communications providers.<sup>10</sup>
- 1.14 Using a combination of the above data, we have estimated the breakdown of the voice-only and split-supplier lines.<sup>11</sup> Also, information on the number of customers and the number of lines indicates that the large majority of SFV customers have a single fixed line. Therefore, the line figures presented below can also be interpreted broadly as customer figures.

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<sup>9</sup> This data is based on the volume of customers not lines. We assume that each split-supplier customer purchases one SFV line.

<sup>10</sup> Our estimates of the number of split-supplier lines include [X] (as at Q1 2017) BT standalone fixed broadband customers, who take a voice line from a non-BT supplier. These customers are distributed to CPs according to the total voice-only plus split-supplier market shares. We do not have s.135 data that would allow us to identify split-supplier customers who take neither their voice nor broadband service from BT and we assume that these customers are not material. One piece of evidence that goes against this is the 2017 SRB survey, which indicates that up to 18% of total split-supplier customers' fixed voice line could be supplied by a non-BT supplier. If we assumed that this 18% figure was in fact accurate, this would not have substantive implications for the conclusions we reached for split-purchase customers.

<sup>11</sup> We primarily rely on standalone broadband customer numbers provided by suppliers for our estimates of split-supplier customers, and make adjustments based on BT estimates where BT has identified another CP as providing standalone broadband to a BT SFV customer, but we do not have data directly from that CP, or BT has not specified the CP.

## Evidence supporting the review of the market for standalone landline telephone services

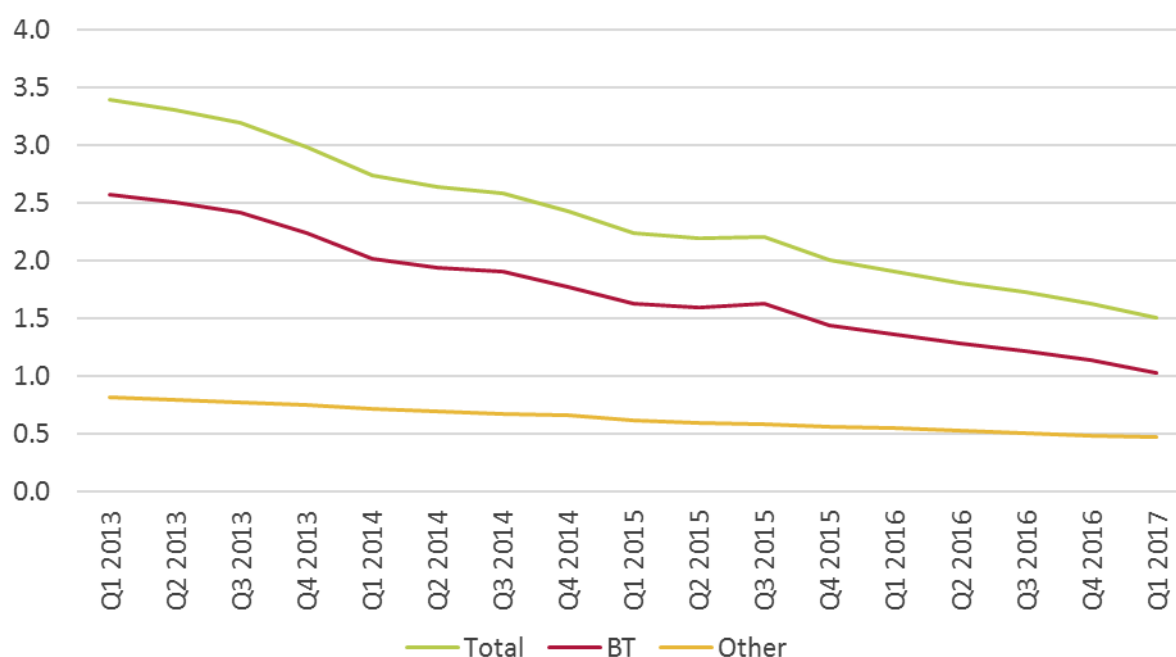
## Trends in the volume of lines and calls

1.15 This section presents volumes data (number of lines and call minutes per line). Where possible, we have presented disaggregated data for voice-only and split-purchase customers, rather than aggregated SFV data.<sup>12</sup>

## Line volumes

1.16 In Q1 2017 the total number of voice only lines were 1.5 million.

**Figure 1.4: Number of voice-only lines in the UK (thousands of lines)**



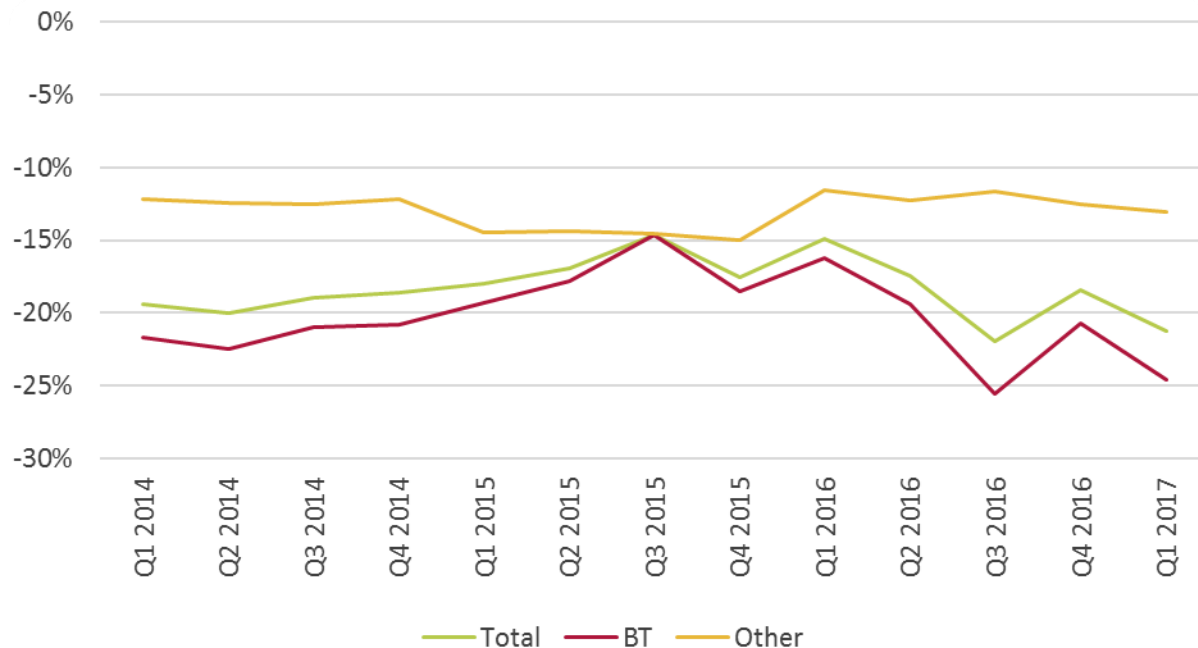
Source: s.135 responses

1.17 Figure 1.5 below presents the annual percentage rates of decline in the number of voice-only lines. The rate of decline for communications providers other than BT has remained fairly constant between 12-15%. BT has generally seen a faster rate of decline of around 20%.

<sup>12</sup> After the publication of the February 2017 consultation, SSE sent a correction to its response to a formal information request. SSE had incorrectly estimated its voice-only and split-supplier line volumes resulting in a significant overestimation of its actual customers. Whilst the impact on SSE data is significant, relative to the market the implications and impact on our analysis are negligible.

Evidence supporting the review of the market for standalone landline telephone services

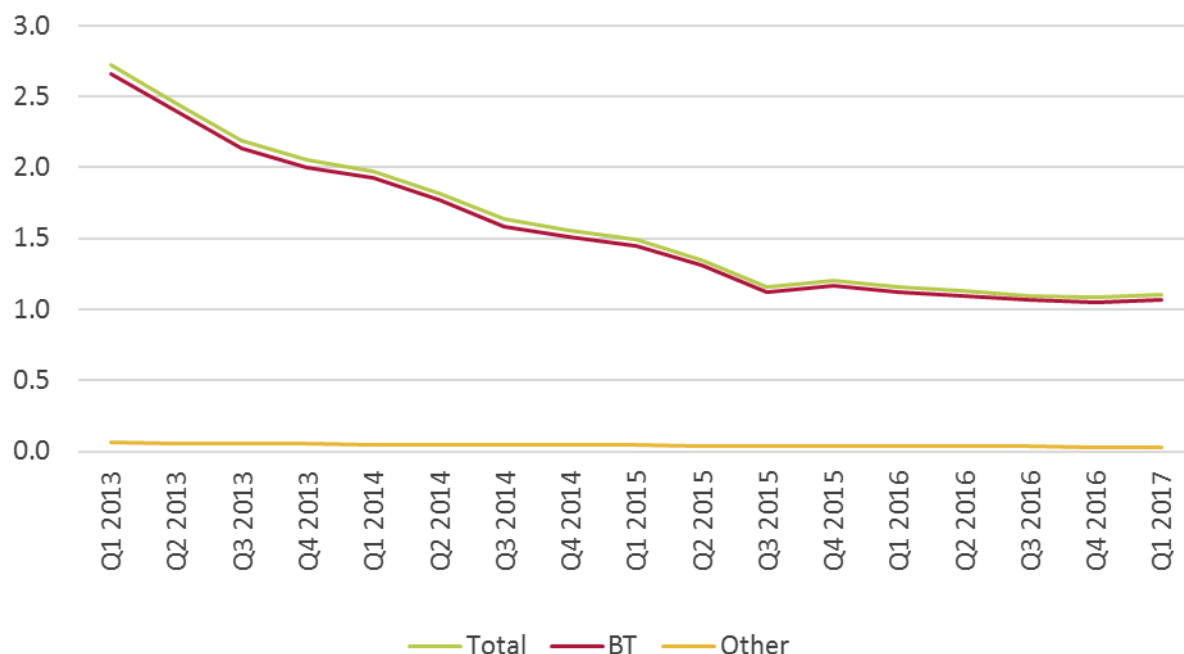
**Figure 1.5: Rate of decline in the number of voice-only lines (% change against same quarter in previous year)**



Source: s.135 responses

1.18 The total number of split-purchase lines has decreased since Q1 2013, from 2.7 million in Q1 2013 to 1.1 million in Q1 2017 (a 60% fall). BT accounts for virtually all the split-purchaser lines in the UK.

**Figure 1.6: Number of split-purchaser lines in the UK (thousands of lines)**

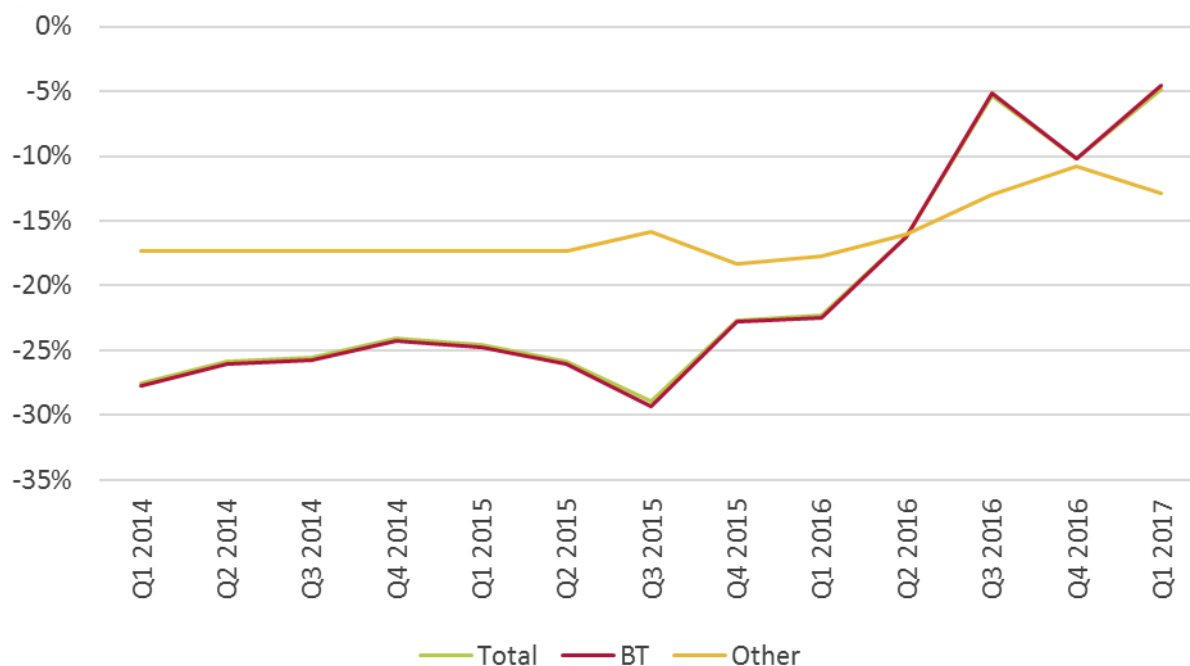


Source: s.135 responses

## Evidence supporting the review of the market for standalone landline telephone services

1.19 The figure below presents the annual percentage rates of decline in the number of split-purchaser lines. Note that only a very small proportion of split-purchase customers have a voice line from a provider other than BT.

**Figure 1.7: Rate of decline in the number of split-purchaser lines (% change against same quarter in previous year)**



Source: s.135 responses

### Call volumes

1.20 Per line call minutes from SFV lines have decreased slightly. Annual SFV call minutes for all operators fell from 2.3 thousand minutes per line in the year up to Q1 2014 to 2.1 thousand minutes in the year up to Q1 2017 (i.e. a 6.1% fall). [X]

**Figure 1.8: Call minutes per SFV line per year (thousands)**

[X]

Source: s.135 responses.

1.21 Figure 1.9 below presents the change in call volumes per line for SFV lines and for all residential lines. [X]

1.22 Generally, in comparison to SFV customers, the call minutes per line of all residential customers have declined at a much greater rate than that of SFV customers. Whilst call minutes per line for all residential lines have consistently decreased, call minutes per line for SFV customers have fluctuated between periods of growth and decline.

## Evidence supporting the review of the market for standalone landline telephone services

**Figure 1.9: Rates of change in call minutes per line per year<sup>13</sup>**

[✂]

Source: Ofcom/operators<sup>14</sup> for all residential lines and s135 responses for SFV lines.

1.23 As explained in paragraphs to 1.11 to 1.14, we have used standalone broadband lines to estimate the breakdown of SFV lines into voice-only and split-purchaser lines. However, we have little further basis on which to base any breakdown of SFV calls and so have not presented voice-only and split-purchaser calls separately.

## Estimates of market shares

1.24 We calculate shares based on the average volumes at the end of each quarter for each year, and present the years 2013-2016. We also have data for Q1 2017. There is no major change between the first quarter of 2017 and previous years presented.

1.25 We exclude lines sold to BT Basic customers and calls originated on these lines. We also exclude BT Basic from access and calls revenue shares. We received data for September 2016 from Direct Save Telecom, Plusnet (BT's value brand) and Utility Warehouse on their number of SFV lines, which imply each of these communications providers has an immaterial share of lines. In light of this, and in absence of time series data, these suppliers have been excluded from the analysis.

1.26 With regards to access, we have estimated Virgin Media's voice-only and split-supplier line volumes for January – December 2013 since Virgin Media were only able to provide this data from January 2014.<sup>15</sup> We have also estimated a subset of BT's split-service lines from January 2013 to October 2014 as this data was incorrect.<sup>16</sup> This small group refers to customers who purchase both a voice-only line and a bundle which includes a voice service.

1.27 We collected both information on the number of customers as well as the number of lines. As before, we have presented data based on the number of lines, however, the number of customers and lines for each CP is very similar, such that there is essentially no difference in the market shares between customers and lines.

## Voice-only access

1.28 Figures 1.10 and 1.11 below show that BT is the largest supplier of lines to voice-only customers. In 2013, BT's share was 76%. This has been declining, and was 5 percentage points lower in 2016, at 71%. As discussed in paragraph 1.38 below, we undertook a

<sup>13</sup> The evidence on call minutes per line was presented incorrectly in Figure A8.7 of the February 2017 consultation, and has now been corrected.

<sup>14</sup> See Ofcom's Telecoms data updates here: <https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates>

<sup>15</sup> We estimated this using the average monthly growth rate calculated from the data it has been able to provide.

<sup>16</sup> We estimated this using the average monthly growth rate calculated from the data it has been able to provide.

## Evidence supporting the review of the market for standalone landline telephone services

number of sensitivity checks under which BT's market share of voice-only lines remained high (over 65%).

- 1.29 To the extent that market shares have been changing over the past four years, the evidence indicates that this is mainly due to providers' customer bases declining at differing rates (as shown in Figure 1.5), rather than customers switching between suppliers, as discussed below in paragraphs 1.32.
- 1.30 TalkTalk has a market share of less than 10%. However, TalkTalk only supplies voice-only services to legacy customers, rather than making them available (or competing) for new customers.

**Table 1.10: Shares of lines to voice-only lines by CP (in ranges)**

	BT	Post Office	TalkTalk	SSE	Virgin Media	Sky	Phone Co-op	Total non-BT
2013	76%	10% - 20%	< 10%	< 5%	< 5%	< 1%	< 1%	24%
2014	73%	10% - 20%	< 10%	< 5%	< 5%	< 1%	< 1%	27%
2015	73%	10% - 20%	< 10%	< 5%	< 5%	< 1%	< 1%	27%
2016	71%	10% - 20%	< 10%	< 5%	< 5%	< 1%	< 1%	29%
Q1 2017	68%	10% - 20%	< 10%	< 5%	< 5%	< 1%	< 1%	32%

Source: s.135 responses

**Table 1.11: Shares of voice-only lines by CP (exact figures)**

[X]

Source: s.135 responses

- 1.31 All major communications providers' SFV line volumes have been in decline for all periods in which we have data, with the exception of Sky, whose voice-only customer base grew in 2014. The rates of decline vary between communications providers. For example, BT's volume of voice-only lines declined by approximately 21% between Q1 2016 and Q1 2017, whereas across the same period [X] experienced a somewhat smaller [X]% decline whilst [X] experienced a somewhat greater [X]% decline.
- 1.32 Meanwhile, switching appears to have had a limited effect on shares. For example, gross customer additions reported by other communications providers suggest that switching could account for at most a small proportion of gross customer losses reported by BT. We have estimated gross customer losses of BT's voice-only customers is, on average, [X] per month over the period we have this data (November 2014 to May 2017).<sup>17</sup> Given that split-

<sup>17</sup> The gross customer addition and loss data we have is for voice-only and split-supplier customers combined, and we have not attempted to break this down. The average ratio of net customer losses to gross customer losses is [X]% and we

**Evidence supporting the review of the market for standalone landline telephone services**

purchase customers are almost exclusively customers of BT, we have conservatively assumed that all gross customer additions data we have for other communications providers is for voice-only customers.

1.33 At most, acquisitions by the next three largest suppliers can account for only a small proportion of BT's losses. [redacted]<sup>18</sup> [redacted]<sup>19</sup> [redacted]

1.34 We have also estimated voice-only access revenues for BT, Post Office, SSE, TalkTalk, Virgin Media, and Sky for four financial years (2013/14, 2014/15, 2015/16, and 2016/17). This is calculated by multiplying each communications provider's average line rental by the average number of voice-only lines in the months within each financial year.<sup>20</sup> We have then calculated each communications providers' share of total voice-only access revenues.

1.35 BT's and Other communications providers' shares of voice-only access revenue are set out in Tables 1.12 and 1.13, below.

**Table 1.12: Shares of voice-only access revenue by CP (in ranges)**

[redacted]

Source: s.135 responses and Pure Pricing UK Broadband Updates

**Table 1.13: Shares of voice-only access revenue by CP (exact figures)**

[redacted]

Source: s.135 responses and Pure Pricing UK Broadband Updates

1.36 [redacted] consistently had the second largest market share of voice-only access revenue across the financial years. Its share has increased approximately 2 percentage points a year from [redacted]% in 2013/14 to [redacted]% in 2016/17, a gain greater than that lost by BT. It believes that this is because the decline in its SFV customers (which are almost exclusively voice-only) has been slower than the market average.

**Split-purchaser access**

1.37 Split-service customers are almost exclusively BT customers, with the exception of a negligible number of customers with TalkTalk. To the nearest percent, BT has 100% of split-service customers.

1.38 On the basis of s.135 responses, we estimate that BT supplies almost all SFV lines to split-supply customers. There is a small proportion of split-supply customers who purchase standalone fixed broadband from BT and an SFV line from other CPs. As outlined above, we

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have applied this ratio to BT's net voice-only customer losses to estimate voice-only gross customer losses of [redacted] per month.

<sup>18</sup> [redacted].

<sup>19</sup> [redacted].

<sup>20</sup> This methodology overestimates access revenue because some CPs include a call allowance with the line rental (e.g. BT includes weekend calls). We are of the view, however, that this is unlikely to materially affect our access revenue estimates.



## Evidence supporting the review of the market for standalone landline telephone services

have no clear evidence of split-supply customers who purchase neither their SFV service nor standalone fixed broadband services from BT, and we have assumed that the number of such split-supply customers is not material. Where there is uncertainty from using an estimate from BT of its competitor overlap, we have conducted sensitivity checks regarding the number of these standalone broadband customers. Under a range of sensitivities, BT's market share in the split-supply segment remains high (>90%).<sup>21</sup>

1.39 Our market share best estimates of split-purchaser lines are presented in Table 1.14 and 1.15 below.

**Table 1.14: Shares of split-purchaser lines by CP (in ranges)**

	BT	Post Office	TalkTalk	SSE	Virgin Media	Sky	Phone Co-op	Total non-BT
2013	98%	< 3%	< 1%	< 1%	< 1%	< 1%	< 1%	2%
2014	97%	< 3%	< 1%	< 1%	< 1%	< 1%	< 1%	3%
2015	97%	< 3%	< 1%	< 1%	< 1%	< 1%	< 1%	3%
2016	97%	< 3%	< 1%	< 1%	< 1%	< 1%	< 1%	3%
Q1 2017	97%	< 3%	< 1%	< 1%	< 1%	< 1%	< 1%	3%

Source: s.135 responses

**Table 1.15: Shares of split-purchaser lines by CP (exact figures)**

[X]

Source: s.135 responses

1.40 We have also estimated split-purchaser access revenues for BT, Post Office, SSE, TalkTalk, Virgin Media, and Sky for four financial years (2013/14, 2014/15, 2015/16, and 2016/17). This takes the same approach as before, by multiplying each communications providers average line rental by the average number of voice-only lines in the months within each financial year.<sup>22</sup> We have then calculated each communications providers' share of total split-purchaser access revenues. BT's and Other communications providers' shares of split-purchaser access revenue are set out in Tables 1.16 and 1.17 below.

<sup>21</sup> We note that a piece of evidence that contradicts this is the 2017 NMR residential survey which suggests that BT has 82% market share of split-supplier customers. We are of the view that this estimate is less reliable than those discussed above (i.e. >90%) because the former is based on consumer responses rather than industry data. However if we assumed that this 18% figure was in fact accurate, this would not have substantive implications for the conclusions we reached for split-purchase customers.

<sup>22</sup> This methodology overestimates access revenue because some CPs include a call allowance with the line rental (e.g. BT includes weekend calls). We are of the view, however, that this is unlikely to materially affect our access revenue estimates.

**Evidence supporting the review of the market for standalone landline telephone services**

1.41 BT had by far the largest share of split-purchaser access revenue in all financial years for which we have data.

**Table 1.16: Shares of split-purchaser access revenue by CP (in ranges)**

[X]

Source: s.135 responses and Pure Pricing UK Broadband Updates

**Table 1.17: Shares of split-purchaser access revenue by CP (exact figures)**

[X]

Source: s.135 responses and Pure Pricing UK Broadband Updates

**SFV calls**

1.42 As we do not have any evidence on which to break down SFV calls into calls made by voice-only customers and those made by split-purchaser customers, we present shares of SFV calls as a whole.

1.43 We have estimated call volumes where communications providers have not been able to provide data. We have estimated BT split-service call volumes for January 2013 – October 2014<sup>23</sup>; Post Office SFV call volumes for January 2013 – October 2014; TalkTalk from January 2013 – July 2015; and Virgin Media for 2013.<sup>24</sup> For the periods for which we have data from communications providers, we did not estimate any call minutes.

1.44 Table 1.18 shows that BT is the largest supplier of SFV calls.

**Table 1.18: Shares of SFV call minutes by CP (exact figures)**

[X]

Source: s.135 responses

1.45 As a proxy for SFV calls revenue we have estimated SFV non-access revenue for BT, Post Office, SSE, TalkTalk, Virgin Media and Sky for four financial years (2013/14, 2014/15, 2015/16, and 2016/17). We have done so by subtracting our estimate of SFV access revenue from the SFV total revenue within each financial year. We are aware that SFV non-access revenue is an overestimate of SFV calls revenue given that some revenues which are neither from access nor calls (e.g. charges for paper billing and ancillary services) would be included. However, in our view non-access revenue is a reasonable proxy for actual calls revenue for the purpose of calculating each CP's market share of SFV calls revenue. Table 1.20 below, sets out communications providers' market shares of SFV non-access revenue.

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<sup>23</sup> We estimated BT's volume of split-supplier calls by applying the average minutes per line from voice-only and split-supplier lines for each month between January 2013 – October 2014. We applied this average to our lower bound estimate of split-service lines between January 2013 and October 2014 to estimate the total volume of minutes originated on split-service lines.

<sup>24</sup> We estimated Post Office, TalkTalk and Virgin media's call volumes by calculating a weighted average minutes per line, from Phone Co-op, Sky and SSE data, for each month. We then applied this to the relevant months for Post Office, TalkTalk and Virgin media, to estimate the volume of total SFV lines.

## Evidence supporting the review of the market for standalone landline telephone services

**Table 1.19: Shares of SFV non-access revenue by CP (exact figures)**

[REDACTED]

*Source: s.135 responses and Pure Pricing UK Broadband Updates***SFV total revenue**

1.46 We estimate each suppliers' total annual revenue generated through SFV lines by applying each suppliers' average revenue generated through voice services (from both line rental and calls) to the average volume of SFV lines for each financial year. This is the sum of the SFV access and non-access revenues presented above.

1.47 Table 1.20 below shows that BT has the largest share of SFV total revenues. [REDACTED]

1.48 [REDACTED]

**Table 1.20: Shares of SFV total revenue by CP (exact figures)**

[REDACTED]

*Source: s.135 responses*

*Notes: asterisk indicates that the average revenue was calculated using SFV revenue. Other suppliers' average revenue was calculated using total voice revenue.*

**Communications providers' views of the market**

1.49 BT provided internal documents with information about its SFV customer base in the context of meetings with Ofcom and in response to s.135 notices. These documents include results from market research conducted or commissioned by BT over the past three years. The following points summarise the content of BT's internal documents with information about its voice-only and split-purchase customer base. We have split these points into those we presented in the February 2017 consultation, and new points that complement the points presented in the February 2017 consultation.

1.50 Points in BT's internal documents presented in the February 2017 consultation:

- [REDACTED].<sup>25 26</sup>
- [REDACTED].<sup>27</sup>
- [REDACTED].<sup>28</sup>
- [REDACTED].<sup>29</sup>
- [REDACTED];<sup>30</sup> [REDACTED].<sup>31</sup>

<sup>25</sup> [REDACTED] (response dated 18 November 2016 to question 1 of the 1<sup>st</sup> BT s.135).

<sup>26</sup> BT presentation to Ofcom 30 November 2016, slide 3.

<sup>27</sup> BT presentation to Ofcom 30 November 2016, slide 10.

<sup>28</sup> BT presentation to Ofcom 8 February 2017, slide 5.

<sup>29</sup> Response dated 18 November 2016 to question 1 of the 1<sup>st</sup> BT s.135.

<sup>30</sup> [REDACTED] (response dated 18 November 2016 to question 1 of the 1<sup>st</sup> BT s.135).

<sup>31</sup> BT presentation to Ofcom 30 November 2016, slide 4.

## Evidence supporting the review of the market for standalone landline telephone services

- [REDACTED].<sup>32</sup>
- [REDACTED].<sup>33</sup> [REDACTED]<sup>34</sup> [REDACTED].<sup>35</sup>
- [REDACTED].<sup>36</sup>

1.51 Other communications providers also provided internal documents with information about their SFV customer base in response to s.135 notices, and/or verbally expressed their view of the SFV customer base in meetings with Ofcom. The documents provided include results from market research conducted or commissioned by these communications providers over the past three years. The following points summarise the content of the internal documents provided by communications providers other than BT and the views they expressed verbally in meetings with Ofcom.

1.52 Points in Other CP's internal documents that were set out in the February 2017 consultation:

- Post Office mentioned that it has three acquisition channels for voice-only customers: online (20%), call centre (40%) and in-branch (40%). It described customers as inert and noted that despite regular contact (in Post Office branches) Post Office struggles to gain much traction. It considered that inertia seems to come from concerns about the switching process even though the potential savings from switching are significant for some customers. However, it said it had successfully reached some of BT's SFV customers by launching various marketing campaigns.<sup>37</sup>
- Post Office ran an introductory offer to incentivise BT's SFV customers to switch. The offer entailed paying a 12-month contract at a price of £14.99 a month instead of the full monthly price of £16.99. At the end of the contract, the customer pays the full monthly price. Post Office marketing material also shows that they try to alleviate customer's concerns about the switching process. For example, in the marketing material for the new offer, the Post Office noted that the end user will keep the same phone line so no engineer will need to visit their home, they can keep the same phone number that everyone knows and there will be no break in service as the switch takes place.
- [REDACTED].<sup>38</sup>
- [REDACTED].<sup>39</sup>
- TalkTalk no longer offers SFV access services to new customers [REDACTED].<sup>40</sup>
- [REDACTED].<sup>41</sup>

<sup>32</sup> BT presentation to Ofcom 30 November 2016, slide 4.

<sup>33</sup> [REDACTED]. See BT presentation to Ofcom 30 November 2016, slide 6.

<sup>34</sup> BT presentation to Ofcom 30 November 2016, slides 5-9.

<sup>35</sup> BT presentation to Ofcom 8 February 2017, slide 4.

<sup>36</sup> Response dated 18 November 2016 to question 1 of the 1<sup>st</sup> BT s.135.

<sup>37</sup> Notes of phone conversation with Post Office on 20 October 2016.

<sup>38</sup> Response dated 29 November 2016 to question 1 of the 1<sup>st</sup> Post Office s.135.

<sup>39</sup> Notes of phone conversation with SSE on 01/12/2016.

<sup>40</sup> TalkTalk email to Ofcom, November 2016.

<sup>41</sup> Notes of phone conversation with Virgin Media on 01/11/2016.

**Evidence supporting the review of the market for standalone landline telephone services**

- [REDACTED].<sup>42</sup>
- [REDACTED].<sup>43</sup>
- [REDACTED].<sup>44</sup>
- [REDACTED].<sup>45</sup>
- [REDACTED].<sup>46</sup>
- [REDACTED].<sup>47</sup>

1.53 New points in Other communications providers' internal documents that complement the points presented in the February 2017 consultation:

- [REDACTED].<sup>48</sup>
- [REDACTED].<sup>49</sup>
- [REDACTED].<sup>50</sup>
- [REDACTED].<sup>51</sup>
- [REDACTED].<sup>52</sup> [REDACTED].<sup>53</sup>

**Communications providers' views on engagement of SFV customers**

1.54 Several communications providers provided accounts of their experiences with attempts to engage SFV customers in the market, either through responses to formal information requests or through correspondence with Ofcom following the February Consultation:

- [REDACTED].<sup>54</sup>
- [REDACTED].<sup>55</sup> [REDACTED].<sup>56</sup>
- [REDACTED].<sup>57</sup>

**Evidence on wholesale market prices**

1.55 Suppliers use different access and call services at the wholesale level in order to provide access and calls to SFV customers at the retail level. When they buy these inputs they pay wholesale market prices.

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<sup>42</sup> Notes of phone conversation with Sky on 15 November 2016.

<sup>43</sup> Notes of phone conversation with Sky on 15 November 2016.

<sup>44</sup> Notes of phone conversation with Sky on 15 November 2016.

<sup>45</sup> Notes of phone conversation with Direct Save on 21 November 2016.

<sup>46</sup> Notes of phone conversation with Direct Save on 21 November 2016.

<sup>47</sup> Notes of phone conversation with Direct Save on 21 November 2016.

<sup>48</sup> Response dated 28 July 2017 to the 3<sup>rd</sup> Post Office s.135.

<sup>49</sup> Response dated 28 July 2017 to the 3<sup>rd</sup> Post Office s.135.

<sup>50</sup> SSE letter to Ofcom, August 2017

<sup>51</sup> Response dated 28 July 2017 to question 5 of the 2<sup>nd</sup> TalkTalk s.135; TalkTalk email to Ofcom, 15 August 2017.

<sup>52</sup> Response dated 2 August 2017 to question 3 of the 2<sup>nd</sup> Sky s.135

<sup>53</sup> Sky email to Ofcom, 22 August 2017.

<sup>54</sup> Response dated 28 July 2017 to question 1 of the 3<sup>rd</sup> Post Office s.135.

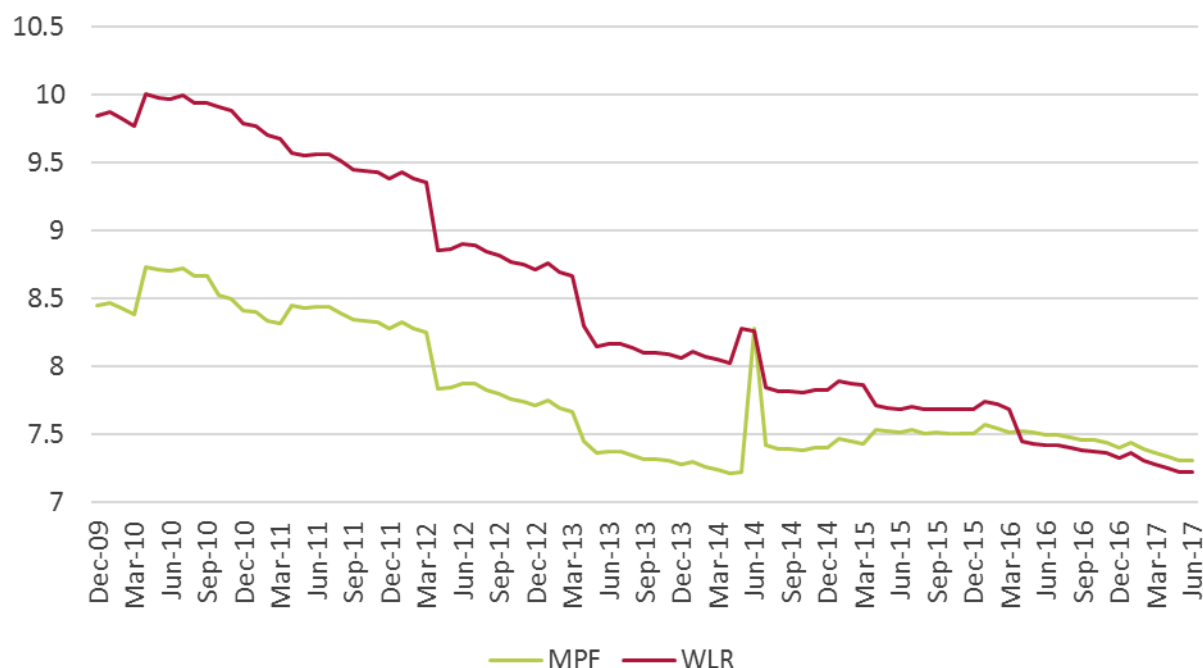
<sup>55</sup> SSE call with Ofcom, 15 June 2017.

<sup>56</sup> SSE letter to Ofcom, 11 August 2017.

<sup>57</sup> TalkTalk email to Ofcom, 15 August 2017.

## Evidence supporting the review of the market for standalone landline telephone services

- 1.56 Regarding access inputs, suppliers that rely on BT's copper network pay Openreach (BT's wholesale access division) for Wholesale Line Rental (WLR) or Metallic Path Facility (MPF). WLR allows only the provision of voice services, while MPF allows both voice and broadband services to be provided. Suppliers, such as Virgin Media, that have their own network may use it to provide access to its SFV customers.<sup>58</sup>
- 1.57 Between December 2009 and June 2017 BT's WLR and MPF prices decreased significantly. WLR prices fell 34% in real terms between 2009 and 2016 (MPF prices fell 14%).

**Figure 1.22: BT's WLR and MPF prices (£/month in June 2017 prices)**

Source: BT Openreach

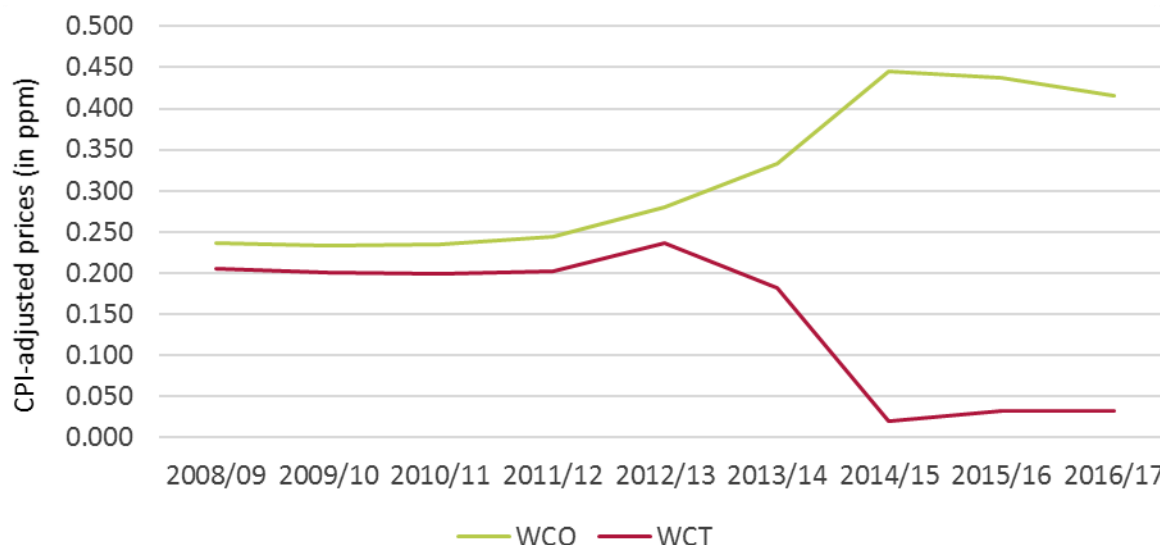
Notes: Y-axis starts at £7/month

- 1.58 Regarding call inputs, providers most commonly purchase Wholesale Call Origination (WCO) from BT, and Wholesale Call Termination (WCT) from either BT or other communications providers. WCO is a service that enables SFV customers to make calls over their lines, while WCT enables these customers to terminate their calls to geographic numbers (a number starting 01 or 02).
- 1.59 Between 2008/09 and 2016/17 BT's WCO and WCT prices have changed significantly in real terms, as shown below.

<sup>58</sup> We are also aware that generally CPs that have their own network may still rely on BT's copper network to provide voice – not many CPs use their own LLU network to provide voice-only services.

## Evidence supporting the review of the market for standalone landline telephone services

Figure 1.23: BT's WCO and WCT prices (June 2017 prices)



Source: BT Regulatory Financial Statements

## Evidence on retail pricing

### Retail line rental prices

- 1.60 This section analyses price data collected by PurePricing which monitors the line rental prices of the main suppliers of broadband services. We analyse BT, Virgin Media, TalkTalk, Sky, and Post Office's line rental prices.<sup>59</sup> Line rental charges are paid by all SFV customers for access to a fixed voice line.<sup>60</sup> Some calls may be included in the price of line rental, however these inclusions vary across suppliers.<sup>61</sup>
- 1.61 Up until 2006, BT was subject to retail price regulation. In 2006, Ofcom<sup>62</sup> decided to allow retail price controls to lapse, though the market remained regulated until 2009.<sup>63</sup> As Figure 1.25 below shows, line rental prices were generally decreasing in real (i.e. inflation adjusted) terms across this period. All line rental prices fell by between 4% and 9%, in real terms, from December 2006 to December 2009, with the exception of Post Office, which increased its line rental prices by 9%, in real terms.

<sup>59</sup> The prices of other suppliers, including SSE, have not been tracked by PurePricing. A more exhaustive list of current SFV prices is in Table 1.26 below.

<sup>60</sup> The line rental component of a dual-play service is no longer advertised as a distinct price following the ASA's ruling. Some CPs now state that they do not charge a price for line rental, however the overall bundled price will still provide fixed voice access.

<sup>61</sup> For example, some suppliers such as BT include free weekend calls with their line rental. Due to restricted available data, these differences are not reflected in our analysis. A detailed list of current market offerings is provided in Table 1.26 below. We take into account that some CPs include some free calls with their line rental when we estimate the market shares of non-access revenue as a proxy for the market shares of calls revenue, see paragraph 1.98.

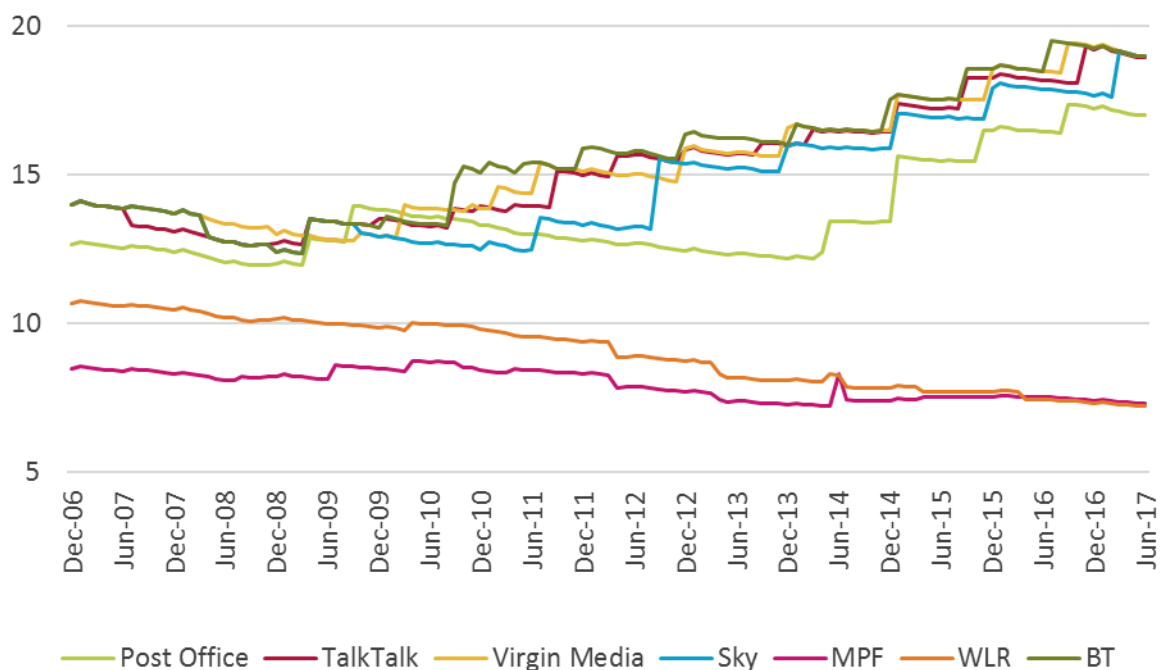
<sup>62</sup> Ofcom replaced Oftel as the regulator with responsibility for electronic communications markets from 29 December 2003.

<sup>63</sup> Ofcom, *Retail Price Controls*, Statement of 19 July 2006 ("2006 Retail Price Control Statement"), [https://www.ofcom.org.uk/data/assets/pdf\\_file/0012/42114/rpcstatement.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0012/42114/rpcstatement.pdf)

## Evidence supporting the review of the market for standalone landline telephone services

1.62 However, since deregulation of the retail narrowband market in 2009, line rental prices have generally been increasing, in real terms, despite decreasing wholesale access prices. Line rental prices have increased, by between 23% and 47% depending on the provider, in real (i.e. inflation-adjusted) terms between December 2009 and June 2017. Since December 2009, BT has offered the single most expensive line rental price in the market for 40 out of the 91 months, and for a further 31 months it was jointly most expensive with Virgin Media. Since September 2016, Virgin Media's line rental price has been the most expensive in the market at £19.00 per month, although this is only one penny more expensive than BT. Line rental prices have converged to some degree in recent years, having diverged after 2009. They have converged mainly due to significant increases in price by Sky and Post Office.

**Figure 1.24: Wholesale and retail line rental price movements (£/month in June 2017 prices)**



Source: Ofcom/PurePricing UK Broadband Updates

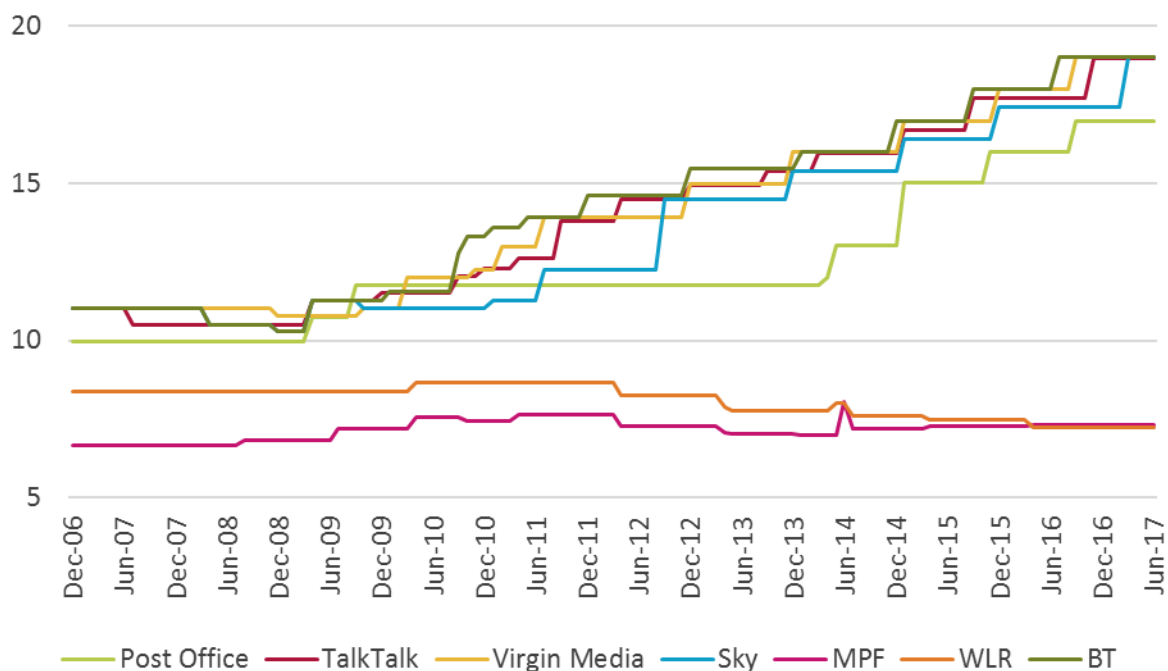
Notes: Adjusted for CPI. Excludes line rental saver pre-payment tariffs. Y-axis starts at £5/month.

1.63 Figure 1.26 below shows the line rental prices in nominal terms, i.e. without adjusting for inflation, since December 2006. These are the line rental prices and changes that would have been visible to consumers in the market.



## Evidence supporting the review of the market for standalone landline telephone services

Figure 1.25 Wholesale and retail line rental price movements (£/month)



Source: Ofcom/PurePricing UK Broadband Updates

Notes: Excludes line rental saver pre-payment tariffs. Y-axis starts at £5/month.

### Timing of line rental price increases

1.64 We outline the timings of communications providers' announcements, and implementation, of line rental price increases. The price increases discussed here relate to prices charged to communications providers existing customer bases, rather than prices offered to new customers.<sup>64</sup> The announcement and implementation dates were collected from ispreview.co.uk, an independent internet service provider review website which publishes articles informing readers of telecoms price increases. Where the announcement date of the price increase is not stated in the article, we have used the publication date of the article as a proxy for the announcement date. Where possible, we have checked these dates and/or months against (a) internal pricing documents we received from BT, Sky and TalkTalk and (b) other press sources of price increases. Information from these sources is consistent with the price increases and dates from ispreview.co.uk.

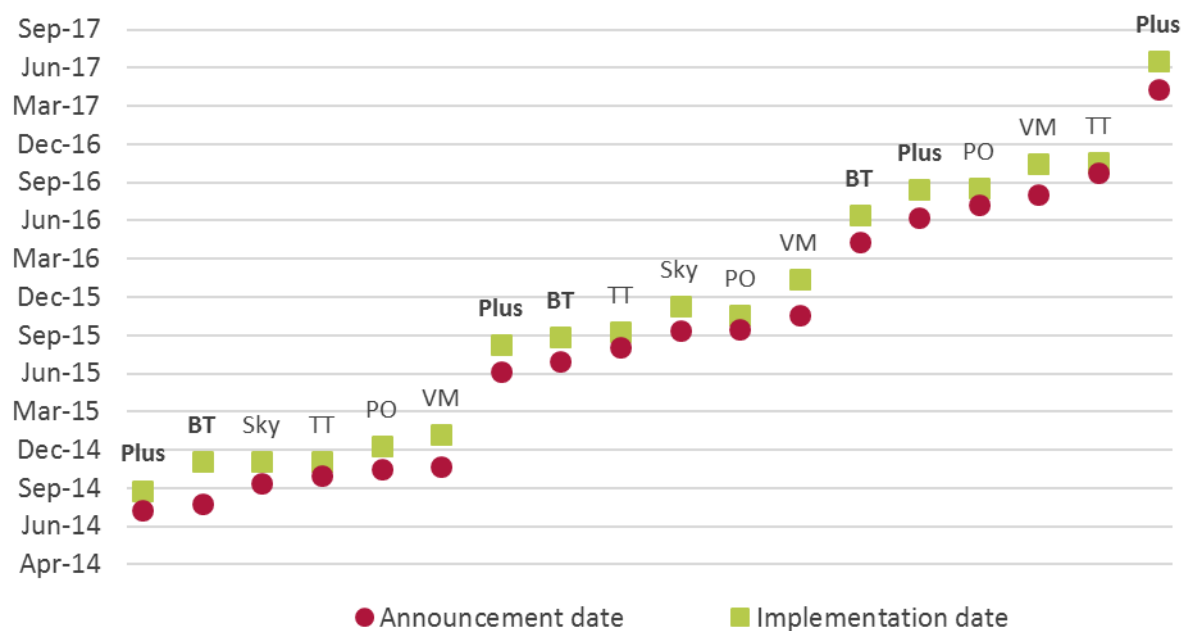
1.65 Figure 1.26 below shows the announcement and implementation dates of line rental price increases across the main communications providers, with each pair of data points for announcement and implementation dates relating to a supplier and a pound value increase. We have labelled the data points for implementation dates with an abbreviation

<sup>64</sup> In a small number of instances, suppliers implement the price increases to new customers 2-3 months prior to the price increase for existing customers.

## Evidence supporting the review of the market for standalone landline telephone services

of the name of the supplier that implemented the increase. The labels are in bold fonts for BT and Plusnet.

**Figure 1.26: Line rental price increase announcement and implementation dates, 2014-2017.**<sup>65</sup>



Source: *ispreview.co.uk*, *moneysavingexpert.com*

- 1.66 In the past three years, price increase announcements have typically clustered within a four to five-month period, followed by at least a five-month period of no price increases (with implementation following within months of the announcement).
- 1.67 BT has typically announced and implemented its line rental price increases before any other supplier over the past three years. Other suppliers then appear to follow BT in the subsequent months.<sup>66</sup> Communications providers typically increase their line rental by the same amount (usually by £1.00 per month) on an annual basis.
- 1.68 In January 2017 Sky announced it was increasing the line rental price by £1.59 to £18.99. Sky also announced that this price increase will not apply not apply to SFV customers, who will continue to pay a price of £17.40. This is the case for both existing and new SFV customers with Sky.
- 1.69 In December 2016 SSE announced it was going to increase the total rental cost (i.e. line rental and package fees) of several of its packages.<sup>67</sup> However, it did not specify how much of the increase corresponded to line rental and therefore is not included in the chart above.

<sup>65</sup> BT and Post Office recently froze the cost of line rental for their customers (BT in January 2017, while Post Office in July 2017).

<sup>66</sup> The exception to this is Plusnet's announcement and implementation. However, BT Group has owned Plusnet since 2007. [3].

<sup>67</sup> See <https://sse.co.uk/help/phone-and-broadband/price-changes/february-2017#item1>

## A description of current market offers

1.70 This section summarises the current market prices for SFV services, including line rental and call plan prices offered by active suppliers of SFV services. We also provide details on BT Basic, BT Home Phone Saver 2020 and Virgin Media Talk Protected.

### Current standard line rental and call plan prices

1.71 Table 1.27 summarises the current prices for SFV services: monthly line rental (including annual pre-payment) and call plans.

**Table 1.27: Prices for SFV services: line rental and call plans (per month)**

	Monthly line rental	Annual line rental pre-payment	Weekend calls (in addition to line rental)	Evening and weekend calls (in addition to line rental)	Anytime calls (in addition to line rental)
BT	£18.99	£17.40	Inclusive	£3.80	£8.99
Phone Co-op	£17.00	£15.00	-	£3.00	£7.00
Direct Save Telecom <sup>68</sup>	£15.95	£14.50	-	£2.95	£7.65
Post Office <sup>69 70</sup>	£15.00*	-	Inclusive	£3.00	£8.00
Sky <sup>71</sup>	£17.40	-	-	£4.00	£8.00
SSE <sup>72</sup>	£16.00	-	-	£2.00	£5.00
Utility Warehouse	£16.50	-	-	£3.00	£9.00
Virgin Media	£19.00	£16.33	£1.00	£5.00	£8.00

Source: Operator websites (accessed 16 August 2017).

Notes: asterisk indicates a promotional price.

<sup>68</sup> Direct Save Telecom also offers line rental on a rolling 28-day contract at £16.95/month.

<sup>69</sup> The price currently offered by Post Office was a promotional price, offered until 17 September 2017. This promotional price applied to a 12-month contract, after which customers would pay the standard price for line rental with inclusive weekend calls of £16.99.

<sup>70</sup> In the previous version of this table, Fuel was included. Since we published our February consultation, Fuel has left the market and Post Office has acquired their customers.

<sup>71</sup> All Sky customers, except those customers who only had a voice service as of 1 March 2017, pay the new line rental price of £18.99.

<sup>72</sup> SSE since 16 August increased its price to a minimum of £19.

## Evidence supporting the review of the market for standalone landline telephone services

**BT Basic**

- 1.72 BT offers an SFV service called BT Basic, which is a tariff for vulnerable consumers. BT offers a separate service called BT Basic + Broadband, which is a dual-play variant of the SFV BT Basic service. To qualify for BT Basic, a customer must be receiving one of the following benefits:
- Income Support;
  - Income-based Job Seekers Allowance;
  - Pension Credit (Guaranteed Credit);
  - Employment and Support Allowance (income related); and
  - Universal Credit (and are on zero earnings)
- 1.73 The line rental price for BT Basic customers is £5.10 per month (27% of BT's standard monthly line rental of £18.99), which includes a call allowance of £1.50 which would allow a customer to make around ten one-minute calls or one thirteen-minute call in a month.<sup>73 74</sup> Calls beyond this allowance can be made at an additional cost, which has a monthly cap of £10, subject to a Fair Use policy.<sup>75</sup>
- 1.74 There are around [§<] SFV lines supplied to BT Basic customers.<sup>76 77</sup>

**Home Phone Saver 2020**

- 1.75 BT offers a product called Home Phone Saver 2020, which bundles line rental, calls and additional features together in a package.<sup>78</sup> This is a standalone service, i.e. it is not offered as part of any bundle with broadband from BT. This product is offered at a price of £21.99 per month, which is fixed until 2020.<sup>79</sup> Table 1.27 below compares Home Phone Saver 2020 with the individual prices of the products and features included in Home Phone Saver 2020.
- 1.76 In June 2017, there were around [§<] lines supplied to Home Phone Saver customers, accounting for [§<]% of BT's SFV lines (excluding BT Basic).<sup>80</sup>
- 1.77 Home Phone Saver 2020 includes:
- monthly line rental;
  - unlimited calls to UK landlines at any time, for up to one hour;
  - inclusive calls to 0845 and 0870 numbers at any time, for up to one hour;

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<sup>73</sup> <http://btplc.com/inclusion/ProductsAndServices/BTBasic/Whatdoyouget/index.htm> [accessed 23/10/2017]

<sup>74</sup> BT Basic line rental does not include free weekend calls.

<sup>75</sup> If a customer exceeds the call allowance, they are charged 11.3 pence per minute (plus 3.3 pence for each phone call) for all calls to UK national and local numbers. They are charged 11.6 pence per minute (plus 3.3 pence for each phone call) for calls to UK mobiles.

<sup>76</sup> BT estimated that there are around a further [§<] BT Basic + Broadband customers (*source: BT presentation to Ofcom, 30/10/2016*).

<sup>77</sup> Source: s. 135 response data.

<sup>78</sup> There are a number of iterations of Home Phone Saver, signalled by the associated date.

<sup>79</sup> Source: Operator website (accessed 16 August 2017).

<sup>80</sup> Source: s. 135 response data.

## Evidence supporting the review of the market for standalone landline telephone services

- 1000 free minutes to BT Mobiles (excluding BT Business Mobile);
- BT Privacy Caller Display (opt-in only);
- Call Minder with enhanced BT Call Protect (opt-in only);
- International Premium Rate Call Barring (opt-in only);
- up to 7 additional calling features, (opt-in only); and
- free 1471 Call Return.

**Table 1.28: Comparison of Home Phone Saver 2020 with individual product prices**

	<b>BT Home Phone Saver 2020</b>	<b>Individual standard prices</b>
Line rental	Included	£18.99/month
Unlimited Anytime Calls <sup>81</sup>	Included (for up to an hour)	£8.99/month
Inclusive calls to 0845 and 0870 numbers at any time	Included (for up to an hour)	Included
1000 free minutes to BT Mobiles (excludes BT Business Mobile)	Included	Included with Unlimited Anytime Calls, otherwise 16p/minute
1471 call returns	Included	27.5p charge plus the cost of the call
BT Privacy with Caller Display	Included (when you opt-in)	£1.75/month
Call Minder	Included (when you opt in)	£4.50/month
BT Call Protect	Included (when you opt in)	Included (when you opt in)
Anonymous Call Reject <sup>82</sup>	Included (when you opt-in)	£6.05/month
Up to 7 additional Calling features	Included (when you opt in)	£11.75/month <sup>83</sup>
<b>Total</b>	<b>£21.99/month</b>	<b>£52.03/month<sup>84</sup></b>

Source: Operator website (accessed 21 August 2017).

1.78 A customer purchasing these SFV services at standard prices could make substantial savings by taking up Home Phone Saver 2020. A customer who purchases standard line rental and unlimited anytime calls from BT could save £5.99/month by switching to Home

<sup>81</sup> Calls to non-BT phone mobile numbers incur a charge of 8 pence per minute in the Unlimited Anytime Calls package, compared with 16 pence per minute under Home Phone Saver 2020.

<sup>82</sup> Provided when BT Call Protect is not available at a customer's exchange.

<sup>83</sup> Based on the cost of a package of 5+ calling features (BT Consumer Price Guide, [http://www.productsandservices.bt.com/assets/pdf/BT\\_PhoneTariff\\_Residential.pdf](http://www.productsandservices.bt.com/assets/pdf/BT_PhoneTariff_Residential.pdf), accessed 21 August 2017)

<sup>84</sup> Sum of all monthly costs (per minute and per call costs not included).

**Evidence supporting the review of the market for standalone landline telephone services**

Phone Saver 2020. A customer who purchases all of the products included with Home Phone Saver 2020, on an individual basis at standard prices could save up to £30.04/month by switching to Home Phone Saver 2020. However, for customers purchasing line rental and weekend calls, Home Phone Saver 2020 is more expensive than their current plan, while for those purchasing line rental, evening and weekend calls, Home Phone Saver is 80p cheaper per month (assuming no out-of-plan calls).

- 1.79 Home Phone Saver 2020, launched in April 2017, has had additional features added to it compared to Home Phone Saver 2019. The potential ‘maximum’ savings from Home Phone Saver 2020 compared to Home Saver 2019 has increased to £30.04/month from £13.05/month. The main reason is the addition of “Call Minder” and “Up to 7 additional Calling features”.

**BT Line Rental Saver**

- 1.80 BT offers an SFV product called Line Rental Saver, which offers BT customers 12 months’ line rental for the price of 11 when paying the entire sum up front. Therefore, instead of paying the monthly rate of £18.99 for 12 months (£227.88 per annum) Line Rental Saver customers pay a single (non-refundable) instalment of £208.80 (which equates to £17.40 per month).<sup>85</sup> Line Rental Saver is not compatible with Home Phone Saver, i.e. the annual price of Home Phone Saver cannot be paid up front in order to receive a discount.

**Virgin Media Line Rental Saver**

- 1.81 Virgin Media offers SFV customers the option to take its Line Rental Saver package, whereby customers are able to pay £196 up front for a year’s line rental. Customers who do this save £32 per annum, paying £196 instead of £228 in 12 monthly instalments. This equates to £16.33 per month for line rental instead of the usual £19.

**Virgin Media Talk Protected**

- 1.82 In December 2016 Virgin Media announced it would be launching a new product called Talk Protected, which freezes its line rental price at the previous rate £17.99, for elderly and disabled customers. This became available to new qualifying customers on 1 January 2017, and existing eligible customers were automatically upgraded to Talk Protected after 10 January. To qualify for Talk Protected a customer must be identified as being over 65, or have additional accessibility needs including limited hearing, sight, speech and mobility. Customers signed up to this product receive additional benefits, such as inclusive evening and weekend calls to UK landlines and mobiles and inclusive voicemail and caller display, among other benefits.

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<sup>85</sup> We note that previously BT’s Line Rental Saver offered a 10% reduction in the cost of a year’s line rental. This new version of Line Rental Saver offers an 8.3% discount.

## Evidence supporting the review of the market for standalone landline telephone services

## Comparisons of prices

1.83 In this section we compare the prices voice-only and split-purchase customers are paying for their services with the prices of dual-play services.

### SFV prices comparison with dual play prices

1.84 Table 1.29 below compares the SFV access price (line rental) with the cheapest available dual-play price. Therefore, it shows the incremental broadband price.

**Table 1.29: Line rental and promotional and standard dual-play prices**

	(1) Monthly line rental price	(2) Cheapest promotional dual-play price	(3) Cheapest standard dual-play price	(2) – (1) Difference to promotional dual-play price	(3) – (1) Difference to standard dual-play price
BT	18.99	24.99	34.99	6.00	16.00
Phone Co-op	17.00	22.00	27.00	5.00	10.00
Post Office	15.00 <sup>86</sup>	20.00	28.00	5.00	13.00
Sky	18.99	20.00	28.99	1.01	10.00
SSE	16.00	26.00 <sup>87</sup>	26.00	10.00	10.00
TalkTalk	18.95	19.95	27.00	1.00	8.05
Virgin Media	19.00	27.00	40.00	8.00	21.00
<b>Weighted average</b>	<b>18.18</b>	<b>24.01</b>	<b>33.11</b>	<b>5.83</b>	<b>14.93</b>

Source: Operator websites (accessed 21 August 2017)

Notes: Averages are weighted by the estimated number of voice-only customers with each CP as at Q1 2017. Promotional prices generally apply to 12-month contract periods with the exceptions of an 18-month contract period for Post Office, and a 24-month contract period for TalkTalk. Cheapest dual-play prices are for speeds of 17Mbit/s, i.e. ADSL, except for Virgin Media (50Mbit/s – the lowest speed offered), and BT whose 38Mbit/s package with a 30Gb data allowance was cheaper than its 17 Mbit/s package which is only available with unlimited data.

<sup>86</sup> This is a promotional price. The standard price for line rental with the Post Office is £16.99 a month.

<sup>87</sup> SSE did not offer a promotional price at the time of access. However, we note that it has previously had a promotional price of £19.50 a month.

## Evidence supporting the review of the market for standalone landline telephone services

- 1.85 Below we compare the price of line rental and calls, which we refer to as SFV services, against dual-play prices using data from Simplify Digital from Q1 2013 to Q1 2017. The prices of SFV services are averaged across BT, Post Office, SSE, and Fuel.<sup>88</sup> ADSL dual-play refers to a dual-play bundle with standard broadband with headline speeds of <30Mbit/s. We use average standard (non-promotional) ADSL dual-play prices and average prices including promotions.<sup>89</sup> These prices include an average call subscription fee. The average prices for ADSL dual-play are based on prices offered by BT, Sky and TalkTalk, the three largest providers in the ADSL market.
- 1.86 Table 1.30 below compares the price of SFV services and ADSL dual-play prices in real (inflation-adjusted) terms, presenting data at yearly intervals from Q1 2013 to Q1 2017. From Q1 2013 to Q1 2017, the price of SFV services increased by 16% (£3.02). Across the same period, the standard (non-promotional) price of ADSL dual-play increased by approximately the same percentage (19%, or £6.30), while average speed increased. The price including promotions decreased slightly by 1% (£0.31). Figure 1.30 presents these relative price changes indexed against the price at the start of Q1 2013.<sup>90</sup>
- 1.87 Figure 1.30 also compares the price difference between SFV services and ADSL dual-play. The average price difference between SFV services and standard ADSL services has increased by 22% (£3.28) between Q1 2013 and Q1 2017. However, the average price difference between SFV services and ADSL prices including promotions has decreased by 34% (£3.33) across the same period.

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<sup>88</sup> And “other packages”. These are prices advertised to new SFV customers.

<sup>89</sup> This price is averaged across all tariff types, i.e. standard and promotional, not exclusively across promotional tariffs.

<sup>90</sup> This presents prices at all points in time tracked by Simplify Digital. This is usually 4-5 times a month.



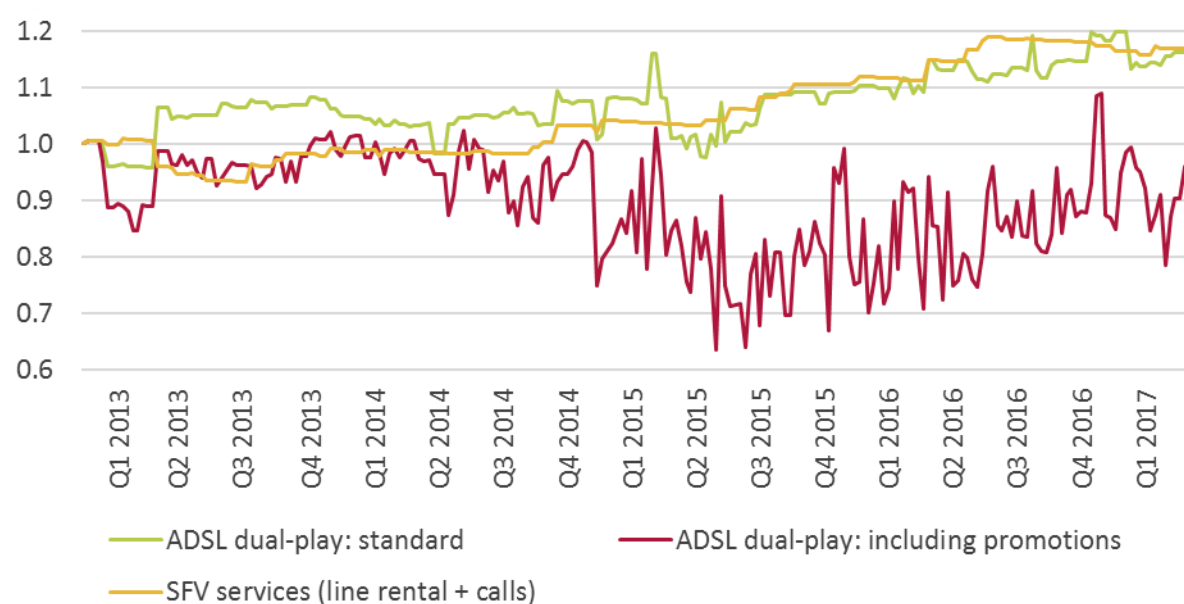
## Evidence supporting the review of the market for standalone landline telephone services

Table 1.30: Prices of SFV services and ADSL dual-play bundles (£/month, June 2017 prices)

	Q1 2013	Q1 2014	Q1 2015	Q1 2016	Q1 2017	% change (2013-2017)	£ change (2013- 2017)
(1) SFV services (line rental + calls)	18.89	18.57	19.55	20.99	21.91	16%	3.02
(2) ADSL dual-play price: standard	33.67	35.97	37.54	38.03	39.97	19%	6.30
(3) ADSL dual-play price: including promotions	28.81	31.07	27.45	25.60	28.50	-1%	-0.31
<b>Difference to SFV services</b>							
(2) - (1) ADSL standard prices	14.78	17.40	17.99	17.04	18.06		
(3) - (1) ADSL promotional prices	9.92	12.50	7.89	4.61	6.59		

Source: Simplify Digital

Figure 1.31: Indexed prices of SFV services and ADSL dual-play bundles (£/month, June 2017 prices)



Source: Simplify Digital

Notes: All prices indexed to the earliest data point available at the start of Q1 2013.

## SFV prices and standalone broadband prices comparison with dual play prices

- 1.88 We have collected data from BT, Plusnet, PostOffice, Sky, and TalkTalk, on the prices paid by their standalone fixed broadband customers and the number of customers on each tariff. We have used this information to estimate each CP's average standalone fixed broadband price weighted by the number of customers on each tariff.
- 1.89 [redacted].<sup>91 92</sup> In total, over 80% of standalone fixed broadband customers, supplied by BT, Sky and TalkTalk, Plusnet receive a standalone fixed broadband with a speed of 17Mb.<sup>93</sup>
- 1.90 The table below shows the price for each 17Mb standalone broadband service (in terms of speed and usage limit) provided by BT, Sky and Talktalk. We present average price weighted by the number of customers on each usage and price combination for each standalone fixed broadband service. In some instances, customers receiving the same service are paying different prices.
- 1.91 It shows that on average customers purchasing 17Mb standalone broadband pay £23.73 and £18.99 for line rental.<sup>94</sup> Compared to average dual-play prices which split purchasers would pay if they bundled these services, they are paying an average of £17.83 more per month compared to promotional dual-play prices or £7.87 more per month compared to standard dual-play prices. However, this variation depends by operator as shown below.

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<sup>91</sup> We exclude customers who receive a standalone fixed broadband service from BT (a) free of charge, and (b) where the price and service combinations are provided to fewer than 100 customers.

<sup>92</sup> We exclude Sky customers who take a 17Mb/2Gb service and a 6Mb/Unlimited service, since there is no closely comparable dual play product, in terms of speed/usage combinations.

<sup>93</sup> Approximately 85% of these customers had unlimited usage, whilst 15% have a capped usage.

<sup>94</sup> We use a line rental price of £18.99, since we estimate that the majority of split purchasers take their line from BT.

## Evidence supporting the review of the market for standalone landline telephone services

Table 1.32: Standalone fixed broadband prices, and promotional and standard dual-play prices

		(1)	(2)	(3)	(4)	(5) = (3)–(2)	(6) = (4)–(2)
	Download speed / Data usage cap	Standalone fixed broadband weighted average price (Q1 2017)	Standalone fixed broadband + Monthly line rental (£18.99)	Cheapest promotional dual-play price	Cheapest standard dual-play price	Difference to promotional dual-play price	Difference to standard dual-play price
BT	17Mb / 12Gb	32.89	51.88	24.99	34.99	-26.89	-16.89
BT	17Mb / 25Gb	25.44	44.43	24.99	34.99	-19.44	-9.44
BT	17Mb / Unlimited	33.79	52.78	24.99	34.99	-27.79	-17.79
Sky	17Mb / Unlimited	15.16	34.15	20.00	28.99	-14.15	-5.16
TalkTalk	17Mb / Unlimited	22.71	41.70	19.95	27.00	-21.75	-14.70
<b>Weighted average</b>	<b>Various</b>	<b>23.73</b>	<b>42.72</b>	<b>24.89</b>	<b>34.85</b>	<b>-17.83</b>	<b>-7.87</b>

Source: S135 response data; dual-play promotional and standard prices from operator websites (accessed 21 August 2017)

Notes: For BT 17Mb / 25Gb we use the promotional and standard price of a 17Mb/12Gb service as a proxy for 17Mb/25Gb, since this usage limit is no longer available.

1.92 Table 1.33 also compares the price difference between SFV services and Standalone Broadband and ADSL dual-play since 2015. The price of ASDL dual play including promotions has been £13-£14 cheaper. However when a simple average of dual play ASDL standard prices is taken the difference is less pronounced.

## Evidence supporting the review of the market for standalone landline telephone services

**Table 1.33: SFV services plus Standalone Broadband and ADSL dual-play bundles (£/month, June 2017 prices)**

	Q2 2015	Q2 2016	Q1 2017	% change (2015- 2017)	£ change (2015- 2017)
(1) Standalone fixed broadband + line rental	38.51	38.91	42.72	11%	4.21
(2) ADSL dual-play price: standard	35.02	39.09	39.97	14%	4.95
(3) ADSL dual-play price: including promotions	25.15	25.18	28.50	13%	3.35
	<b>Difference to standalone fixed broadband + line rental</b>				
(2) - (1) ADSL standard prices	-3.49	0.18	-2.75		
(3) - (1) ADSL promotional prices	-13.36	-13.73	-14.22		

Source: Simplify Digital for ADSL and line rental prices, and s135 responses for standalone fixed broadband prices.

## Estimates of revenue per line

1.93 In this section we estimate the revenue per line, across communications providers from 2013/14 to 2016/17.

1.94 Figure 1.34 presents SFV total revenue per line figures, calculated by dividing SFV total revenues by the number of SFV lines for BT, Post Office, SSE, TalkTalk, Virgin Media, Sky, and the Phone Co-op.

**Figure 1.34: SFV total revenue per line (£/month, June 2017 prices)**

[X]

Source: S135 responses

1.95 SFV total revenue per line has been increasing for some communications providers and decreasing for others. [X]

1.96 Figure 1.35 below, presents the access revenue per SFV line by operator (in real terms). This is equivalent to the line rental price.

**Figure 1.35: Access revenue per SFV line (£/month in June 2017 prices)**

[X]

Source: S135 responses

**Evidence supporting the review of the market for standalone landline telephone services**

1.97 [redacted] had the highest access revenue per line in the seven financial years between 2010/11 and 2016/17.

1.98 Figure 1.36 below presents non-access revenue per SFV line by operator per month in real terms. Non-access revenues are a proxy for revenues across all call types.<sup>95</sup> To calculate non-access revenue we subtract total access revenue from total SFV revenue, divided by the number of SFV lines.

**Figure 1.36: Non-access revenue per SFV line (£/month in June 2017 prices)**

[redacted]

Source: S135 responses

1.99 All communications providers' non-access revenue have fallen over 2013/14 to 2016/17, but by significantly different amounts. [redacted]

1.100 Figure 1.37, below, presents the annual non-access revenues per minute by operator for the past four financial years.<sup>96</sup>

**Figure 1.37: Non-access revenues per minute (pence per minute, June 2017 prices)<sup>97</sup>**

[redacted]

Source: s.135 responses

**Consumer characteristics****Survey evidence introduction**

1.101 This section presents some of the characteristics of SFV customers based on three consumer research studies:

- The 2017 NMR residential survey;<sup>98</sup>
- The Ofcom Technology Tracker, H1 2017;<sup>99</sup> and

<sup>95</sup> Non-access revenue is an overestimate of call revenue because non-access includes revenues which are neither from calls nor access (e.g. charges for paper billing and ancillary services).

<sup>96</sup> The figures presented in the February 2017 consultation were calculated using an average of the number of minutes in each month rather than a sum. This significantly overestimated the non-access revenues per minute, however, all CPs were out by approximately by the same factor (depending on the relative rate of decline in calls) and so the analysis is not affected. The corrected figures are presented here.

<sup>97</sup> In the February 2017 consultation, non-access revenues per minute were mistakenly calculated using the average number of calls over the financial year rather than the total number of calls. There is no impact to the analysis as all numbers were overstated by approximately the same factor.

<sup>98</sup> Run by Saville Rossiter-Base on behalf of Ofcom to understand the choices that residential consumers make regarding their use of fixed telecoms services, and to explore how they might react to hypothetical changes in the prices of their services. This is part of wider research also looking at business consumers to support the 2017 Narrowband Market Review. Detailed results can be found here: <https://www.ofcom.org.uk/consultations-and-statements/category-1/narrowband-market-review>

<sup>99</sup> Run by Saville Rossiter-Base on behalf of Ofcom to track the attitudes and behaviour of the general public with respect to the residential telecommunications market as well as broadcasting more generally.

## Evidence supporting the review of the market for standalone landline telephone services

- The Ofcom Switching Tracker, 2016.<sup>100</sup>
- 1.102 The evidence set out from the 2017 NMR residential survey is an update to the previous 2015 Jigsaw Research Survey (which is not presented in this document). The Ofcom Technology Tracker H1 2017 is an update to Ofcom Technology Tracker H2 2016 which was presented in the February Consultation. Evidence from Switching Tracker is replicated from the February Consultation.
- 1.103 In the context of consumer surveys, isolating the split-service customer segment is problematic.
- 1.104 In the Technology Tracker and Switching Tracker, the number of customers who reported that they do not bundle landline and broadband was unreasonably high, and therefore not comparable with more reliable s.135 data. This may be due to respondents either (a) not realizing that the line rental component of a dual-play bundle equates to bundling voice services with fixed broadband, or (b) not acknowledging that they bundle landline and fixed broadband when they pay the same supplier for both of these services.
- 1.105 The 2017 NMR residential survey corrects for this by instead asking respondents who receive landline and broadband services from a single provider whether they receive a single bill, or separate bills for their services. The results from this survey are in a more realistic order of magnitude<sup>101</sup> but the number of respondents only totalled 83. Given the small sample size, and to provide consistency with the other surveys we have not isolated this split-service customer segment.
- 1.106 We believe split-supply customers to be a reasonable proxy for split-purchasers as we estimate that split-supply customers account for around 80% of split-purchasers, with the remaining 20% being split-service customers.
- 1.107 For these reasons, we have defined the groups outlined below in Figure 1.38 for our analysis of consumer survey evidence.

**Table 1.38: Groups used for consumer survey evidence**

Group name	Definition
Voice-only	Landline, no fixed broadband
Split-supply	Landline and fixed broadband, with different suppliers
Dual-play	Landline and fixed broadband with the same supplier <sup>102</sup>

<sup>100</sup> Run by Saville Rossiter-Base on behalf of Ofcom to monitor the general public's switching and engagement behaviour with communications services.

<sup>101</sup> Although still overestimated by a factor of between 2 and 3.

<sup>102</sup> This group will contain an immaterial number of split-service customers, which does not affect our analysis of this group within our analysis of survey evidence.

## Evidence supporting the review of the market for standalone landline telephone services

## Demographics of SFV customers

1.108 This section presents evidence on SFV customer demographics broken down into voice-only and split-supplier customers in terms of age, socioeconomic grade, working status, and income. The sources of this data are the 2017 NMR residential survey and the Ofcom Technology Tracker (H1 2017).

### Evidence on age<sup>103</sup>

1.109 The 2017 NMR residential survey and Technology Tracker collected information on age for voice-only, split-supply, and dual-play customers. These are presented in Table 1.39 (2017 NMR residential survey) and Table 1.40 (Technology Tracker) below. Both figures also include information on age for the overall UK population for comparability purposes.

**Table 1.39: Information on age (2017 NMR residential survey)**

	Voice-only customers	Split-supply customers	Dual-play customers	UK population
<b>Unweighted base</b>	<b>266</b>	<b>282</b>	<b>2,223</b>	<b>53,257,957</b>
16-24	3%	4%	11%	14%
25-34	9%	12%	22%	17%
35-54	19%	35%	37%	33%
55-64	11%	22%	14%	14%
65-74	18%	20%	11%	12%
75+	41%	7%	7%	10%

Source: 2017 NMR residential survey, and ONS (mid 2016)

<sup>103</sup> In the February Consultation we presented data on the distribution of SFV customers by age group based on s135 responses. We have not replicated this data here.

## Evidence supporting the review of the market for standalone landline telephone services

**Table 1.40: Information on age (Technology Tracker)**

	Voice-only customers	Split-supply customers	Dual-play customers	UK population
<b>Unweighted base</b>	<b>450</b>	<b>157</b>	<b>2,672</b>	<b>53,257,957</b>
16-24	4%	19%	14%	14%
25-34	4%	12%	18%	17%
35-54	12%	38%	38%	33%
55-64	14%	13%	15%	14%
65-74	23%	12%	11%	12%
75+	43%	5%	5%	10%

Source: Ofcom Technology Tracker (H1 2017), and ONS (mid 2016)

**Evidence on socioeconomic grade**

1.110 The 2017 NMR residential survey and Technology Tracker collected information on socioeconomic grade for voice-only, split-supplier, and dual-play customers. These are presented in Table 1.41 (2017 NMR residential survey) and Table 1.40 (Technology Tracker) below.

**Table 1.41 Information on socioeconomic grade (2017 NMR residential survey)**

	Voice-only customers	Split-supplier customers	Dual-play customers
<b>Unweighted base</b>	<b>266</b>	<b>282</b>	<b>2223</b>
AB	16%	41%	29%
C1	17%	27%	28%
C2	31%	12%	22%
DE	35%	20%	20%

Source: 2017 NMR residential survey



## Evidence supporting the review of the market for standalone landline telephone services

Table 1.42: Information on socioeconomic grade (Technology Tracker)

	Voice-only customers	Split-supplier customers	Dual-play customers
<b>Unweighted base</b>	<b>450</b>	<b>157</b>	<b>2672</b>
AB	14%	26%	31%
C1	19%	28%	28%
C2	27%	31%	21%
DE	40%	16%	20%

Source: Ofcom Technology Tracker, H1 2017

## Evidence on working status and household income levels

1.111 The 2017 NMR residential survey and Technology Tracker collected information on working status and household income for voice-only, split-supplier, and dual-play customers. This is presented in Tables 1.43 and 1.44 below.

Table 1.43: Information on working status (2017 NMR residential survey)

	Voice-only customers	Split-supplier customers	Dual-play customers
<b>Unweighted base</b>	<b>266</b>	<b>282</b>	<b>2223</b>
Working	30%	54%	63%
Not working	70%	47%	36%
	<b>Income</b>		
Under £10,399	15%	5%	6%
£10,400 - £15,599	15%	13%	10%
£15,600 - £25,999	11%	18%	15%
£26,000 - £36,399	5%	16%	16%
£36,400+	3%	31%	22%
No response	49%	18%	32%

Source: 2017 NMR residential survey

## Evidence supporting the review of the market for standalone landline telephone services

Table 1.44: Information on socioeconomic grade (Technology Tracker)

	Voice-only customers	Split-supplier customers	Dual-play customers
<b>Unweighted base</b>	<b>450</b>	<b>157</b>	<b>2672</b>
Working	21%	63%	64%
Not working	79%	37%	36%
	Income		
Under £11,500	16%	3%	4%
£11,500 - £17,499	14%	6%	7%
£17,500 - £29,999	8%	11%	10%
£30,000+	6%	15%	22%
No response	56%	65%	58%

Source: Ofcom Technology Tracker, H1 2017

## Landline and mobile usage

### Mobile usage

- 1.112 The 2017 NMR residential survey suggests that a considerably lower proportion of voice-only customers (72%) have access to a mobile phone, compared to 92% of split-supplier customers. Dual-play customers are slightly more likely to have access to a mobile phone, with 97% of respondents stating they do.
- 1.113 This is supported by the Technology Tracker, which indicates that 65% of voice-only customers have access to a mobile phone, much lower than split-supplier customers and dual-play customers (96% and 98% respectively).<sup>104</sup>
- 1.114 9% of voice-only customers reported that they had access to mobile broadband (through a USB modem or 'dongle', rather than fixed broadband). This percentage is similar to dual-play and split-supplier customers (8%).

### Landline usage

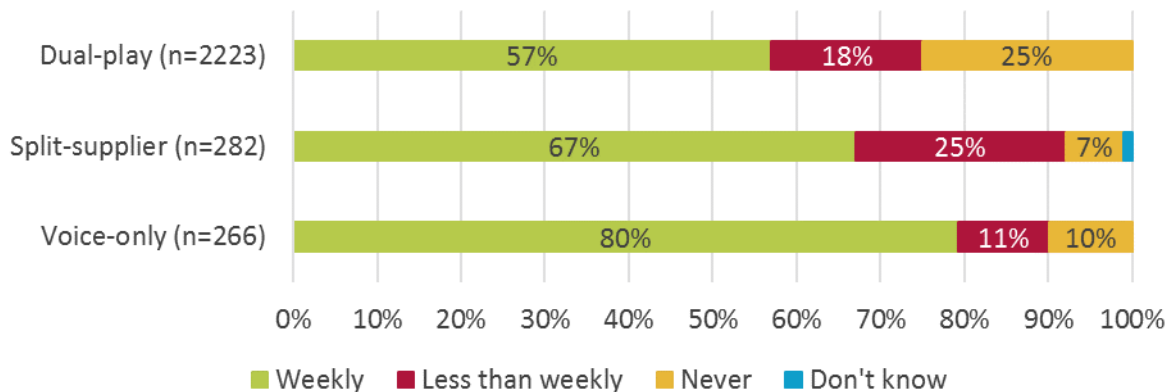
- 1.115 Overall, a similar proportion of voice-only and split-purchase customers use their landline to make calls at all (91% and 92% respectively), compared to 75% of dual-play customers.

<sup>104</sup> Ofcom, Technology Tracker, H1 2017.

Evidence supporting the review of the market for standalone landline telephone services

However, voice-only customers are more likely to make landline calls on a weekly basis (80%) than the other two groups.

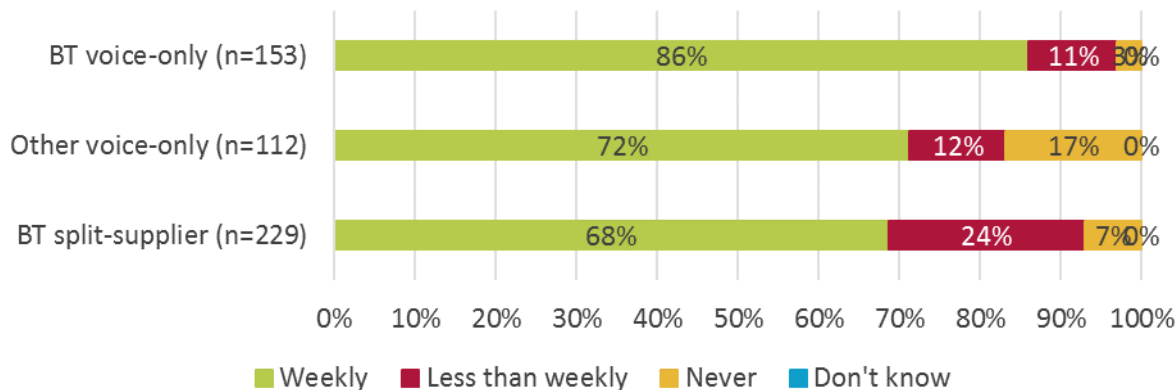
Figure 1.45: Frequency of making landline calls



Source: 2017 NMR residential survey

1.116 Figure 1.46 suggests that BT voice-only customers make landline calls on a more regular basis compared to voice-only customers of other providers. There is less of a distinction between BT and non-BT among the split-supplier customers.

Figure 1.46 Frequency of making landline calls: BT versus Other communications providers

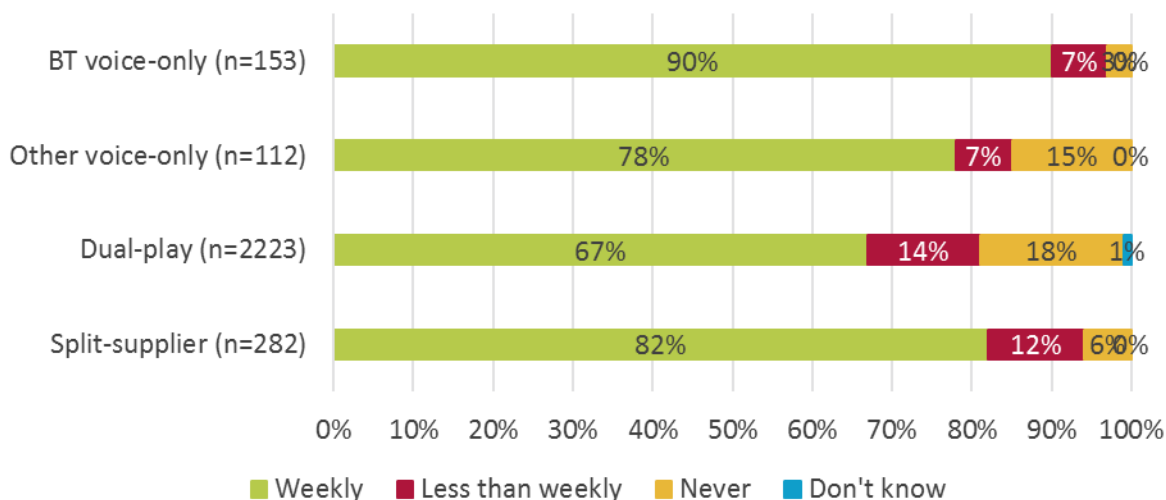


Source: 2017 NMR residential survey

1.117 Figure 1.47 suggests that voice-only customers tend to receive calls more frequently than split-supplier customers who, in turn, receive calls more frequently than dual-play customers. BT customers also cited receiving calls more frequently than non-BT customers.

## Evidence supporting the review of the market for standalone landline telephone services

Figure 1.47: Frequency of receiving landline calls



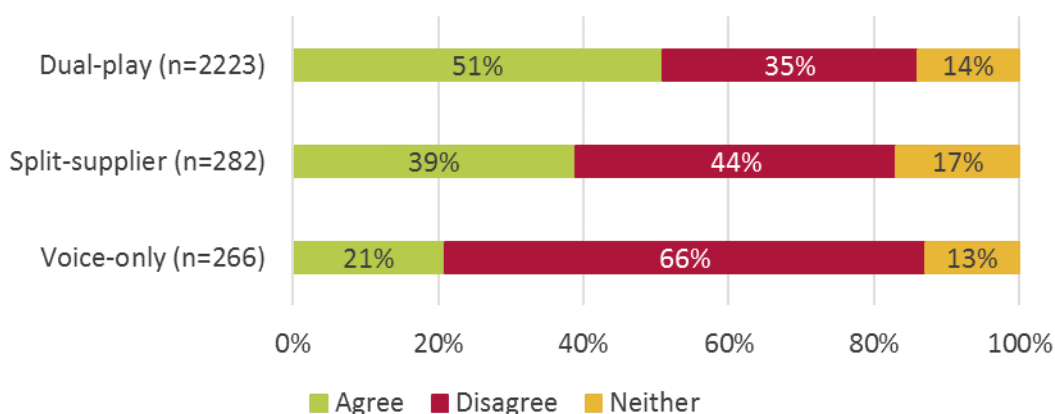
Source: 2017 NMR residential survey

## Attachment to landline services

1.118 Respondents were asked whether they agree with the statement “Under certain circumstances, I would be prepared to give up the ability to make and receive calls from my landline”. Figure 1.48 shows that voice-only customers appear to have a stronger attachment to their landline - two thirds disagreed with the statement, compared to 44% for split-purchaser customers, and 35% for dual-play customers.

Figure 1.48: Willingness to give up landline calls

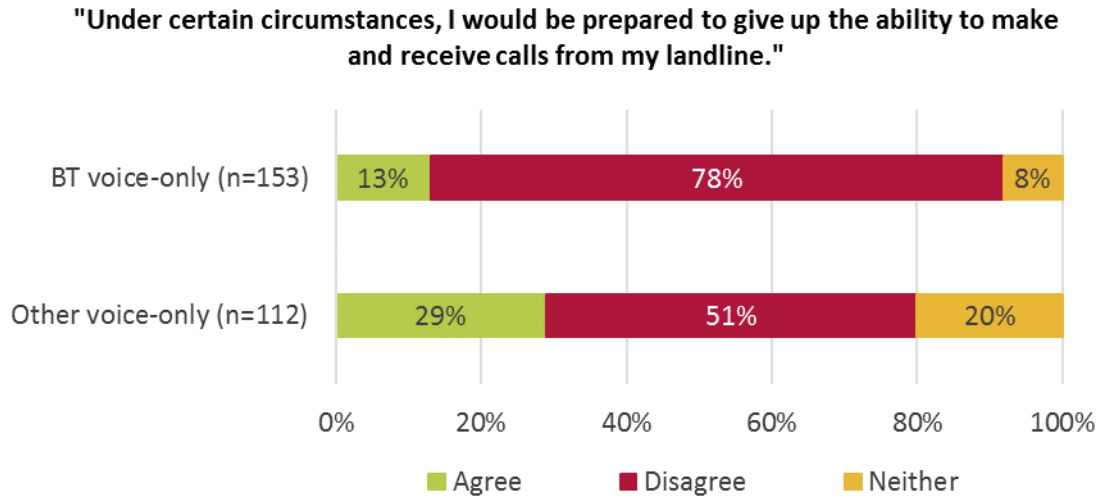
**"Under certain circumstances, I would be prepared to give up the ability to make and receive calls from my landline."**



Source: 2017 NMR residential survey

1.119 Among voice-only customers, those who use BT appear less willing to give up their landline than those with other providers – close to 8 in 10 of the former disagreed with the statement compared to around half for the latter.

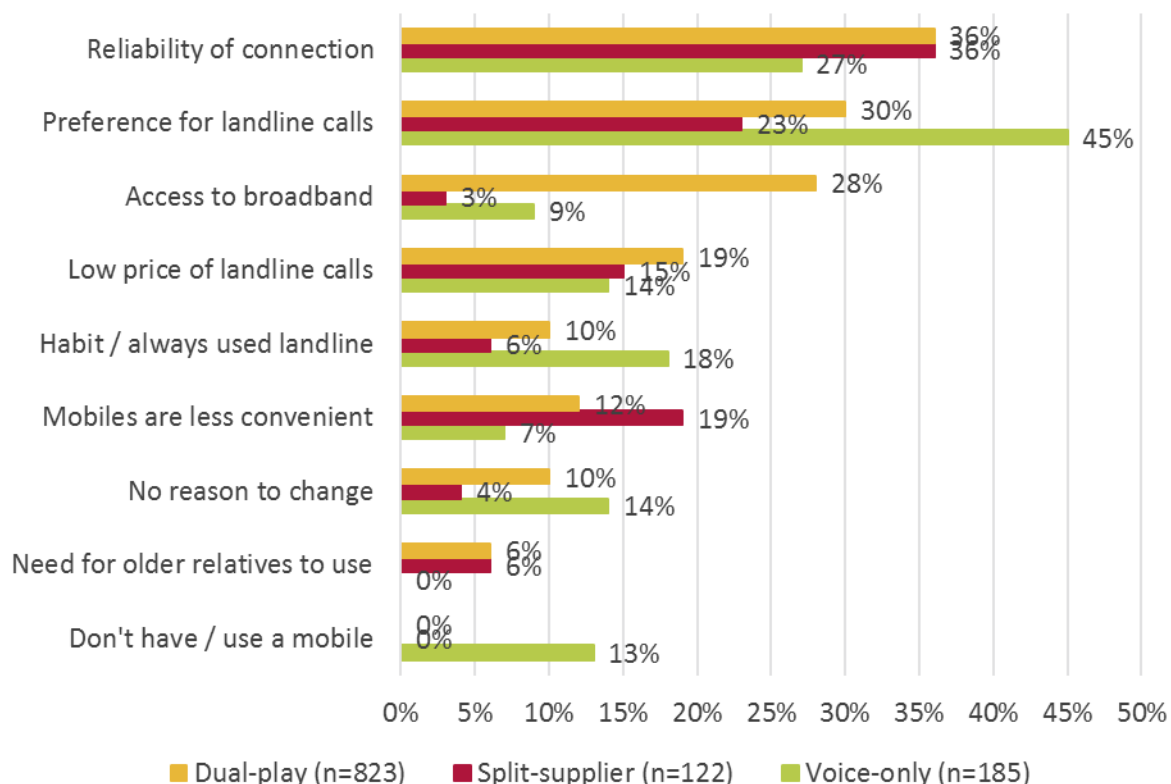
Figure 1.49: Willingness to give up landline calls: BT versus other communications providers



Source: 2017 NMR residential survey

- 1.120 As a follow up to the agreement statement, respondents who said they were not willing to give up making and receiving landline calls under any circumstances were asked why. As shown in Figure 1.50 the main reason cited by voice-only customers was a general preference for making calls on a landline (45%), whereas for dual-play and split-supplier customers reliability of connection was seen as more important.

## Evidence supporting the review of the market for standalone landline telephone services

Figure 1.50: Reasons for unwillingness to give up landline calls<sup>105</sup>

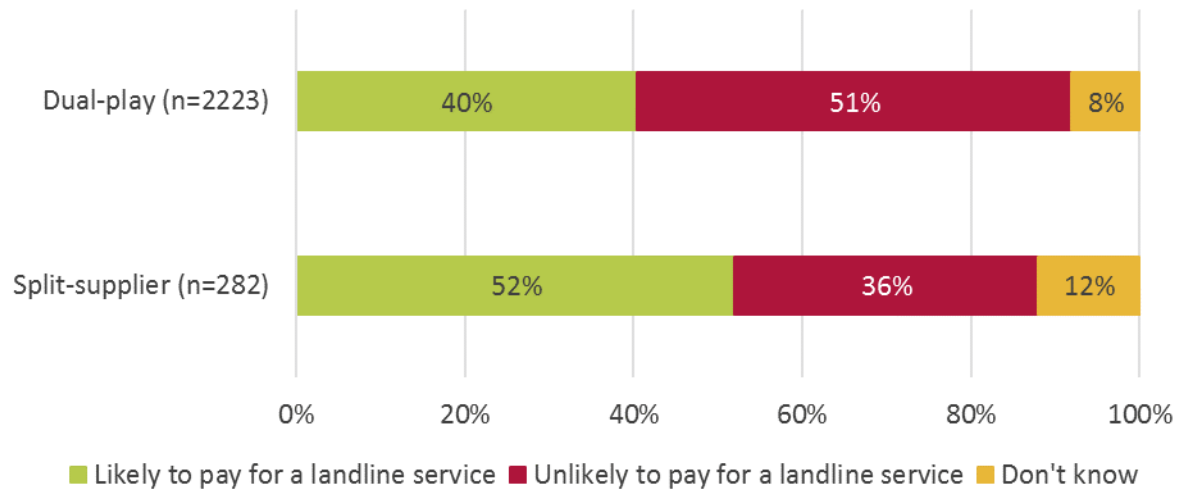
Source: 2017 NMR residential survey

1.121 We asked customers who had a fixed broadband service whether they would be likely to continue paying for a landline service if they could have broadband as a standalone service. Compared to split-supplier customers (52%), a lower proportion of dual-play customers (40%) said they would.

<sup>105</sup> This presents the main reasons reported by customers. We have omitted responses for which less than 5% of each customer group reported.

## Evidence supporting the review of the market for standalone landline telephone services

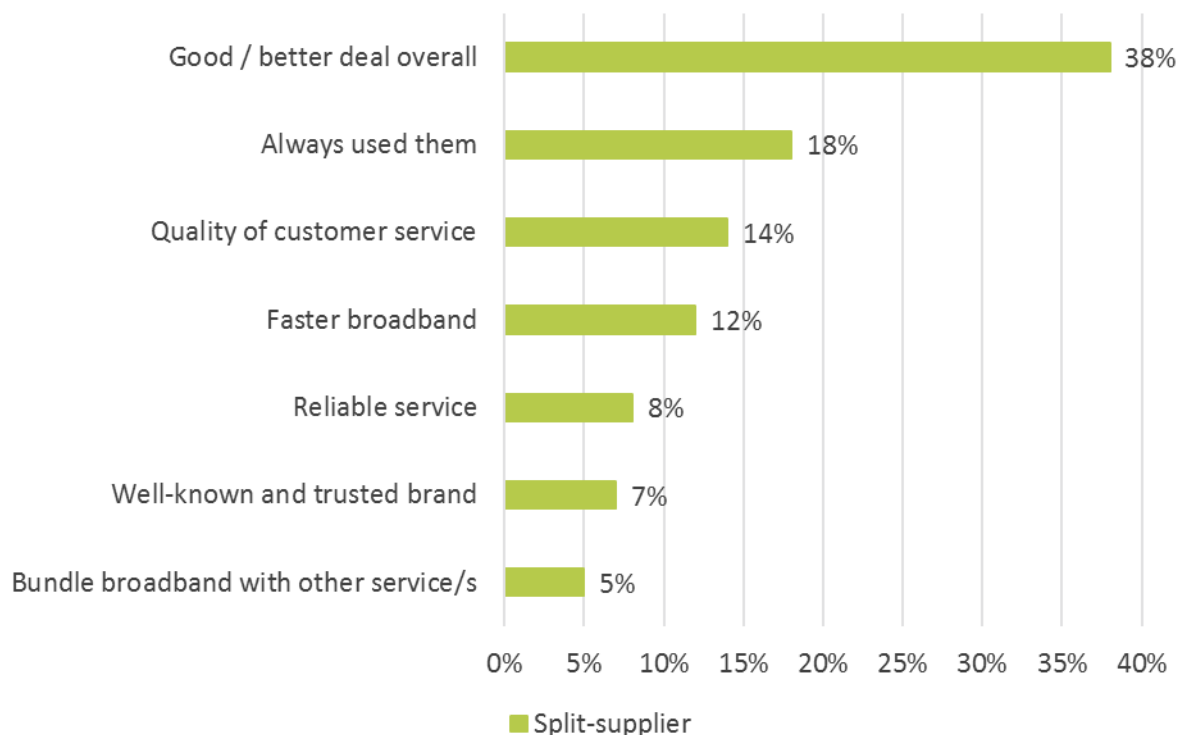
Figure 1.51: Paying for a landline service if not required for fixed broadband



Source: 2017 NMR residential survey

### Reasons to be a split-supplier

1.122 Split-supplier customers were asked why they purchased a broadband service from a different supplier to their landline. The most common reason was that they got a good, or better deal from separate suppliers and this was reported by 38% of split-supplier customers. Other commonly reported reasons were having always used them (18%), quality of customer service (14%), faster broadband (12%), reliable service (8%), well-known and trusted brand (7%), and to bundle broadband with other services (5%).

**Figure 1.52: Reasons for purchasing broadband from a different supplier to their landline<sup>106</sup>**

Source: 2017 NMR residential survey

## Engagement, switching, and satisfaction levels

- 1.123 The Ofcom Switching Tracker uses an engagement index which measures past and current switching behaviour and interest in the market through survey questions. Those who are “inactive” may have had some past involvement, but have a low interest in the market. Those who are “passive” are more likely to have participated in the past and indicate some interest in the market. Those who are “interested” are similar to those who are passive, but are more likely to keep an eye on the market and look out for better deals. Those who are “engaged” are the most active group in terms of past and current behaviour. The index scores associated with the consumer’s behaviour categorises the consumer.<sup>107</sup>
- 1.124 Only 6% of voice-only customers are classified as engaged, compared to 20% of dual play customers. Split-supplier customers have a higher level of engagement than voice-only, with 15% classified as engaged. The difference between split-supplier and dual-play is not statistically significant.

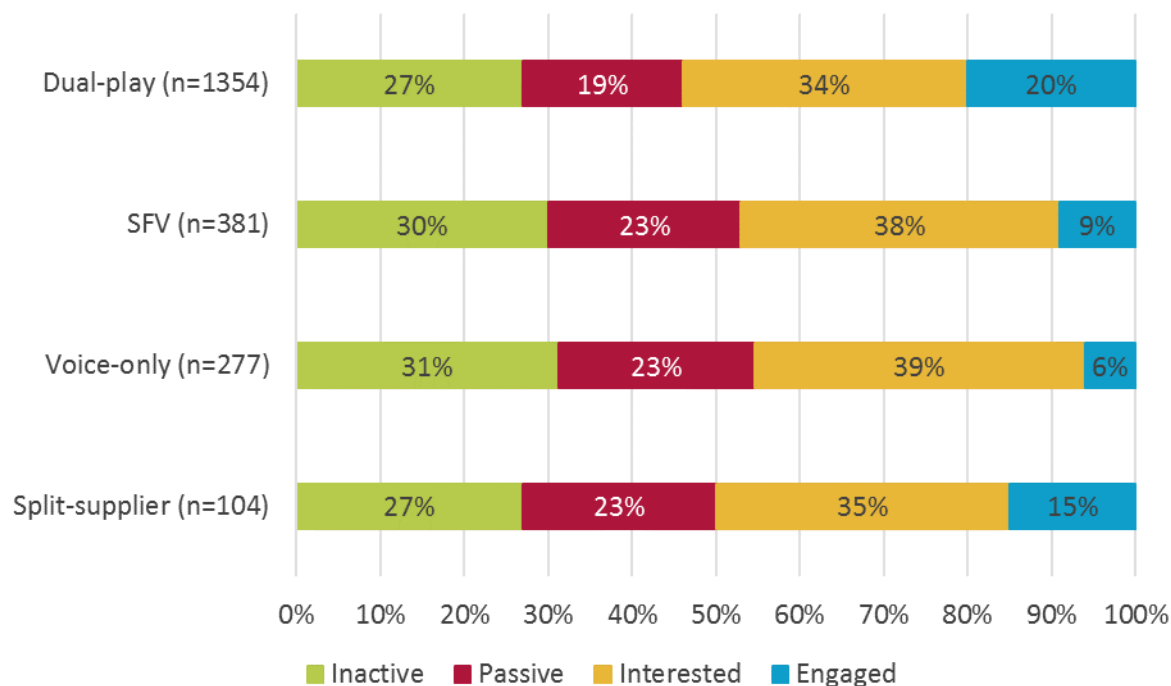
<sup>106</sup> This presents the main reasons reported by customers. We have omitted responses for which less than 5% customers reported.

<sup>107</sup> 2017 NMR residential survey.



## Evidence supporting the review of the market for standalone landline telephone services

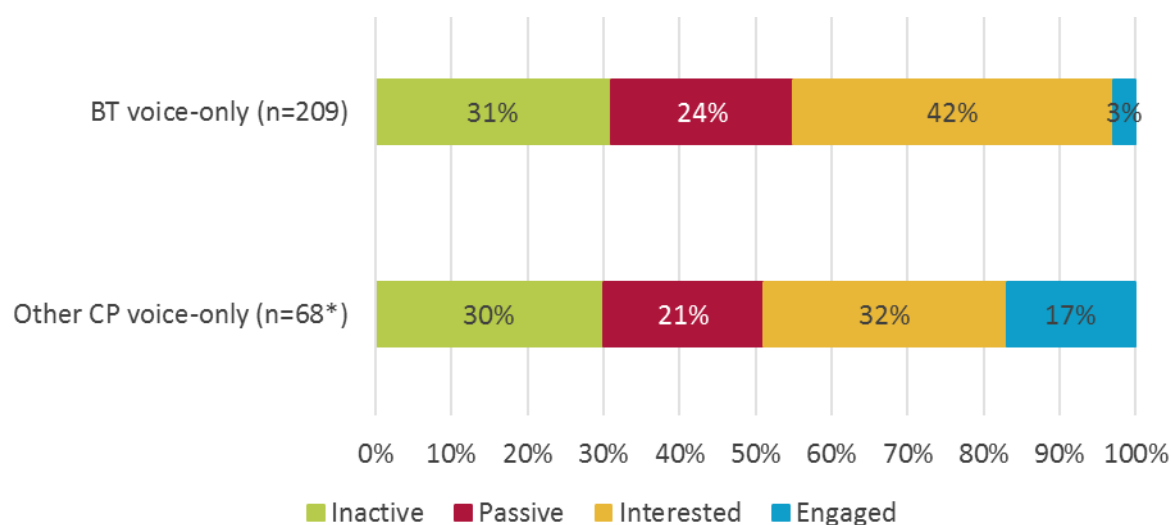
Figure 1.53: Engagement levels in relation to fixed line services



Source: Ofcom switching tracker, July – August 2016

1.125 Figure 1.54 indicates that BT voice-only customers are less engaged compared to customers of other communications providers. Only 3% of BT SFV customers are classified as engaged, compared to 17% of other CP SFV customers (although the sample size is small).

Figure 1.54: Engagement levels in relation to fixed line services: BT versus Other communications providers



Source: Ofcom switching tracker, July – August 2016

Notes: \*Caution:base under 100.

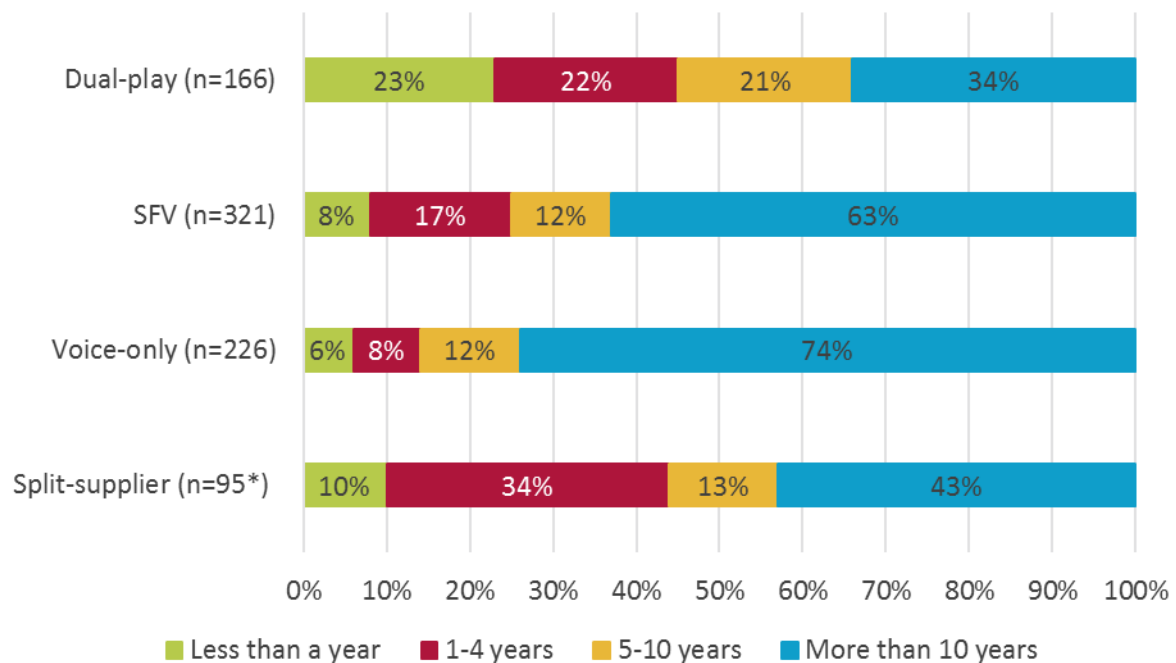
## Evidence supporting the review of the market for standalone landline telephone services

1.126 The 2017 NMR residential survey did not create an overall engagement index, however it did ask consumers questions on switching and their level of activity in the market. This is presented later in the annex.

**Length of time with current provider**

1.127 Figure 1.55 below indicates that a comparatively high proportion (74%) of voice-only customers have been with their current landline provider for more than 10 years.

**Figure 1.55: Length of time with current landline provider**

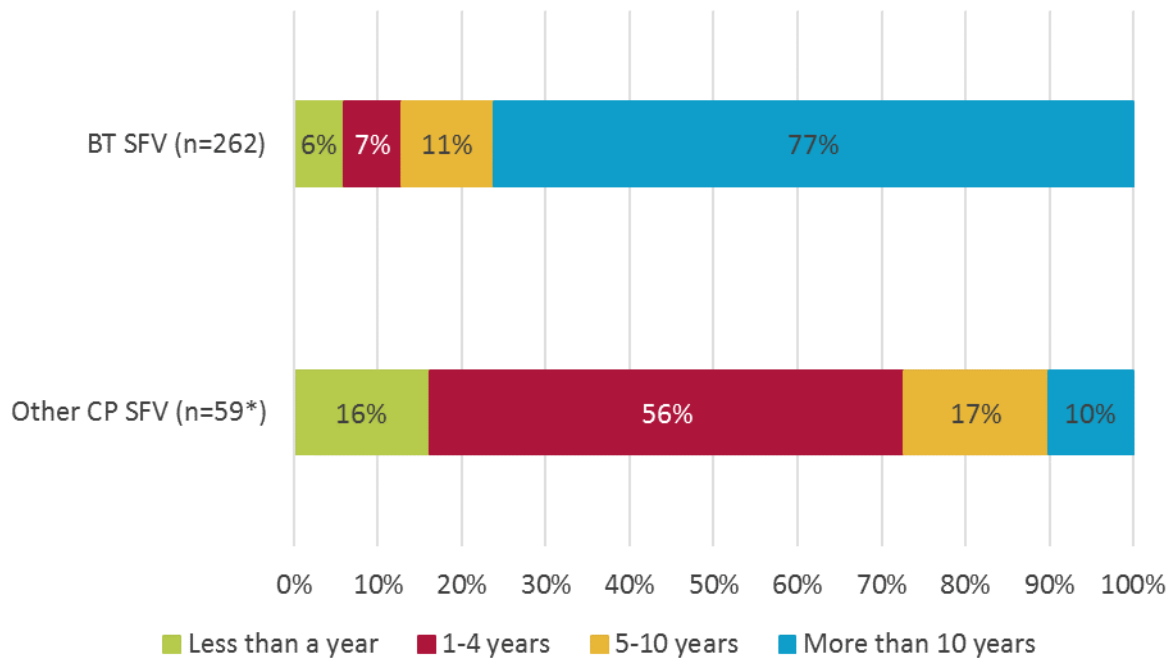


Source: Ofcom switching tracker, July – August 2016

Notes: \*Caution:base under 100.

1.128 Figure 1.56 below shows that a substantially higher proportion (77%) of BT SFV customers have been supplied by BT for more than 10 years as compared to voice-only customers with other communications providers (10%).

## Evidence supporting the review of the market for standalone landline telephone services

**Figure 1.56: Length of time with current landline provider: BT versus other communications providers**

Source: Ofcom switching tracker, July – August 2016

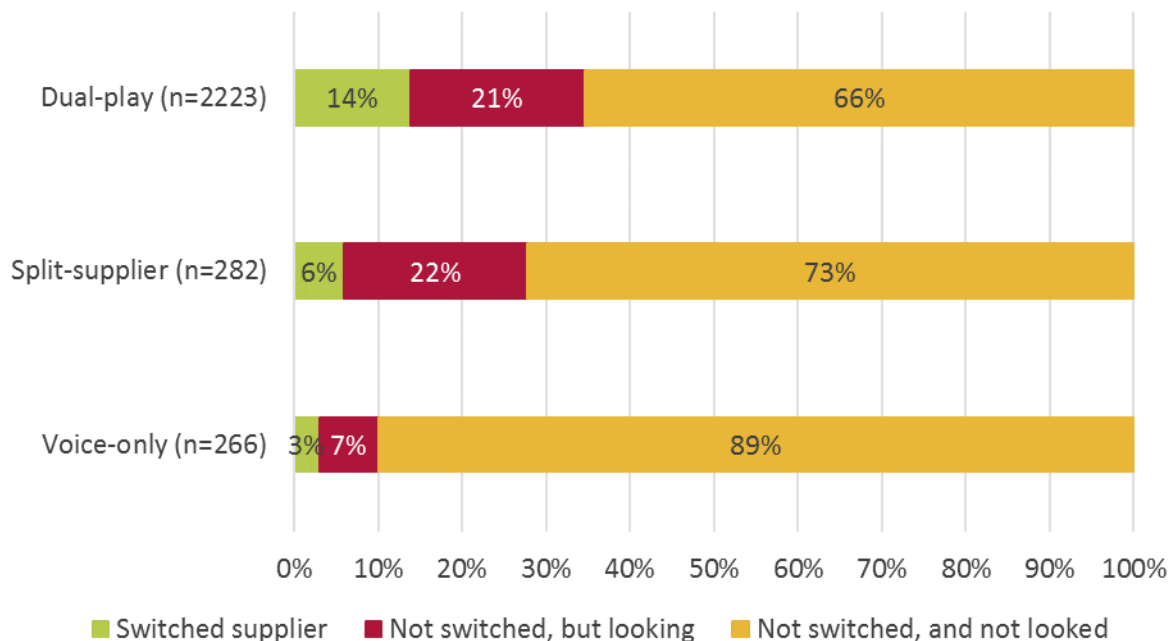
Notes: \*Caution: base under 100.

**Switching activity levels**

1.129 Figure 1.57 below shows that switching landline provider is less common among split-supplier customers than dual-play customers. Only 6% of split-supplier customers reported switching within the last 12 months, compared to 14% of dual-play customers. This is even lower for voice-only customers where only 3% said they switched in the last 12 months.

Evidence supporting the review of the market for standalone landline telephone services

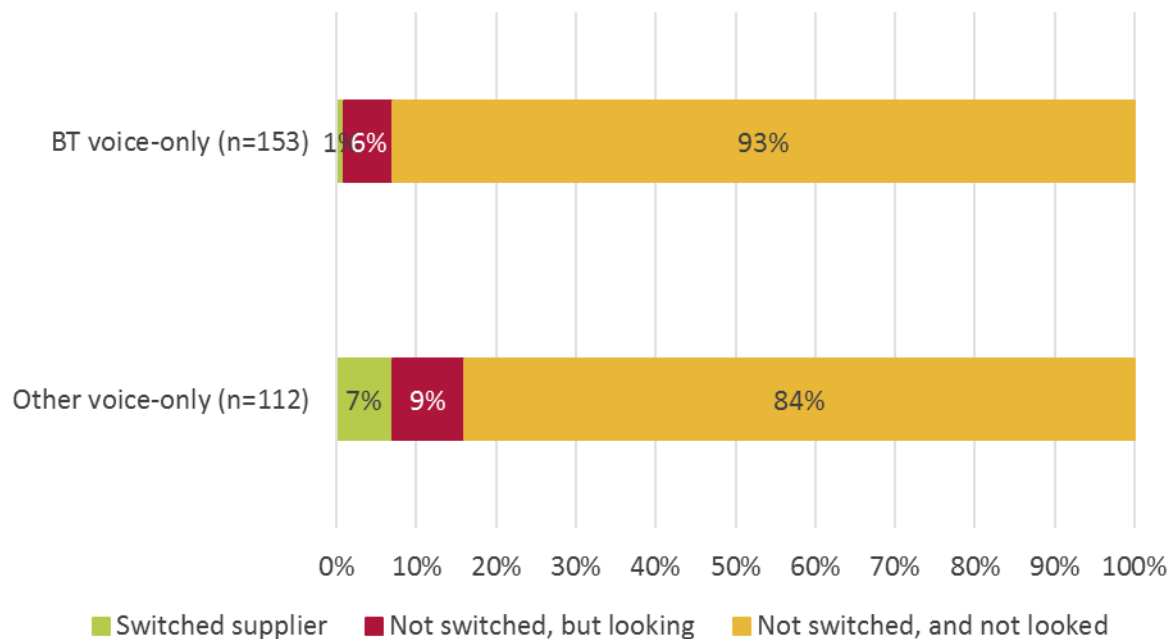
Figure 1.57: Switching activity in the past 12 months



Source: 2017 NMR residential survey

1.130 A greater proportion of BT voice-only customers said they had neither switched landline provider nor looked for information in the last 12 months (99%), compared to voice-only customers of other communications providers (93%).

Figure 1.58: Switching activity in the past 12 months: BT versus other communications providers

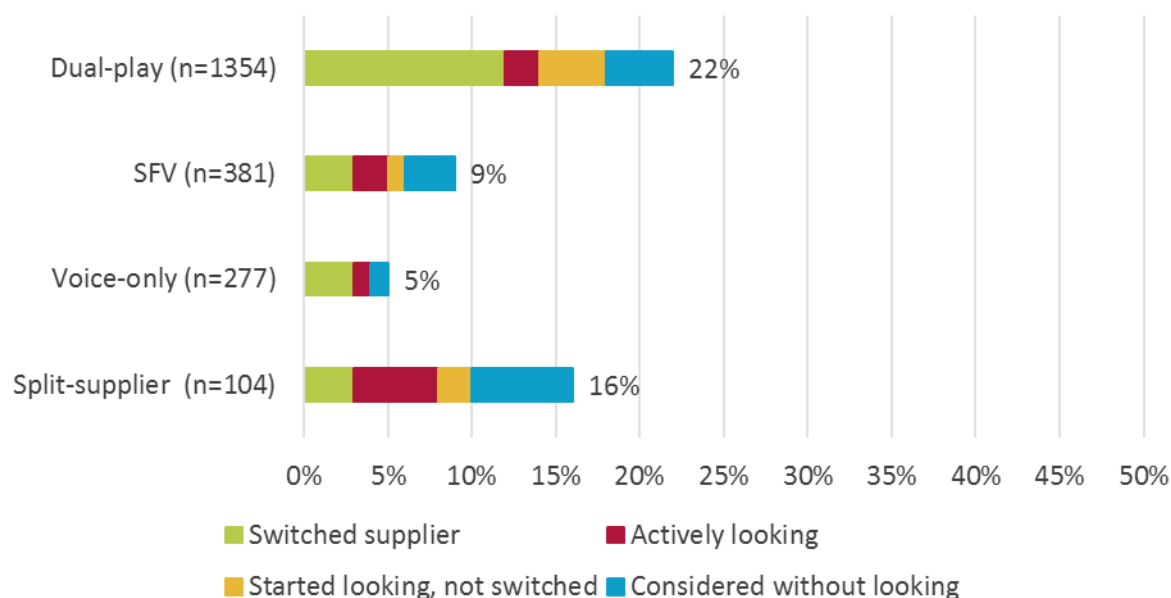


Source: 2017 NMR residential survey.

## Evidence supporting the review of the market for standalone landline telephone services

1.131 The switching tracker also looked at activity in the market. Both voice-only customers and split-supplier customers showed the same switching rates in the last 12 months of 3%, compared to 12% of dual-play customers.

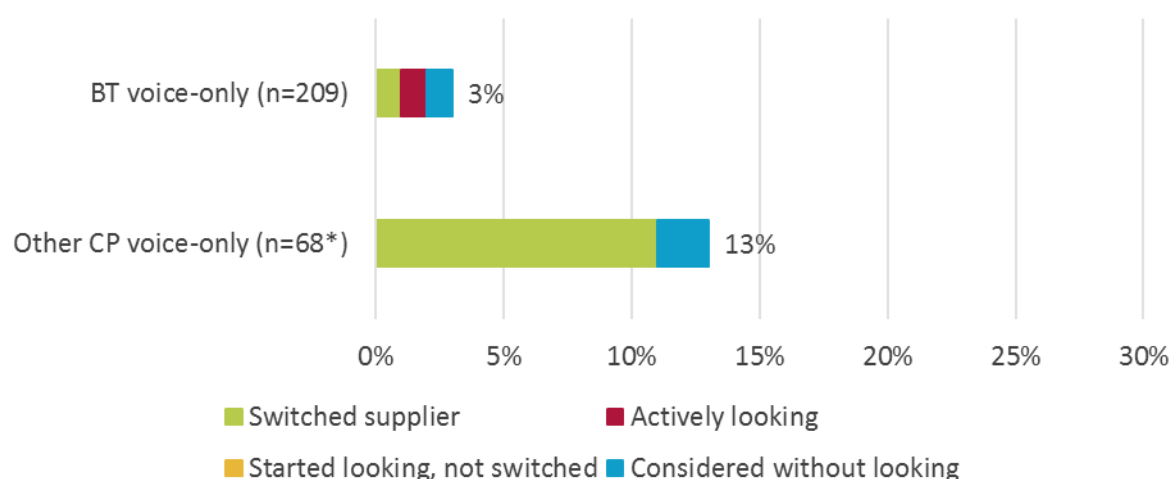
**Figure 1.59: Switching activity in the past 12 months**



Source: Ofcom switching tracker, July – August 2016

1.132 Figure 1.60 indicates that BT SFV and BT voice-only customers have lower reported switching activity compared to other CP's customers.

**Figure 1.60: Switching activity in the past 12 months: BT versus other communications providers**



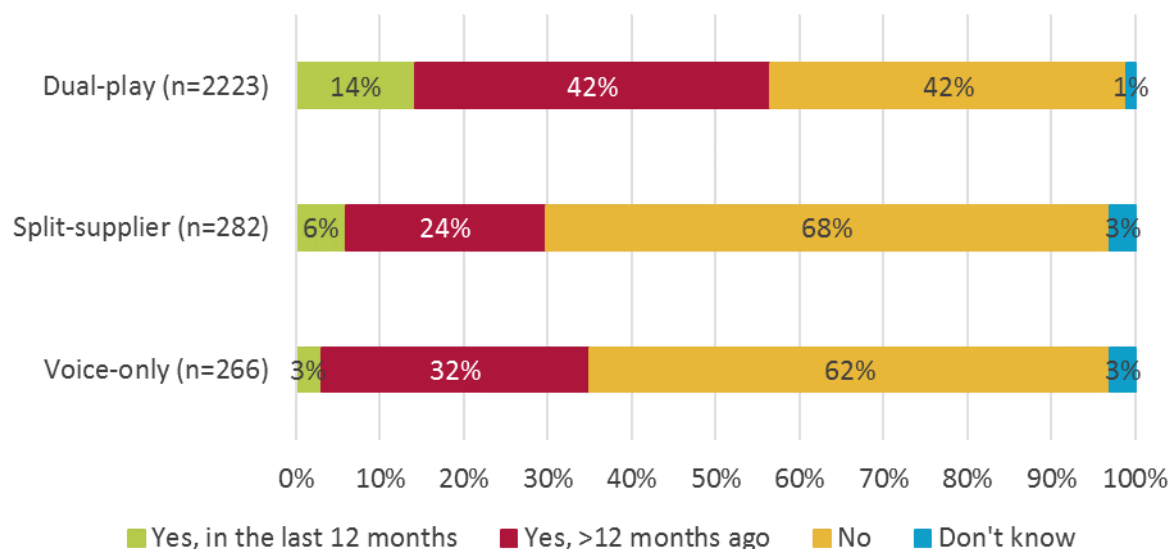
Source: Ofcom switching tracker, July – August 2016

Notes: \*Caution:base under 100.

## Evidence supporting the review of the market for standalone landline telephone services

1.133 Figure 1.61 shows that 62% of voice-only and 68% of split-supplier customers reported having never switched their landline provider. Dual-play customers were much more likely to have switched landline provider in the past, with 56% having done so.

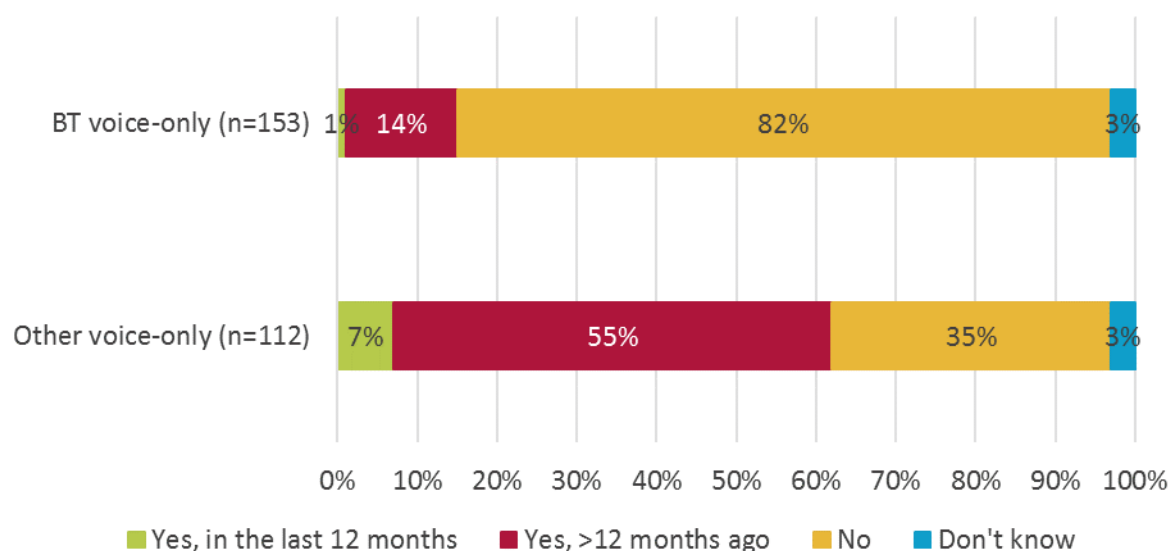
**Figure 1.61: Whether switched landline provider**



Source: 2017 NMR residential survey

1.134 When looking at these figures split between BT customers and other providers, the former were much less likely to say they had switched in the last 12 months or in their lifetime.

**Figure 1.62: Whether switched landline provider: BT versus Other communications providers**

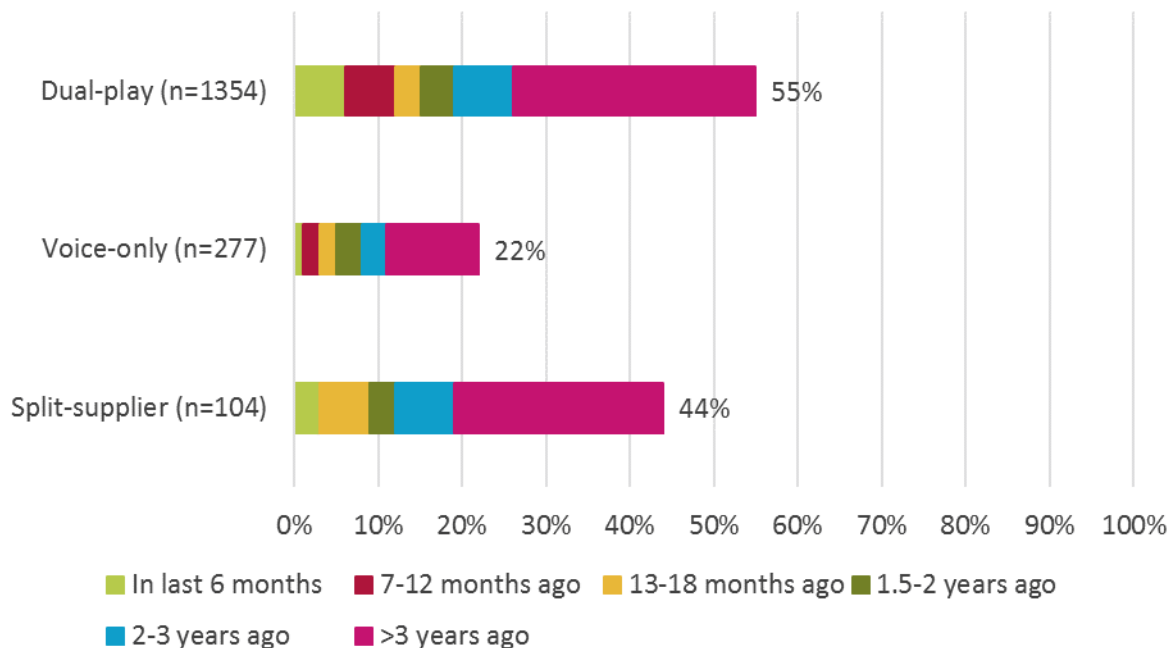


Source: 2017 NMR residential survey.

1.135 The switching tracker provided a slightly different picture. Only 22% of voice-only customers reported that they had ever switched their landline provider.

Evidence supporting the review of the market for standalone landline telephone services

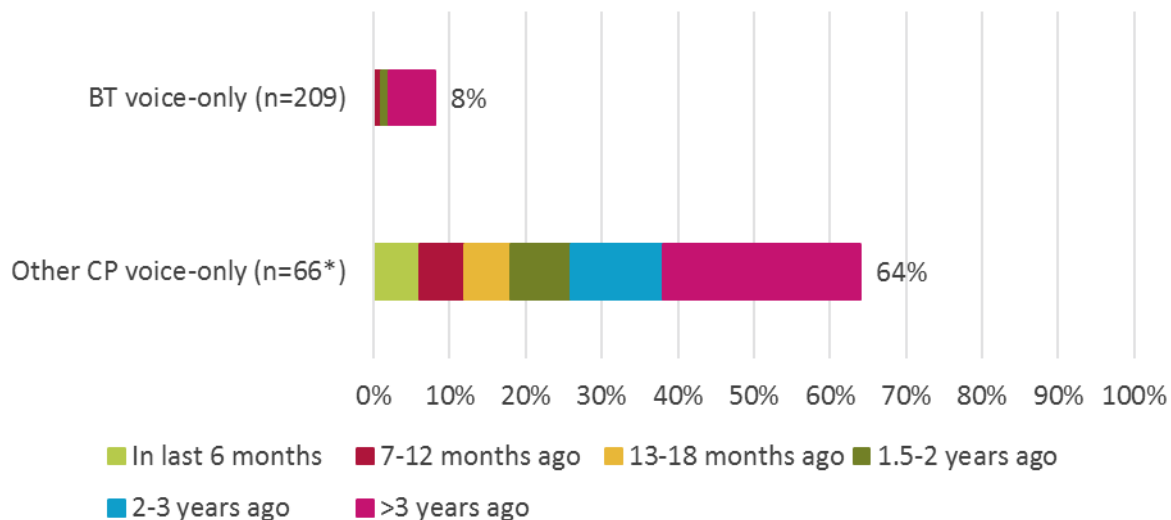
Figure 1.63: Whether switched landline provider



Source: Ofcom switching tracker, July – August 2016

1.136 Figure 1.64 presents this information broken down into BT customers and customers of other communications providers. A much lower proportion of BT voice-only customers reported having ever switched suppliers compared to customers with other communications providers.

Figure 1.64: Whether switched landline provider: BT versus other communications providers



Source: Ofcom switching tracker, July – August 2016

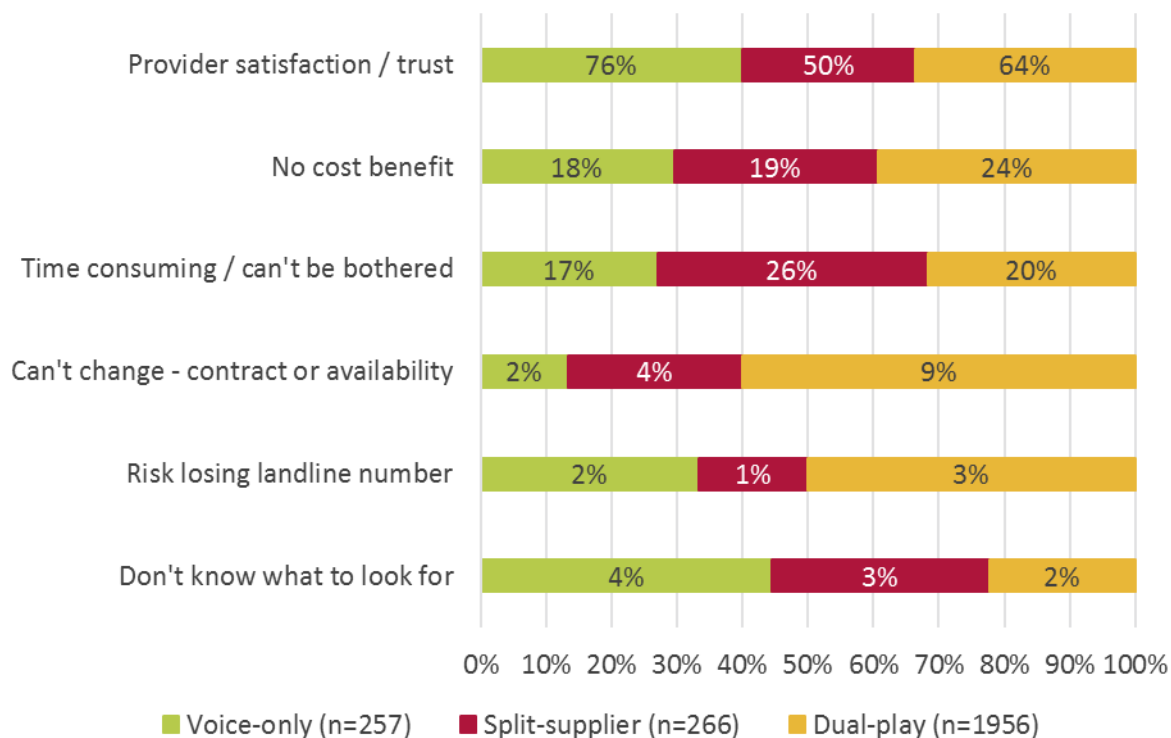
Notes: \*Caution:base under 100.

Evidence supporting the review of the market for standalone landline telephone services

**Reasons for not being interested in switching**

1.137 Those who had not switched their landline provider in the past 12 months were asked why, and this is shown in Figure 1.62. The primary reason given was satisfaction / trust in provider across all three groups, but this was comparatively higher among voice-only customers at 76%.

**Figure 1.65: Reasons for not being interested in switching**



Source: 2017 NMR Residential survey

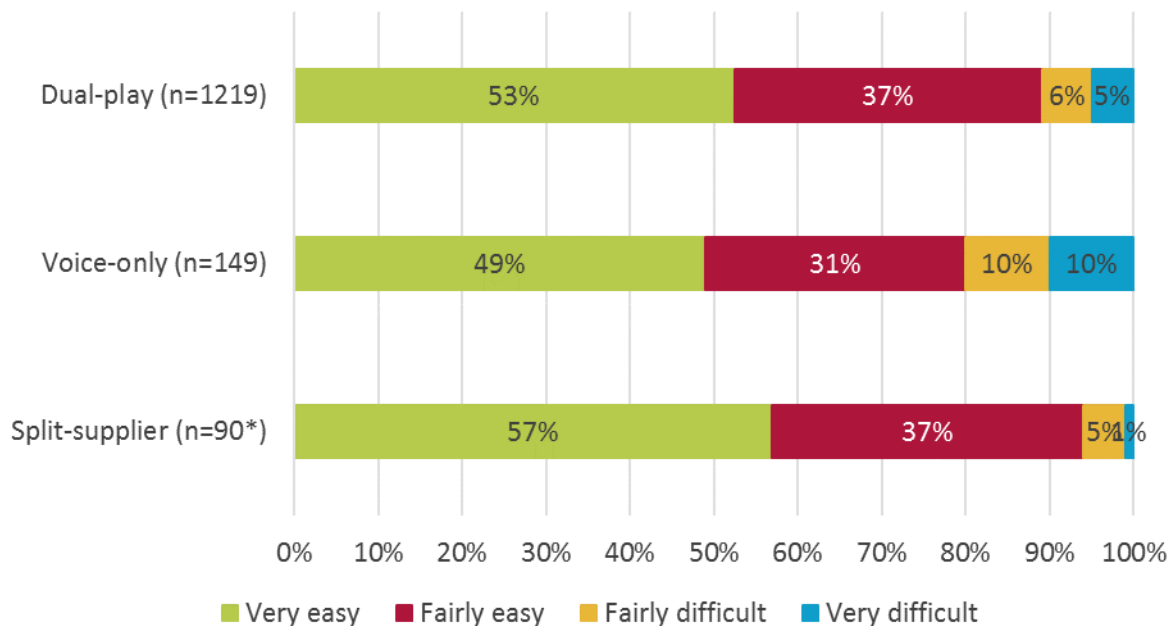
**Perceptions of switching**

1.138 As shown in Figure 1.66 a comparatively higher proportion (20%) of voice-only customers, but a lower proportion of split-supplier customers, said they perceive the switching process as either fairly or very difficult.



Evidence supporting the review of the market for standalone landline telephone services

Figure 1.66: Ease of switching providers

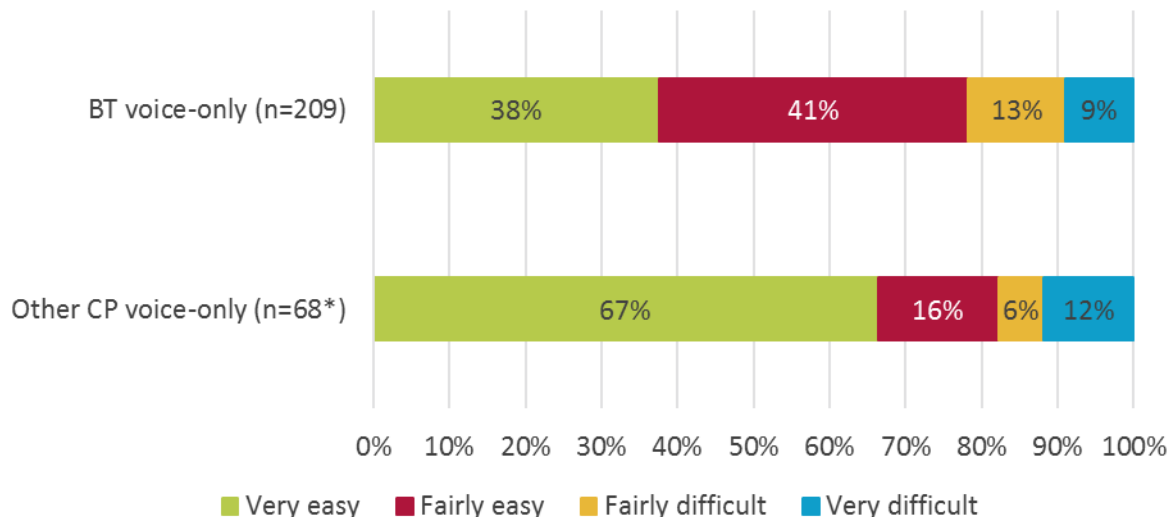


Source: Ofcom switching tracker, July to August 2016

Notes: \*Caution: base under 100.

1.139 Switching is perceived to be easier amongst voice-only of other providers compared to those that use BT.

Figure 1.67: Ease of switching providers: BT versus other communications providers



Source: Ofcom switching tracker, July to August 2016

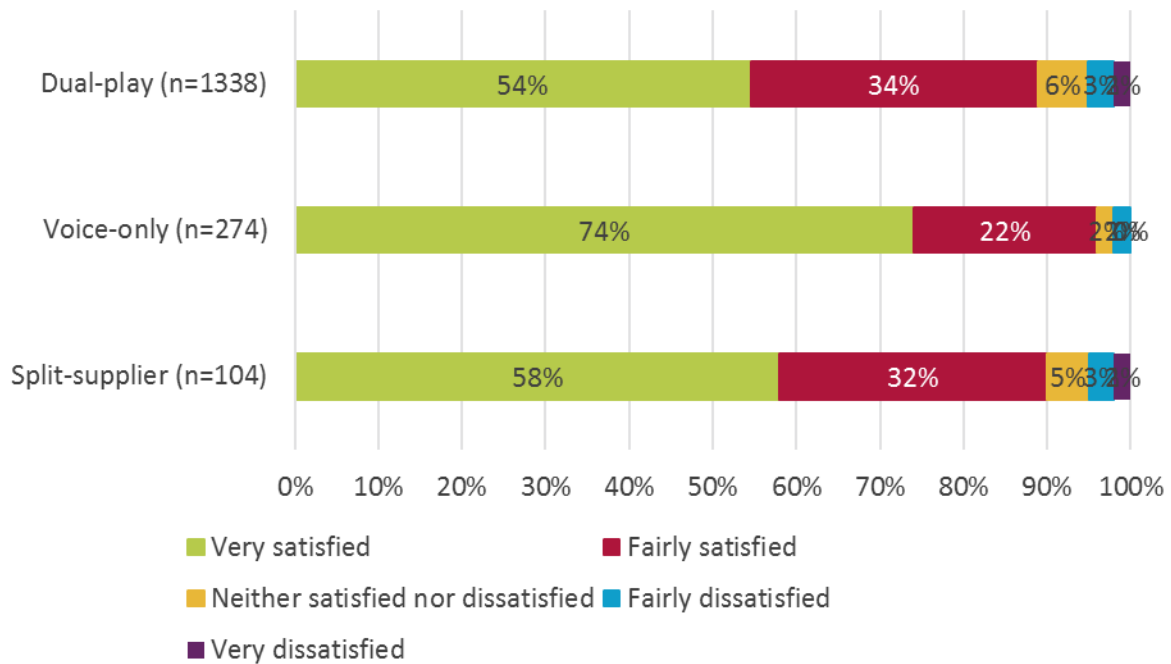
Notes: \*Caution: base under 100.

## Evidence supporting the review of the market for standalone landline telephone services

## Satisfaction

1.140 Close to three quarters of voice-only customers cited that they were very satisfied with the service provided by their landline provider, which was higher than both split-supplier (58%) and dual-play (54%) customers.

Figure 1.68: Satisfaction with overall service provided by landline provider

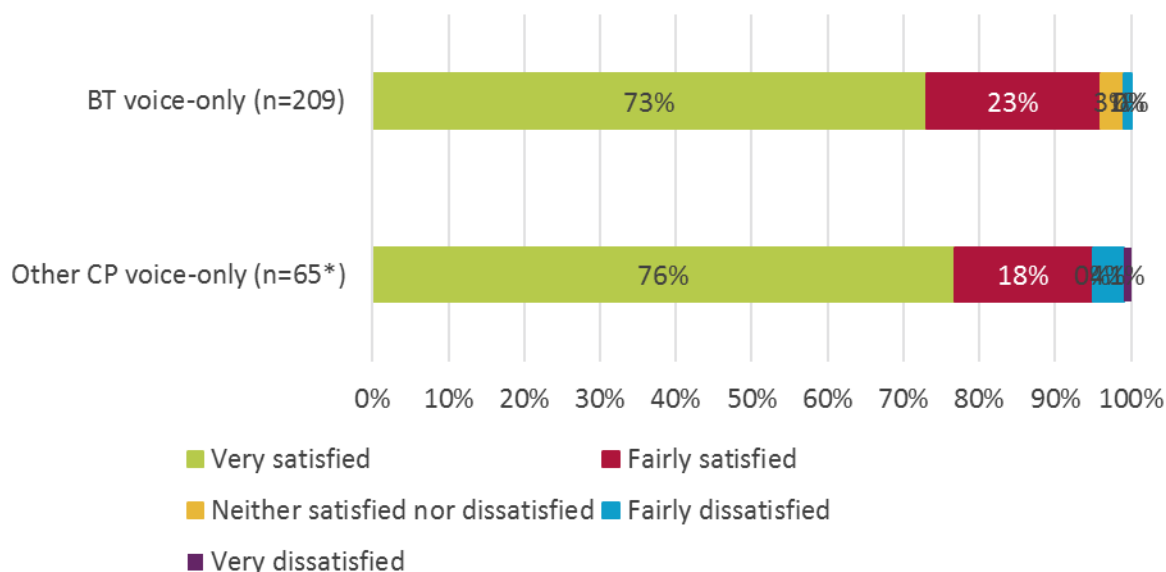


Source: Ofcom switching tracker, July to August 2016

1.141 Figure 1.69 indicates that there is no material difference in terms of satisfaction with service between BT and other CP voice-only customers.

Evidence supporting the review of the market for standalone landline telephone services

**Figure 1.69: Satisfaction with overall service provided by landline provider: BT versus other communications providers**

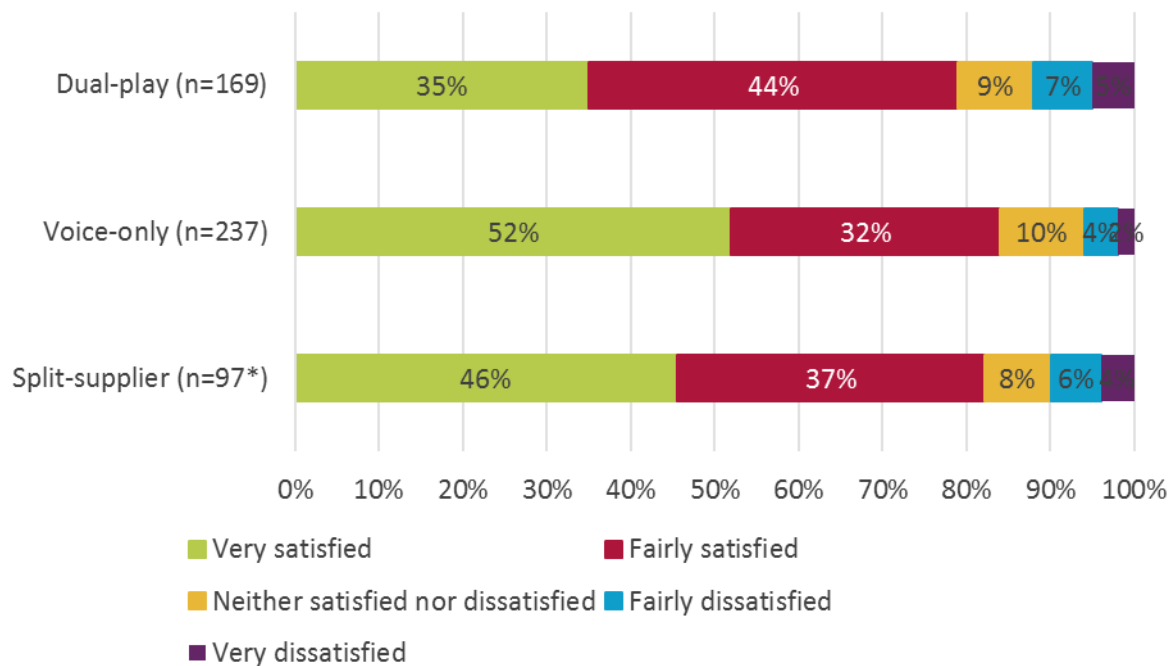


Source: Ofcom switching tracker, July to August 2016

Notes: \*Caution: base under 100.

1.142 Figure 1.70 shows approximately more voice-only and split-supplier customers were satisfied compared to dual-play.

**Figure 1.70: Satisfaction with value for money provided by landline provider**



Source: Ofcom switching tracker, July to August 2016

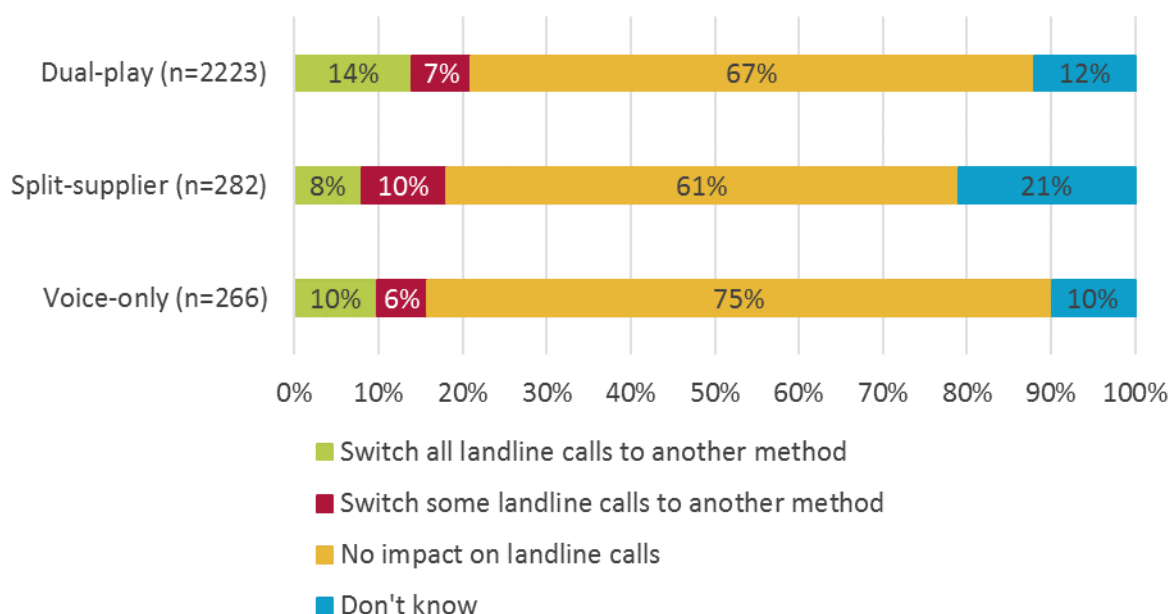
Notes: \*Caution: base under 100.

## Evidence supporting the review of the market for standalone landline telephone services

## SSNIP responses

- 1.143 This section presents how customers reported they would respond after a hypothetical small but significant, non-transitory increase in price (SSNIP) of both landline calls, and total landline bills.
- 1.144 Here, our SSNIP is defined as a 10% increase. The questions specified that this increase in price was across all providers (so no benefit would be gained from switching), and that the cost of other forms of communication would remain unchanged.
- 1.145 As shown in Figure 1.71 the majority of all three groups of customers said a 10% price increase would have no impact on their landline calls. However, the figure was comparatively higher among voice-only customers at 75%.

Figure 1.71: Response to 10% SSNIP on landline calls

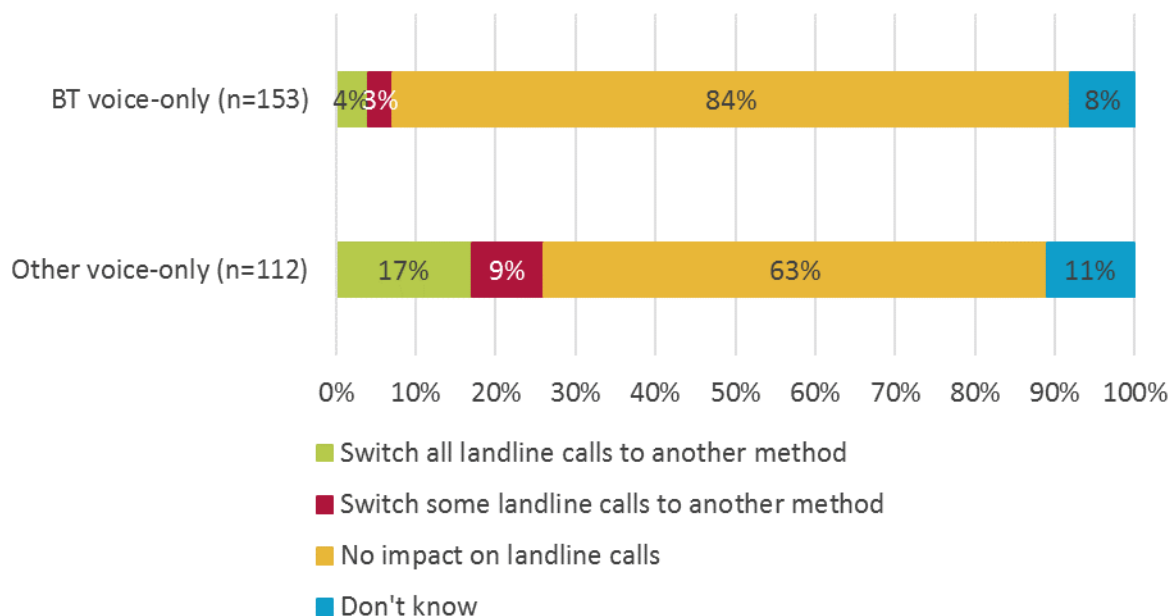


Source: 2017 NMR Residential survey

- 1.146 BT voice-only customers (84%) were more likely than other CP voice-only customers (63%) to say that a 10% SSNIP on landline calls would have no impact on how they make landline calls.

## Evidence supporting the review of the market for standalone landline telephone services

Figure 1.72: Response to 10% SSNIP on landline calls: BT versus Other communications providers

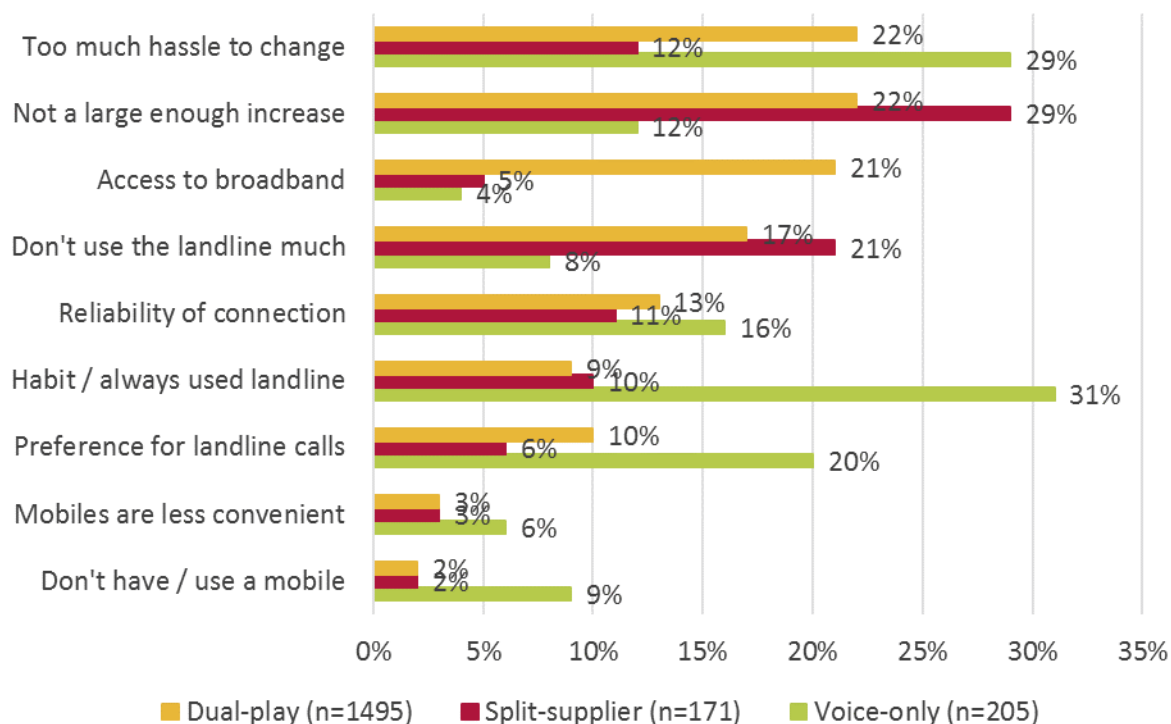


Source: 2017 NMR residential survey.

- 1.147 Figure 1.73, presents the reasons customers gave for why they would not take any action in response to a 10% SSNIP on landline calls.
- 1.148 Dual-play and split-supplier customers were more likely to cite that they would not respond to such a price increase as they did not use the landline much (17% and 21% respectively), compared to only 8% of voice-only customers. While the question asked specifically about the response to using landline calls rather than physical access to the landline, 21% of dual-play customers stated that access to broadband was a reason for unwillingness to give up landline calls, in comparison to only 5% of split-supplier customers.<sup>108</sup>

<sup>108</sup> We note that 4% of voice-only customers reported access to broadband as a reason for being unwilling to give up broadband. By definition, these customers do not have a broadband service. It is possible that some of these customers value the option of taking broadband, but this proportion seems unreasonably high.

## Evidence supporting the review of the market for standalone landline telephone services

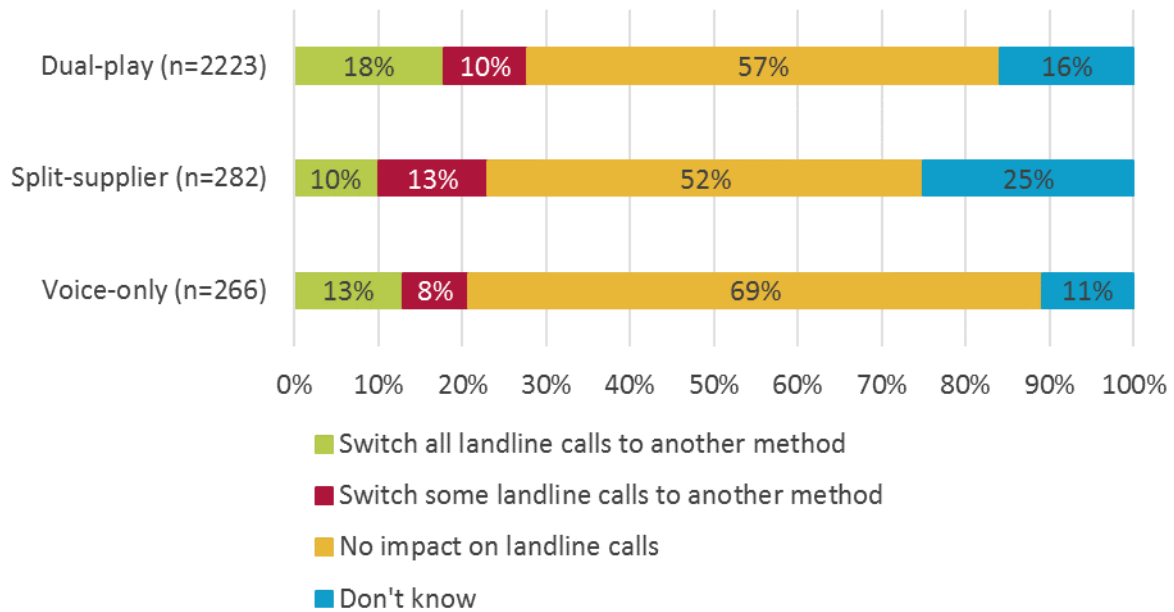
Figure 1.73: Reasons for no response to 10% SSNIP on landline calls<sup>109</sup>

Source: 2017 NMR Residential survey

- 1.149 Respondents were also asked how they would respond to a 10% SSNIP of their total landline bill (rather than just calls). Results were similar, but with higher proportions stating it would have an effect on their landline behaviour.

<sup>109</sup> We note that 4% of voice-only customers reported access to broadband as a reason for being unwilling to give up broadband. By definition, these customers do not have a broadband service. It is possible that some of these customers value the option of taking broadband, but this proportion seems unreasonably high.

## Evidence supporting the review of the market for standalone landline telephone services

Figure 1.74: Response to 10% SSNIP on total landline bill<sup>110</sup>

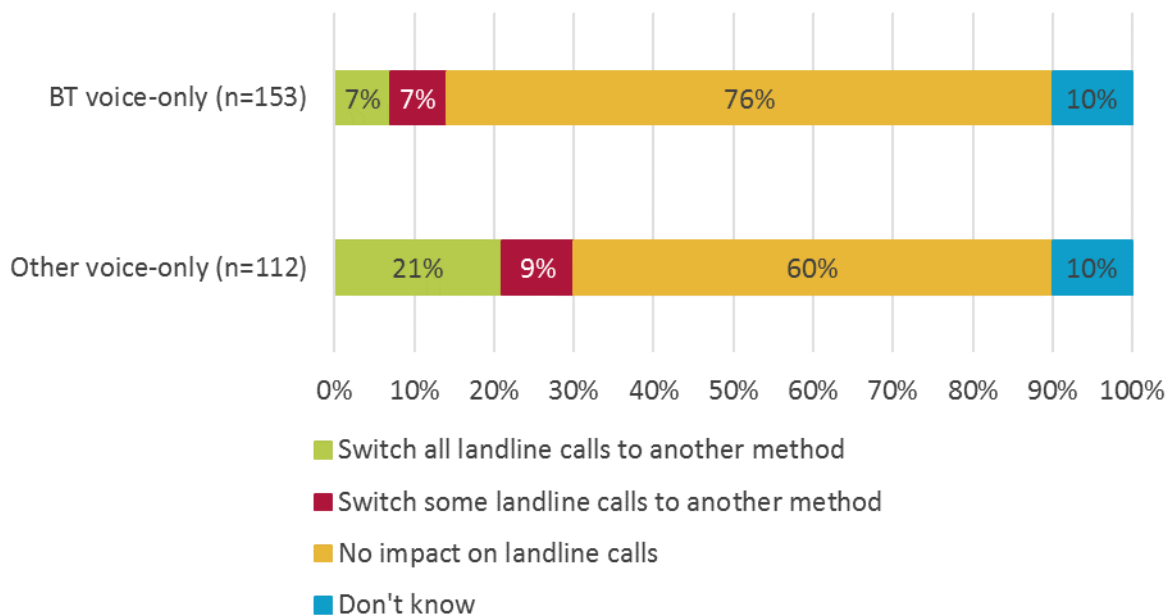
Source: 2017 NMR Residential survey

1.150 Again, the differences between BT and other CP customers for a 10% SSNIP on the total landline bill was similar to that for a 10% SSNIP on landline calls, although customers were more willing to change the way they make calls in the home as a response to this higher price increase. BT voice-only customers (76%) were more likely than other CP voice-only customers (60%) to respond that a 10% SSNIP on the total landline bill would have no impact on how they make landline calls.

<sup>110</sup> This presents the main reasons reported by customers. We have omitted responses for which less than 5% of each customer group reported.

Evidence supporting the review of the market for standalone landline telephone services

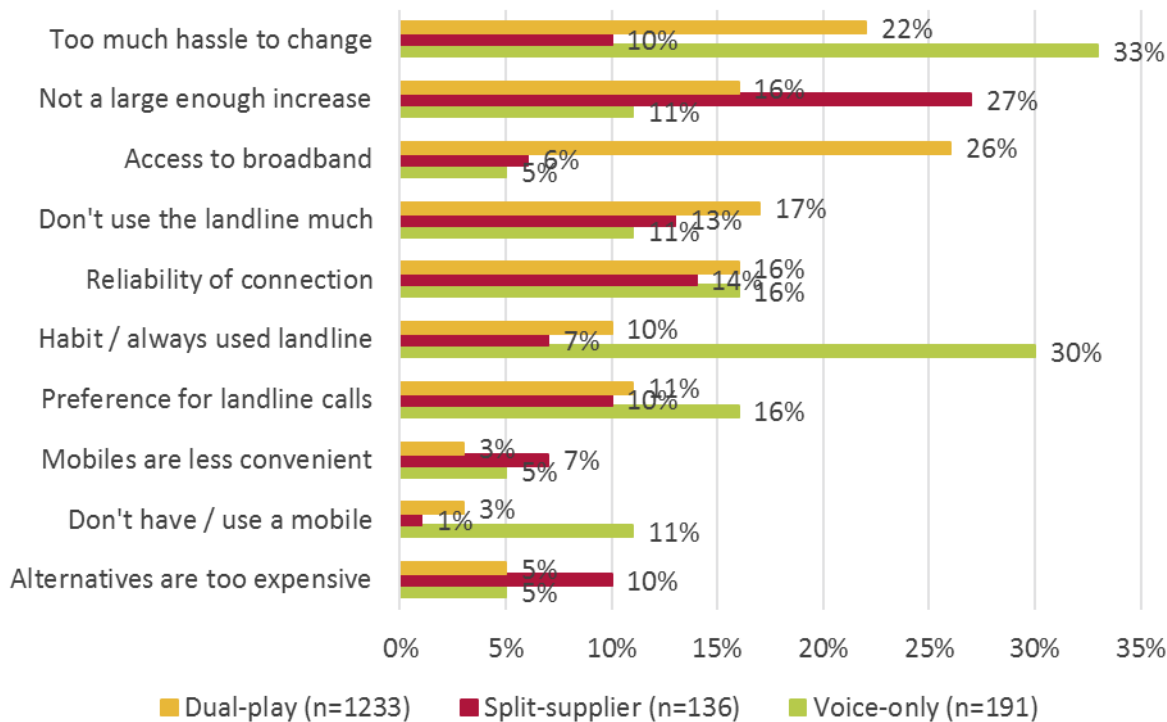
**Figure 1.75: Response to 10% SSNIP on total landline bill: BT versus Other communications providers**



Source: 2017 NMR residential survey.

1.151 Figure 1.76, below, presents the reasons customer reported they would not respond to a 10% SSNIP on the total landline bill. The general trends are very similar to the results of the responses to the 10% SSNIP on landline calls.

**Figure 1.76: Reasons for no response to 10% SSNIP on total landline bills**



Source: 2017 NMR Residential survey



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**ANNEX 5**

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# The review of the market for standalone landline telephone services

Provisional conclusions

Consultation

Publication date: 28 February 2017

Closing Date for Responses: 9 May 2017

## About this document

We are consulting on our review of the retail market for standalone landline telephone services, that is the sale of telephone services to those people who buy such services in a standalone contract and not as part of a bundle with other services such as broadband or pay-TV. This affects around 2.9 million households in the UK.

The review was prompted by concerns over rapidly rising prices for these services, despite falling wholesale costs suggesting that these customers have not benefited from competition in the same way as those buying bundles.

We consider whether we can define a distinct market for such services and whether in this market there is one or more companies with significant market power, i.e. that they are able to act without sufficient constraint from competitors.

We provisionally conclude that there is a distinct market, with BT holding significant market power and we set our proposal to address this. We will take all responses to this consultation into account before reaching our final conclusions which we plan to publish in a statement at the turn of the year.

# Contents

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3	Retail market definition	14
4	Retail market power assessment: Access	41
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8	Options for a price control remedy	92
9	Our proposals	107

## Section 1

# Executive summary

## Strategic context

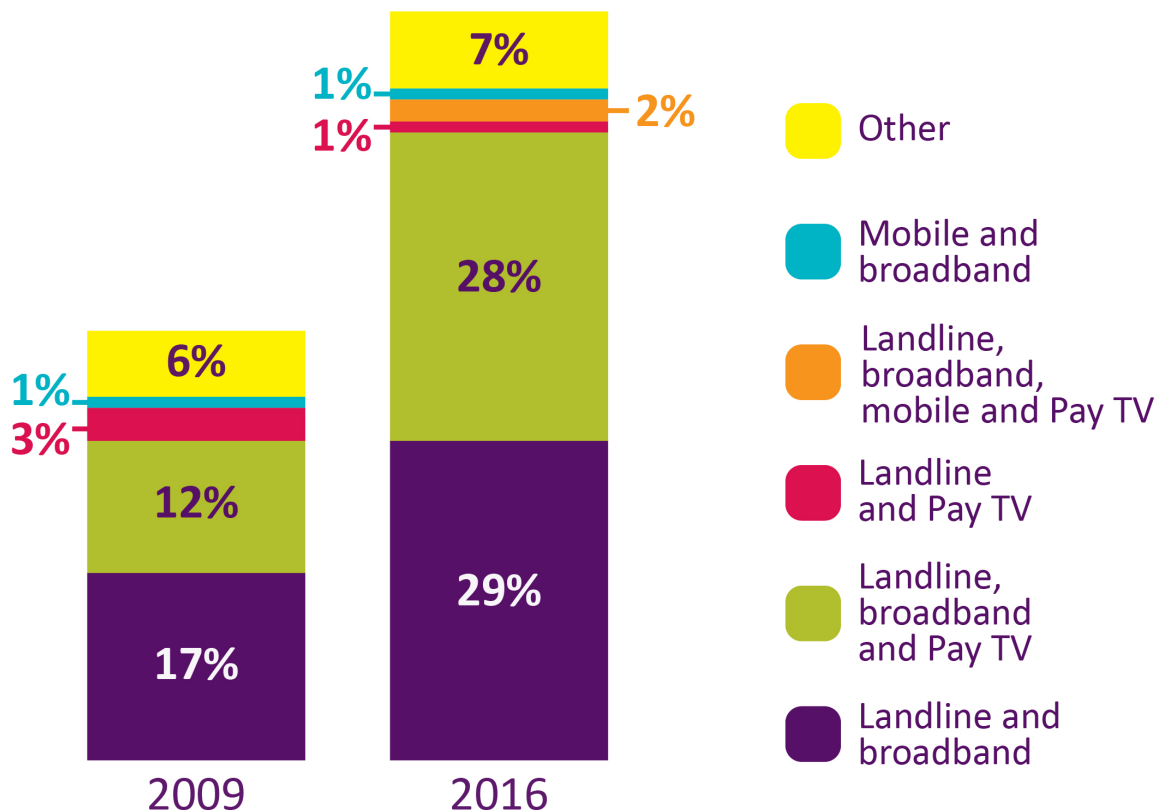
- 1.1 Over the past decade, the landscape for fixed line telecommunications in the United Kingdom has been transformed. Competition has brought new services, increased choice and delivered real benefits to consumers.
- 1.2 Fifty-nine per cent of homes now buy a bundle including a landline telephone service and a broadband service. The majority of these customers bundle their landline and broadband services (29% of homes); followed by customers who bundle their landline, broadband and Pay TV services (28% of homes); and customers who bundle their landline, broadband, mobile and pay-TV services (2% of homes).
- 1.3 People who buy bundled services are getting more for their money than before. Average broadband speeds have increased over time from 8 Mbit/s in 2011 to 29 Mbit/s<sup>1</sup> in 2015. Similarly, average broadband data use has increased from 8GB per connection in 2008 to 97GB in 2015. Over the same period, bundles have been expanded to include on-demand television and related content services, often at little or no extra cost.
- 1.4 Consumers have recognised these benefits, and take-up of bundles including three or more services has increased significantly over the period (see Figure 1.1).

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<sup>1</sup> Average speed November 2015 – see Ofcom, *Communications Market Report 2016*, 4 August 2016, <https://www.ofcom.org.uk/research-and-data/cmr/cmr16>.

Figure 1.1: Take up of bundled services<sup>2</sup>

## Consumer bundling, 2009 vs 2016



Source: Ofcom, Technology Tracker. Data from January-February fieldwork, both 2009 and 2016.

- 1.5 However, customers that do not take bundled services have not benefited from competition in the same way. We are particularly concerned about people who only buy a landline from a provider – either because they do not want broadband or pay-TV, or because they take these services separately, usually from different companies.
- 1.6 Our concerns are that relative to those who purchase services in a bundle, these consumers have less choice of suppliers, are not benefiting from strong price competition or promotional offers and their loyalty to their suppliers is leading to ever higher prices. Further, while price increases up to 2013 might have been explained by the rebalancing of revenue from calls and the line rental, since then we have observed a more rapid inflation and it is now clear we need to act.

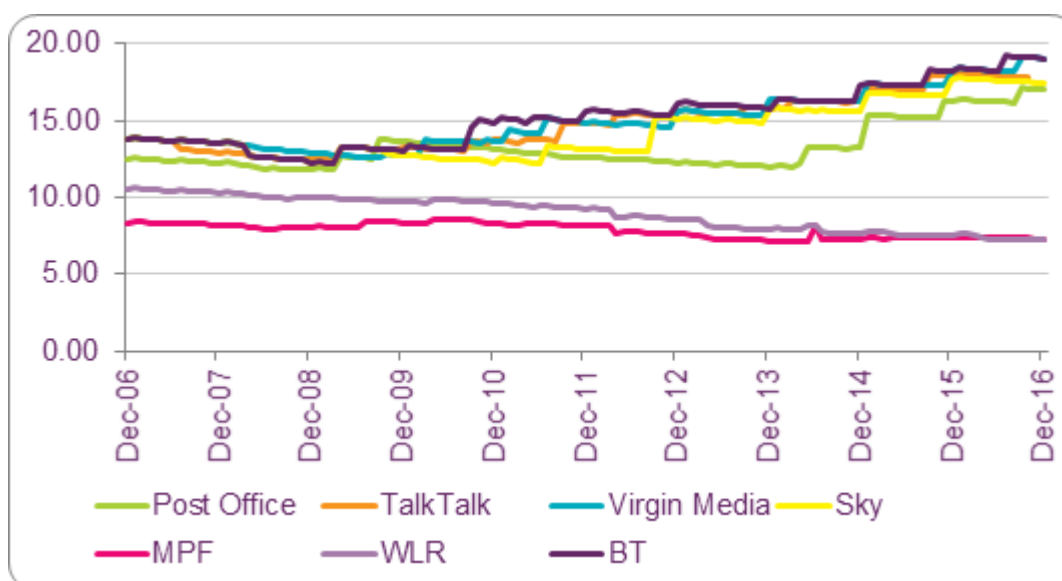
<sup>2</sup> Data relates to the proportion of customers self-reporting a bundle of services, and understates the proportion purchasing multiple services from a single provider. We use this to allow for comparability with 2009 data. Revised analysis for 2016 based on the main provider used for each service is reported in Figure A8.1. This analysis also defines those who pay line rental in addition to their broadband service, as a bundle.

- 1.7 We have found that these customers – often elderly people who have remained with the same landline provider for many decades – are getting increasingly poor value for money. They are particularly affected by price increases, and, we consider, are in need of additional protection in a market that is not serving them well enough.
- 1.8 To address this situation, we are now proposing to cut the price of BT’s standard line rental by at least £5 per month for customers with standalone landline contracts. Thereafter BT would only be allowed to increase its average prices for line rental and calls in line with inflation.<sup>3</sup>

## Retail and wholesale landline prices

- 1.9 As we set out in our Digital Communications Review (“DCR”)<sup>4</sup>, and as shown in Figure 1.2 below, line rental prices have increased significantly. From December 2009 to December 2016, line rental prices have risen by between 25% and 49% in real terms. At the same time, the wholesale costs for providing landline services have fallen by up to 26% in real terms. Wholesale costs are represented by the WLR and MPF lines in Figure 1.2. These two wholesale products are used by providers to offer retail line rental services to consumers.
- 1.10 This fall in the wholesale costs has allowed more competitive pricing in the bundled market but for landline only has simply meant that the profit in the provision of this service has grown significantly.

**Figure 1.2: Wholesale and retail line rental price movements (£/month at December 2016 prices)**



Source: PurePricing broadband updates

Notes: Adjusted for CPI; excludes line rental saver pre-payment tariffs

<sup>3</sup> Any increase over the rate of inflation in either line rental, calls or ancillary services would need to be offset by price decreases in some of the other services.

<sup>4</sup> [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0016/50416/dcr-statement.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0016/50416/dcr-statement.pdf)

- 1.11 This trend is observable across all major providers of landline services – not just BT. We are therefore concerned that standalone landline telephone consumers are increasingly worse off compared to consumers of bundled services.
- 1.12 There are currently about 2.9 million standalone landline consumers which account for 11% of total residential landline customers.<sup>5</sup> They fall into two categories:
- About 1.7 million consumers buy landline services but do not purchase fixed broadband. We refer to this group as “voice-only” consumers.
  - Approximately 1.2 million consumers buy both landline and broadband services but on a standalone basis outside of a bundle. They have faced the same line rental price increases as voice-only consumers and have not benefited from competition in bundles. We refer to this second group as “split purchasers”.
- 1.13 Standalone landline customers generally do not engage with the market: 70% of standalone landline customers have never switched provider or considered doing so. They tend to be older and less likely to shop around for a better deal. Approximately 43% of standalone landline customers are at least 75 years old, and 35% live in DE socio-economic group households (for comparison, 4% of dual-play customers are 75 or over, and 20% are in DE group households).<sup>6</sup>

## Our market assessment

- 1.14 We have carried out a review of the retail market for standalone voice services to determine the problems and what can be done to address any consumer detriment which has arisen. A market review involves us carrying out an assessment of competition in specific markets. Where we identify competition issues we can impose specific regulatory obligations on providers that we find to have significant market power (SMP). This consultation document sets out our provisional conclusions of our review of retail standalone landline telephone service markets.
- 1.15 On the basis of our analysis, we have provisionally concluded that there is a separate market in the UK<sup>7</sup> for the provision of standalone landline telephone services (or as we term them in the review, standalone fixed voice services<sup>8</sup>). This market does not include landline telephone services when they are provided as part of a bundle (landline telephone and broadband or landline telephone, broadband and pay-TV). The market also does not include mobile services as the evidence suggests that these remain at most a complementary service for most consumers.<sup>9</sup> While we acknowledge that the market may be transformed in the future as the current copper

<sup>5</sup> The number of standalone landline customers is declining at a rate of about 15-20% per year.

<sup>6</sup> Ofcom, s135 requests. Additionally, Ofcom’s Consumer Experience 2015 report suggested voice-only customers (i.e. standalone landline customers who do not buy fixed broadband) seem to be older on average than split purchase customers (i.e. standalone landline customers who buy fixed broadband outside a bundle). Almost 60% of voice-only consumers are over-75, and nearly half (47%) live in DE socio-economic group households.

<sup>7</sup> Specifically, in the UK excluding the Hull Area, as the market conditions there are different since there is only one major provider in Hull – KCOM.

<sup>8</sup> We have actually defined two standalone fixed voice service markets – the market for the purchase of access, i.e. the line rental, and the market for the purchase of calls.

<sup>9</sup> We note that many customers of standalone fixed voice services also have mobile phones, though a substantial number (around 30%) do not.



network moves to fibre based services, any transformation will be outside the period of our review (3 years).

- 1.16 We have also provisionally concluded that BT has significant market power (i.e. has a dominant position) in the market for standalone landline telephone services. This allows it to act in setting the terms and conditions of sales in this market without facing significant competitive constraint from other providers. This is particularly true when it comes to setting prices.
- 1.17 BT benefits from a very high market share; over 70%, in a market where many customers are not actively engaged. This in turn has allowed BT to act as a price leader, steadily increasing the price of standalone landline services. Further, given the difficulty in winning new customers from BT, the range of choice from competing providers has declined as prices have increased.
- 1.18 As illustrated in Figure 1.2 above, BT has been able to raise prices to its standalone landline telephone customers despite falling costs.
- 1.19 A key reason for the decline in costs has been reductions in regulated charges for wholesale inputs. However, while wholesale regulation has supported competition in bundles, as we have discussed, it has clearly not been able to sufficiently protect these standalone customers.
- 1.20 Consequently, we consider we need to act directly in the retail market through regulation of BT's retail landline services.

#### Retail price control

- 1.21 We are proposing to impose a price control on BT covering both line rental and calls as well as ancillary services for standalone landline telephone services.
- 1.22 This control – a price cut on the standard line rental of between £5-7 per month – will immediately reduce the gap between wholesale costs and retail prices we have seen emerge over the last few years. Thereafter BT will only be allowed to increase its charges for line rental and calls in line with inflation.<sup>10</sup>
- 1.23 The price cut will apply to all BT customers using standalone landline telephone contracts (whether or not they buy fixed broadband from BT or other telephone companies outside of a bundle). It does not apply to landline services sold by BT as part of a bundle of services, which include broadband or other services as we consider competition in this market is delivering good outcomes for consumers.

#### Promoting competition

- 1.24 We believe that competition has the potential to deliver benefits for consumers in terms of price and choice. In order to stimulate competition, consumers must be sufficiently engaged to make well-informed decisions about switching to get a better deal. For this to happen, we believe that consumers need to have access to helpful, easy to understand information so that they can make more informed choices.

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<sup>10</sup> We discuss the options for the design of the price control in more detail at Section 8 of this document.

- 1.25 Therefore, we propose to require BT to work with us to trial – and, if appropriate, ultimately deliver – consumer information which will encourage its standalone landline customers to look for better value deals. There are significant challenges in effectively communicating with consumers who are not actively engaged in the market. Experience in other sectors, such as energy and banking, has shown that the degree to which the provision of consumer information affects consumer behaviour depends on details of exactly how it is presented and by whom. We therefore propose to trial various ways of providing consumer information which will help customers understand what they are buying and what alternatives they have to get better value for money.
- 1.26 Our aim in imposing these measures is to allow other providers to compete more vigorously in this market and to win customers. If the engagement remedies we are proposing are effective, we would expect consumers to benefit in terms of price and choice.

### Consultation and next steps

- 1.27 We invite comments on the proposals in this document. The consultation runs for 10 weeks and the deadline for responses is **9 May 2017**. Annex 1 provides further details of how to respond.
- 1.28 We are also considering whether there is a need for additional regulatory accounting obligations. If we decide this is necessary, we will consult on these separately.
- 1.29 We aim to publish our conclusions at the turn of the year.

## Section 2

# Introduction and background

2.1 In this section we introduce the Review of Standalone Landline Telephone Services 2017. We discuss briefly our concerns in retail fixed narrowband markets, the regulatory background of the fixed narrowband market in the UK, the scope of this review, the regulatory framework, including the process of market definition and assessing market power, and the impact assessments carried out in the context of this Review.

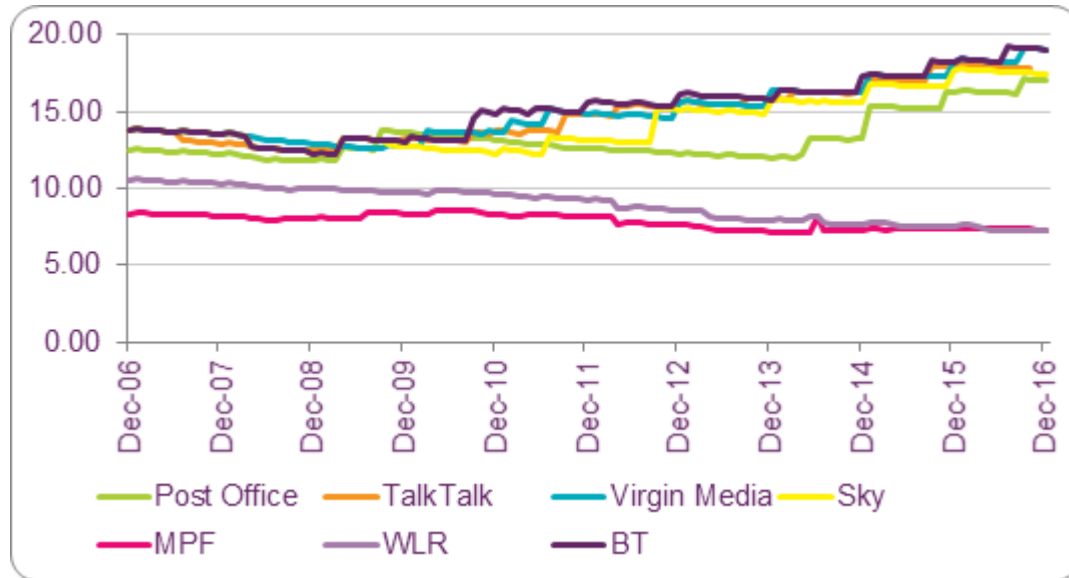
## Our concerns leading to this review

- 2.2 Since 2009, when we removed all regulation on BT in the retail voice telephony markets, many consumers have moved towards buying services in bundles, and this is where we have seen the focus of competition. In 2016, 68% of households reported buying at least two of their communication services in a bundle, with dual-play packages of landline and broadband and triple-play packages of landline, broadband and pay-TV being the most popular.<sup>11</sup> This percentage keeps rising.
- 2.3 Consumers purchasing bundled products have benefitted from competition in terms of prices and choice of products available. Whilst, until October 2016, consumers purchasing bundled products paid the same line rental charges as all other customers, the prices of the bundles they purchase did not increase in the same way. Indeed, in October 2016, the Advertising Standards Authority issued a ruling requiring communications providers (CPs) to no longer separate out line rental for bundles.<sup>12</sup> Broadband suppliers' price claims must therefore now show all-inclusive, up-front and monthly costs. Consumers purchasing bundled products including voice services therefore no longer pay a separate line rental charge.
- 2.4 We have identified concerns that competition is not benefiting standalone voice customers (i.e. those that do not purchase bundled products) to the same extent. There are currently 2.9 million households which take voice services outside a bundle, representing 11% of all residential landline users (i.e. including those that purchase landline services in a bundle). Whilst the number of such customers is declining over time, it is nevertheless likely to remain significant for the foreseeable future.
- 2.5 As Figure 2.1 shows, these customers have been progressively exposed to increasing line rental prices since 2010. This has been occurring despite wholesale charges for products used to provide line rental falling by up to 26% in real terms. Wholesale costs are represented by the WLR and MPF lines in Figure 2.1. These two wholesale products are used by providers to offer retail line rental services to consumers.

<sup>11</sup> Ofcom, *The Communications Market Report 2016*, 4 August 2016, <https://www.ofcom.org.uk/research-and-data/cm/cmr16>

<sup>12</sup> <https://www.asa.org.uk/News-resources/Media-Centre/2016/Changes-to-broadband-price-claims-in-ads-comes-into-force-today.aspx#.WK69c8FviCs>

**Figure 2.1: Wholesale and retail line rental price movements (£/month in December 2016 prices)**



Source: Ofcom/Pure Pricing UK Broadband Updates.

Notes: Adjusted for CPI; excludes line rental saver pre-payment tariffs

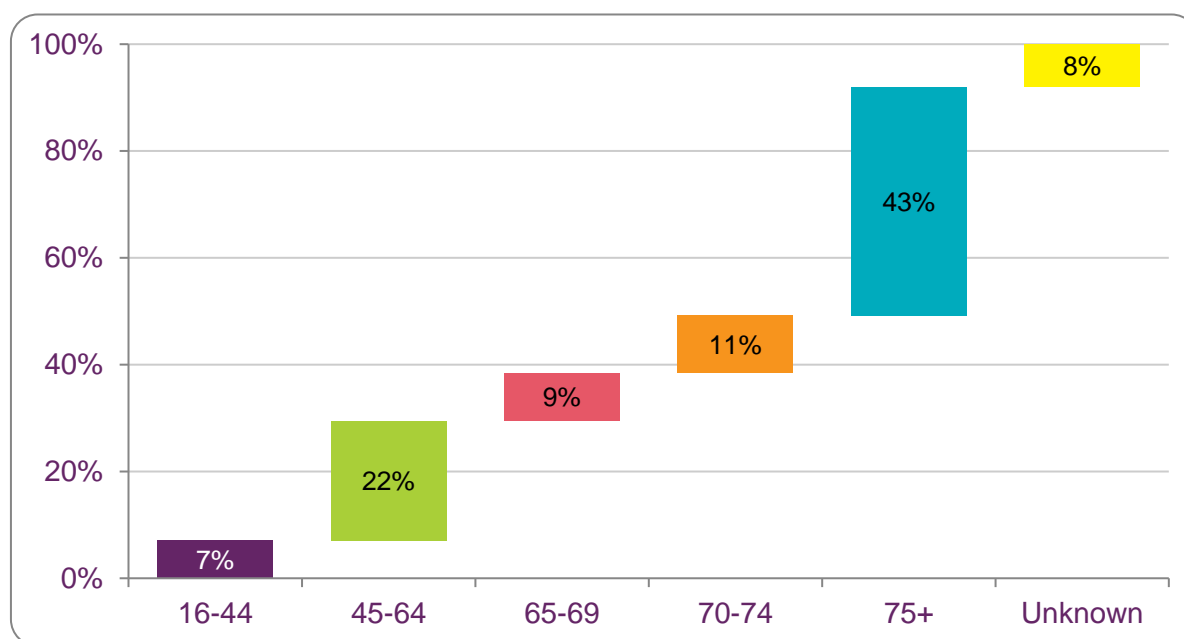
- 2.6 While some of the price increases may be due to rebalancing prices as fixed voice call revenue falls, declining wholesale costs suggest that CPs serving this market have been increasing their profitability.
- 2.7 We are particularly concerned that this trend affects a significant number of consumers who are elderly. As Figure 2.2 below shows, over half of these consumers are over 70.<sup>13</sup> Moreover, this group of consumers is generally more disengaged; Ofcom research has shown that 71% of consumers who use standalone landline services have never switched providers or considered doing so.<sup>14</sup> We are concerned that these customers are receiving poor value for money given the rising line rental charges which they face.

<sup>13</sup> Ofcom, *The Consumer Experience 2015*, 10 February 2016

[https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0012/51105/cer\\_2015\\_final.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0012/51105/cer_2015_final.pdf)

<sup>14</sup> Ofcom, *The Consumer Experience, 2015: Research Annex*, 10 February 2016

[https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0023/38543/annex.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0023/38543/annex.pdf)

**Figure 2.2: Residential standalone fixed voice consumers by age group**

Source: s.135 responses.

## Background to this consultation

### Retail regulation

2.8 Up until 2006, BT was subject to retail price regulation. In 2006, Ofcom<sup>15</sup> decided to allow retail price controls to lapse.<sup>16</sup> In doing so, we recognised, however, that certain groups of vulnerable consumers might require more protection than the average consumer who could switch easily.<sup>17</sup> In particular, we acknowledged that there may be some consumers for whom competition was weaker, leaving them vulnerable to price rises.

2.9 In 2009, we concluded that relevant retail markets were effectively competitive and BT no longer held a position of SMP in those markets. In light of that conclusion, we removed the remaining regulation which applied. We indicated that we would continue to monitor consumers' experience of these services and would intervene, if appropriate, in the future.

### Wholesale regulation

2.10 One of the ways in which an operator can offer services which compete with BT's retail fixed line voice services is through the purchase of wholesale line rental and wholesale call origination. Those services allow an operator to offer retail voice services over BT's infrastructure.

<sup>15</sup> Ofcom replaced Oftel as the regulator with responsibility for electronic communications markets from 29 December 2003.

<sup>16</sup> Ofcom, *Retail Price Controls*, Statement of 19 July 2006 ("2006 Retail Price Control Statement"), [https://www.ofcom.org.uk/data/assets/pdf\\_file/0012/42114/rpcstatement.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0012/42114/rpcstatement.pdf)

<sup>17</sup> 2006 Retail Price Control Statement, paragraph 1.13.

- 2.11 Ofcom imposes regulation requiring BT to offer such wholesale products to its competitors through market reviews to allow them to compete effectively at the retail level. BT has been required to provide wholesale line rental and wholesale call origination over a number of market reviews and that remains the case.
- 2.12 In December 2016, we published a consultation document setting out the initial findings of our current review of the wholesale narrowband markets (the 2016 NMR Consultation).<sup>18</sup> The closing date for responses for the wholesale narrowband market review is 29 March 2017. The markets relevant to this review are:
- Wholesale fixed analogue exchange lines (WFAEL): standard fixed lines used by residential consumers; and
  - Wholesale call origination (WCO): a complementary service to the provision on narrowband access lines, which enables consumers to make calls over those lines.
- 2.13 In the 2016 NMR Consultation document, we proposed that BT continues to have SMP in the WFAEL and WCO markets in the UK excluding the Hull Area. However, we have proposed not to impose charge controls, in favour of a fair and reasonable charges obligation, in recognition of the growing alternatives to traditional fixed voice services.

## Scope of the review

- 2.14 The concerns identified above have led us to conduct this review to determine if there are features of the retail market which mean that competition is not working well for consumers who take standalone fixed voice services and do not benefit from competition in bundled services. The starting point for this market review is therefore to consider the state of competition for residential consumers who take landline services but do not purchase them in a bundle (Standalone Fixed Voice (SFV) customers).
- 2.15 Our aim is to determine whether there is effective competition in the relevant markets, and if not, how best to regulate the behaviour of any companies that we find to have SMP.

## Hull area

- 2.16 We have always recognised that the retail markets in the Hull Area were distinct from those in the rest of the UK. The material differences in the sizes of these markets, the prospect of competitive entry and the relative cost of regulation on the incumbents (and the potential those costs are passed onto their customers) have led to differences in the nature of regulation. We have not extended this review to include an assessment of competition in the Hull area (and we explain in Section 3 why the relevant geographic market for the rest of the UK excludes Hull).
- 2.17 We note that KCOM has consistently set matching or lower prices than BT for fixed voice line rental and calls packages. We might therefore expect the impact of any regulatory intervention in the rest of the UK to flow through to retail conditions in Hull to the benefit of its consumers. If, subsequent to this review, we had evidence of

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<sup>18</sup> Ofcom, *Narrowband market review* (“2016 NMR Consultation”), 1 December 2016, [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0016/95011/Narrowband-Market-Review.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0016/95011/Narrowband-Market-Review.pdf)

significant detriment to consumers in the Hull area, we would consider what further action is required, including the possibility of a separate review for the Hull area.

## Regulatory framework

- 2.18 Sections 78-86 of the Communications Act 2003 (“the Act”) set out the procedure to be followed by Ofcom when undertaking market reviews. Section 91 of the Act contains additional provisions which apply to the conduct of market review in retail markets and is therefore relevant here.
- 2.19 We set out the applicable regulatory framework in Annex 7. In this section, we set out, in summary, what the market review process involves and the specific requirements that apply in relation to the regulation of retail markets.

## Market review process

- 2.20 The market review process is designed to assess the state of competition within a relevant market for the purposes of deciding whether or not regulation is required. Broadly, the market review process is carried out in three stages:
- we identify and define relevant markets in which regulation may be warranted;
  - we assess the state of competition in those markets to decide whether they are effectively competitive, which involves assessing whether any operator has significant market power (SMP); and
  - where we find SMP, we must impose remedies to address the competition problems identified in the relevant markets.
- 2.21 A finding of SMP is equivalent to a finding of dominance under competition law and means that an operator is able to act independently of its customers and competitors in a market. Where we identify SMP, we seek to impose appropriate remedies to address competition concerns, taking into account our duties in the Act, in particular our duty to act in the interests of consumers, where appropriate by promoting competition, and the need for regulation to be targeted only at cases in which action is needed.
- 2.22 Where we identify SMP in a retail market, the SMP Conditions which we can impose are set out in section 91. Such obligations may include requirements that the SMP operator does not charge excessive prices, inhibit market entry or restrict competition by setting predatory prices, show undue preference to specific end-users or unreasonably bundle services. We may therefore impose appropriate retail price cap measures, measures to control individual tariffs, or measures to orientate tariffs towards costs or prices on comparable markets, in order to protect end-user interests whilst promoting effective competition.

## Relevant legal tests and statutory duties

- 2.23 Any SMP condition we impose must satisfy the tests set out in section 47 of the Act, namely that the condition is:
- objectively justifiable in relation to the networks, services, facilities to which it relates;

- not such as to discriminate unduly against particular persons or against a particular description of persons;
- proportionate to what the condition or modification is intended to achieve; and
- transparent in relation to what is intended to be achieved.

2.24 In addition to the above requirements, section 91(2) requires us to only impose retail remedies where we are satisfied that the setting of conditions in wholesale markets would not address the concerns we have identified in the retail market. In Section 9 we set out how our proposed SMP Conditions satisfy the legal tests in sections 47 and 91 of the Act.

2.25 We set out in this document our analysis of competition in the relevant markets in accordance with the framework above. In doing so, we are required to have regard to a number of documents produced by the European Commission and the Body of European Regulators for Electronic Communications (BEREC), in particular the European Commission's Recommendation on Relevant Markets and SMP Guidelines.

## Impact assessment and equality impact assessment

### Impact assessment

2.26 The analysis presented in this document constitutes an impact assessment as defined in section 7 of the Act.

2.27 Impact assessments provide a valuable way of assessing different options for regulation and showing why the preferred option was chosen. They form part of good practice policy-making. This is reflected in section 7 of the Act, which sets out that we have to carry out impact assessments where our proposals would be likely to have a significant effect on businesses or the general public, or when there is a major change in Ofcom's activities. However, as a matter of policy Ofcom is committed to carrying out impact assessments in relation to the great majority of our policy decisions. For further information about our approach to impact assessments, see our guidelines *Better policy-making: Ofcom's approach to impact assessment*.<sup>19</sup>

### Equality Impact assessment ('EIA')

2.28 Annex 4 sets out our EIA for this market review. Ofcom is required by statute to assess the potential impact of all our functions, policies, projects and practices on race, disability and gender equality. EIAs also assist us in making sure that we are meeting our principle duty of furthering the interests of citizens and consumers regardless of their background or identity.

2.29 We have considered whether these proposed remedies would have an adverse impact on promoting equality. In particular, we have considered whether the remedies would have a different or adverse effect on UK consumers and citizens with respect to the following equality groups: age, disability, sex, gender reassignment, pregnancy and maternity, race, religion or belief and sexual orientation, and, in Northern Ireland, political opinion and dependants. We consider that our proposals will not have a detrimental impact on any equality group.

<sup>19</sup> [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0026/57194/better\\_policy\\_making.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0026/57194/better_policy_making.pdf)



- 2.30 Further, we do not propose to carry out separate EIAs in relation to race or gender equality or equality schemes under the Northern Ireland and Disability Equality Schemes. This is because we anticipate our proposed regulatory intervention would not have a differential impact on people of different genders or ethnicities, consumers with protected characteristics in Northern Ireland or on disabled consumers compared to consumers in general.
- 2.31 Rather, we consider that the proposals set out in this consultation would further the aim of advancing equality of opportunity between different groups in society by furthering the interest of all consumers in the retail fixed voice markets.

## Document structure

- 2.32 The structure of this document follows the structure of our analysis and is set out as follows:
- First we define the relevant retail markets and identify SMP within those markets (Sections 3, 4 and 5), and;
  - Set out a suite of potential remedies (Sections 6, 7 and 8), before;
  - Detailing our proposals (Section 9).
- 2.33 We are also publishing Annexes to this consultation document which support our main conclusions. These include the draft legal instruments which would implement our proposed remedies.

## Next steps

- 2.34 The questions we are seeking responses are set out at each of the relevant section. For ease we have listed all the consultation questions at Annex 3. Details about how to respond to the consultation are set out at Annex 1. Responses must be sent to Ofcom by 9 May 2017.

## Section 3

# Retail market definition

## Introduction and summary

- 3.1 This Section sets out our provisional market definition assessment for residential Standalone Fixed Voice (SFV) services in the UK. As explained in Section 2, SFV services are landline services that are not sold as part of a bundle with non-voice services. This includes access (i.e. line rental) and calls.
- 3.2 In the 2009 Review we defined the following relevant fixed narrowband markets in the UK (excluding the Hull Area):
- 3.2.1 Residential Fixed Narrowband Analogue Access;
  - 3.2.2 Residential Fixed Narrowband Calls;
  - 3.2.3 Business Fixed Narrowband Analogue Access;
  - 3.2.4 Business Fixed Narrowband Calls.
- 3.3 Consistent with our conclusions in the 2009 Review, we have provisionally concluded that:
- 3.3.1 A relevant market exists for the provision of SFV access in the UK, excluding the Hull Area. This includes sales to voice-only customers and split purchasers and is limited to residential services.
  - 3.3.2 A relevant market exists for the provision of SFV calls (i.e. fixed voice calls sold to SFV access customers) in the UK, excluding the Hull Area. As for access, this includes sales to voice-only customers and split purchasers and is limited to residential services. We take account of substitution to mobile calls as an out-of-market constraint at paragraphs 3.85-3.96 below.
- 3.4 After considering the two relevant markets identified against the three criteria test, we have provisionally concluded that they are both susceptible to *ex ante* regulation.
- 3.5 We present the analysis and findings underlying our proposals in the following order:
- 3.5.1 Approach to market definition;
  - 3.5.2 Retail product market definitions;
  - 3.5.3 Retail geographic market definitions;
  - 3.5.4 Provisional conclusions on market definitions;
  - 3.5.5 Application of the EC's three-criteria test to the relevant market(s).

## Approach to market definition

- 3.6 The market review procedure requires us to analyse markets in order to determine whether they are effectively competitive, and then to decide on appropriate remedies

if necessary. Before an assessment of competitive conditions is possible, it is necessary to define the relevant market.

- 3.7 The market definition exercise is not an end in itself, but a means to assessing whether there is effective competition and thus whether there is a need for *ex ante* regulation. It is in this light that we have conducted our market definitions in this review.
- 3.8 We set out our approach to market definition in Annex 7. This approach includes two principal stages. First, we identify the products that will be the starting point of our analysis (i.e. the focal product). Next we consider whether there is a case for broadening the market to include other products. In doing so, we:
- 3.8.1 Apply the “Hypothetical Monopolist Test” (HMT, also called the SSNIP test), which considers whether a hypothetical monopolist could profitably impose a small but significant non-transitory increase in price (a SSNIP) above competitive prices in the candidate market. If demand-side substitution to, or supply-side substitution from, alternative services is sufficient to render the price increase unprofitable, then the market should be widened to include these services, and the HMT should be repeated on this broader candidate market.
- 3.8.2 Consider whether other products exist which face the same competitive conditions as the focal product, and/or a common pricing constraint. If so, it will generally be appropriate to include such products within the candidate market.

## Product market definition

### Focal product

- 3.9 In defining relevant product markets, we start by considering the narrowest set of services which might fall within a relevant market and add additional products or services depending on whether competition from those products or services constrains the price of the main product or service in question.<sup>20</sup> First, we therefore determine the focal product for the analysis. The concerns which have given rise to this review concern the supply of standalone landline services.<sup>21</sup> We have therefore taken this as a starting point in our consideration of the appropriate focal products.

### Our focal products include residential services only

- 3.10 The concerns expressed in the DCR relate to the purchase of standalone landline services for residential customers. The starting point for our consideration is therefore SFV services that are available to residential customers, excluding services that are only available to businesses.
- 3.11 We note that a significant proportion of SMEs, particularly smaller businesses, purchase residential lines. Around 30% of all SMEs do not have a business-specific contract: 31% for those with 1-9 employees, 10% for those with 10-49 employees and 5% for those with 50-249 employees. In total, 9% of SMEs purchase a

<sup>20</sup> SMP Guidelines, paragraph 41.

<sup>21</sup> DCR, paragraph 7.9.

(residential) SFV service.<sup>22</sup> With 5.4 million SMEs in the UK, this would suggest around 490,000 out of 2.9 million SFV customers are SMEs – around 17%. We include these customers in our focal product.

- 3.12 In paragraphs 3.53-3.55 below we consider whether or not the relevant market should be broadened to include SFV services offered to businesses.

### Separate markets for access and calls

- 3.13 The Explanatory Note to the 2014 EC Recommendation states that at the retail level “fixed calls services ... are more often bundled with the access to the fixed network/narrowband service”.<sup>23</sup> This is consistent with evidence for the UK market.<sup>24</sup>
- 3.14 There has been a marked decline in consumers using different suppliers of calls and access lines over the last decade. Rather, access and calls are almost invariably bought in a bundle. Survey evidence suggests that:
- 3.14.1 The proportion of residential consumers purchasing residential access and calls services from separate suppliers has diminished to negligible levels. In 2015, only 1% of residential survey respondents said that they had a landline to make calls and used separate suppliers for calls and access. This is compared to 14% of respondents reporting that they used different suppliers in 2009.<sup>25</sup> However, to the extent that SMEs purchase residential SFV services, they may use separate suppliers to a greater extent. Between 18% and 25% of SMEs continue to purchase access and calls from separate CPs.<sup>26</sup>
- 3.14.2 We do not have survey evidence for customers purchasing residential SFV services only, however, our analysis shows that a significant majority purchase calls and access from the same supplier. If we assume that a) 1% of all customers who purchase residential services have separate suppliers for calls and access and b) all of these customers have SFV lines, this would account for only 9% of total SFV lines.<sup>27</sup>
- 3.15 However, while consumers typically purchase a bundle of access and calls, there is scope for differences in competitive conditions between the two, and in particular SFV calls may face stronger price constraints than SFV access.

<sup>22</sup> Based on data provided to Ofcom by Jigsaw as part of *The SME experience of communications services: research report*. Note that this statistic does not appear in the report. [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0030/96348/Ofcom-SME-consumer-experience-research-2016-Report.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0030/96348/Ofcom-SME-consumer-experience-research-2016-Report.pdf)

<sup>23</sup> EC, *Explanatory Note to the 2014 EC Recommendation*, p. 25, <https://ec.europa.eu/digital-single-market/en/news/explanatory-note-accompanying-commission-recommendation-relevant-product-and-service-markets>

<sup>24</sup> The evidence we have on the bundling of access and fixed call services is for the total market for residential fixed voice services, rather than specifically for voice-only consumers.

<sup>25</sup> Ofcom, 2016 Narrowband Market Review Consultation (“2016 NMR Consultation”), footnote 110, found at [https://www.ofcom.org.uk/data/assets/pdf\\_file/0016/95011/Narrowband-Market-Review.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0016/95011/Narrowband-Market-Review.pdf)

<sup>26</sup> 2016 NMR Consultation, paragraph 4.26, found at [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0016/95011/Narrowband-Market-Review.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0016/95011/Narrowband-Market-Review.pdf)

<sup>27</sup> 1% of all residential lines in the UK (26.4 million in Q3 2016) refers to approximately 264k lines. If we assumed all these were SFV lines, they would account for only 9% (i.e. 264k / 2.9 million) of all SFV lines.

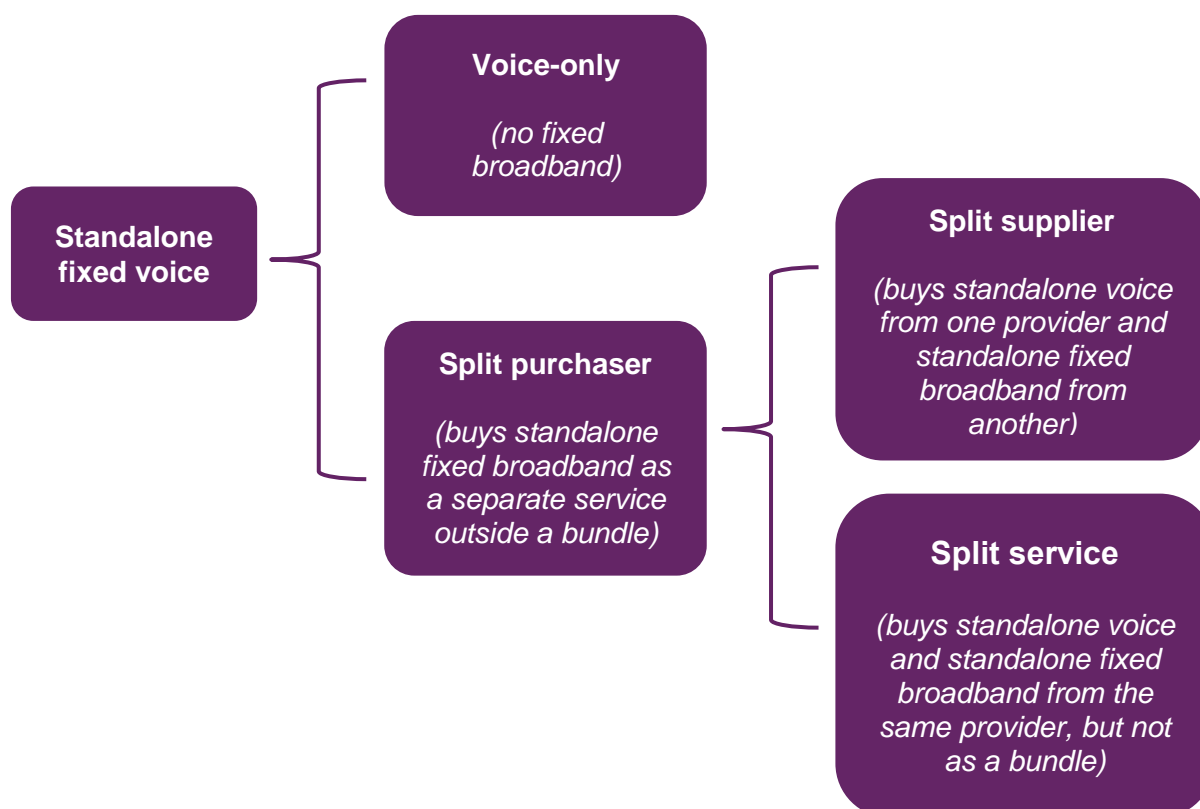
- 3.16 A customer might respond to prevailing prices for calls in a number of ways, such as making fewer out-of-bundle calls, or switching to a less generous call allowance and limiting the fixed voice calls they make in order to stay within this allowance (e.g. by avoiding making calls at times of the week when they are not “free” under the allowance). It is possible that some SFV customers could respond to the price of calls in this way while making fewer, or shorter, calls overall.
- 3.17 In addition, the potential for call-by-call substitution means the nature of substitution has the potential to differ significantly between access and calls. In particular, around 70% of SFV customers have mobile phones, and there is scope for these customers to make more calls on their mobile phone instead of their fixed line. In many cases this may be at zero marginal price because post-pay mobile packages often include an allowance of free calls.
- 3.18 In contrast, the price of the landline may not be subject to the same degree of pricing constraint, because for many consumers giving up their landline would be a bigger decision than deciding whether to make more calls on their mobile phone. For example, consumers may have concerns about missing calls from people who only have their landline number, the cost of making international calls via mobile, or the reliability of mobile phone connections in emergencies.
- 3.19 Survey evidence also suggests that, while the majority of residential landline customers said they think about the costs of line rental and calls together, a sizable minority (21% of residential survey respondents) still report considering them separately.<sup>28</sup> In addition, we noted above that some SMEs continue to purchase access and calls from separate CPs.
- 3.20 Overall, we therefore consider it is appropriate to analyse access and calls as separate markets, because there is scope for a difference in competitive conditions between them. This is consistent with the approach that we adopted in the 2009 Review.

### Our starting point does not include services offered to split purchase customers

- 3.21 SFV services are sold to three customer segments (see Figure 3.1):
- 3.21.1 Voice-only customers, who have no fixed broadband service;<sup>29</sup>
- 3.21.2 Split purchase customers, who have fixed broadband but not as part of a bundle, and who are either:
- a) Split-supplier customers, who buy fixed broadband from a different provider than their SFV service; or
  - b) Split-service customers, who buy fixed broadband from the same provider as their SFV service (but not as part of a bundle).

<sup>28</sup> 2015 Jigsaw residential survey (wave 1).

<sup>29</sup> These customers may or may not have access to mobile and/or pay TV services.

**Figure 3.1: Customer groups within SFV<sup>30,31</sup>**

3.22 As set out above, in determining the starting point of our analysis, we are seeking to determine the narrowest set of products and services which may form part of the relevant market. Whilst our concerns leading to this review are around the supply of landline services on a standalone basis, including all three customer segments, we have taken a narrower group of voice-only customers for our focal product. This is so that we explicitly address the question below of whether or not split-purchase customers should be included in the same market as voice-only customers.

### Focal product for access

3.23 We note that access services are typically offered to SFV customers as part of packages which include line rental and a call allowance.

3.24 BT, for example, does not offer a standalone line-rental product - its standard line rental has an inclusive call allowance for calls at weekends at no additional price (“Unlimited Weekend Calls” package). BT also offers a number of optional packages which include different call plans at an incremental price to line rental (e.g. “Unlimited Evening & Weekends Calls”) and the “Home Phone Saver” product which offer access, calls and some ancillary services for a single package price. BT customers can pay their line rental annually in advance and receive a 10% discount for doing so (BT call this Line Rental Saver). Other CPs similarly offer a range of call plans, with

<sup>30</sup> ‘Voice-only’ is equivalent to the ‘fixed voice-only’ category discussed in our 2016 NMR Consultation (footnote 76 in Section 3), [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0016/95011/Narrowband-Market-Review.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0016/95011/Narrowband-Market-Review.pdf)). In the NMR Consultation, we at times use the term ‘split purchaser’ to mean ‘split supplier’ customers (footnote 118 in Section 4). In this document, we use ‘split purchaser’ to mean the combination of ‘split-supplier’ customers and ‘split-service’ customers.

<sup>31</sup> A small proportion of split-service customers buy SFV and a separate dual-play service, rather than a separate standalone broadband service.

small differences to BT's products (although we are not aware of any CP offering a product that is comparable to BT's Home Phone Saver).

- 3.25 The focal product of our analysis includes the line rental services which are provided as part of these packages. Any call services provided as part of these packages (whether they are provided at an incremental price to line rental or not) are included in our focal product for calls.<sup>32</sup>
- 3.26 BT also offers BT Basic, which is a product that is only available to a limited number of eligible customers.<sup>33</sup> The BT Basic package offers line rental and a limited call allowance for a much lower price than BT's other packages (see Annex 8, paragraph A8.111-A8.113). Given that BT Basic is a somewhat different product, available to only a small subset of households at a considerably lower price, we have not included it in our focal product. We nonetheless consider below (paragraphs 3.50-3.53) whether BT Basic should be included in the market on the basis of being a substitute for standard packages.
- 3.27 We discuss the focal product for calls as part of our product market definition for calls (see paragraphs 3.72-3.74)

### **Product market definition for access**

- 3.28 In assessing whether the relevant market is broader than our starting point of voice-only access, we consider the following questions:
- 3.28.1 Are dual play services in the same market as SFV services bought by voice-only customers?
- 3.28.2 Are dual play services in the same market as SFV services bought by split purchase customers?
- 3.28.3 Are SFV services bought by split purchase customers in the same market as SFV services bought by voice-only customers?
- 3.29 We then consider whether the relevant market includes:
- 3.29.1 BT Basic;
- 3.29.2 business services;
- 3.29.3 mobile services; and
- 3.29.4 fibre based services.

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<sup>32</sup> We note that calls that are inclusive with the line rental cannot be bought separately from access, so there is an argument to include them in the focal product for access. However, for simplicity, we have instead included them in the focal product for calls. This has no material effect on our analysis of SMP for access and calls.

<sup>33</sup> As far as we are aware, no other CP in this market offers an equivalent to BT Basic (KCOM, which operates in the Hull area, also has a Social Access Package available to customers in receipt of certain state benefits). Virgin's Talk Protected tariff has some similar features in offering additional inclusive calls and other features to eligible customers. However, the eligibility criteria differ from BT's package, being based on age or certain disabilities. More detail on this tariff is set out in paragraph A8.118 in Annex 8.

### Dual-play services are not in the same market as SFV services bought by voice-only customers

- 3.30 CPs offer fixed voice services bundled with other communication services, e.g. broadband, pay TV or mobile. These multi-play bundles are usually sold at a discount compared to the price of purchasing the individual components separately from different providers (or the same provider). As illustrated in Figure 1.1 in Section 1, dual-play (voice and broadband) and triple-play (voice, broadband and pay TV) bundles are particularly common. We focus on dual-play as the closest candidate substitute to SFV services bought by voice-only customers.
- 3.31 We consider whether the availability of dual-play bundles imposes competitive constraints on the provision of voice-only access. The strength of any such constraint will depend on whether enough voice-only customers are likely to switch to dual-play in response to a SSNIP to make the SSNIP unprofitable.
- 3.32 As set out in Annex 7 the relevant question for the SSNIP test is whether a price increase could be sustained above competitive levels. Our analysis is that current SFV access prices are in fact substantially above competitive levels, on the basis that:
- 3.32.1 Prices have increased materially year on year since 2009, and these increases cannot be attributed to higher input costs (indeed the largest input cost, WLR, has fallen over this time period) or falling call volumes (Figure A8.23 in Annex 8).
- 3.32.2 Our analysis is that provision of SFV services by CPs is highly profitable and profitability has been increasing over time (see Annex 5).
- 3.33 In these circumstances, the application of a SSNIP test starting from the current SFV access prices does not provide a reliable indicator as to whether dual play services are in the same relevant market. This is because, a SSNIP applied to the current prices of SFV services could be unprofitable if such prices are substantially above competitive levels, whereas it could be profitable if the SSNIP were applied to competitive prices.
- 3.34 We also note that the price of SFV services (line rental and calls) has generally been increasing at a faster rate than ADSL dual-play prices.<sup>34</sup> We compared average prices between Q1 2013 and Q3 2016 in real (inflation-adjusted) terms. On this basis, the price of SFV services increased by 17% (£3.20), compared to a 15% (£4.92) increase in standard (non-promotional) ADSL dual-play prices, but a 7% (£2.10) decrease in ADSL dual-play prices including promotions.<sup>35</sup> Prices of dual-play bundles have historically included the same line rental prices as for SFV customers, and an incremental broadband price, which generally has been the focus of competitive activity for bundles. Comparing the price of SFV services against promotional prices for ADSL bundles, the average incremental cost of upgrading from SFV to a promotional ADSL dual-play package has decreased, on average, by 53% (£5.30).<sup>36</sup>

<sup>34</sup> For more details, see Annex 8, paragraphs A8.130-A8.137.

<sup>35</sup> *Simplify Digital*.

<sup>36</sup> *Simplify Digital*.



- 3.35 We have considered whether, in principle, dual play services could impose competitive constraints on prices to voice-only customers, on the basis that:
- 3.35.1 It is possible for consumers to make a price-quality trade-off, i.e. responding to a SSNIP by switching to a product with a higher price, if the additional services included in that product (i.e. broadband) make it worth the higher price.
- 3.35.2 Accordingly, voice-only customers could potentially switch to dual play, even if they did not place much value on broadband, if the incremental price of broadband were small enough. As set out in Annex 8 paragraph A8.130, the promotional price of an ADSL dual-play service is, on average £6.18 (35%) more expensive than the line rental price offered by the main SFV providers. In this context, we note that the incremental price of broadband in a dual-play offer, above the current price of standalone voice, has decreased materially in recent years.
- 3.36 Our assessment is that voice-only customers are unlikely to be making a price-quality trade-off between their current service and dual-play, in sufficient numbers to provide a competitive constraint on SFV prices:
- 3.36.1 While price-quality trade-offs can in principle put differently-priced products in the same market, substitution requires customers to derive a utility from the higher quality or additional features sufficient to compensate them for the higher price.
- 3.36.2 In practice both standalone voice and dual-play are mature markets. To conclude that dual-play was part of our relevant market on a forward-looking basis, we would need to expect that a material number of voice-only customers, who have not taken up fixed broadband yet, would do so in response to a moderate increase in the price of SFV services. From our survey research, 68% of voice-only respondents said that the reason they do not take a bundle which includes broadband was that they do not use broadband. A much smaller proportion (8%) said they did not take a bundle including broadband due to the price of fixed broadband.<sup>37</sup> This suggests the relative price of a service with and without broadband is not the driving factor for not taking up broadband for the majority of voice-only customers.
- 3.36.3 We have received internal pricing documents from BT and other CPs relating to their decisions to increase line rental in recent years. [redacted].<sup>38</sup>
- 3.36.4 From the perspective of a provider of SFV access, any pricing constraint could be increased by the possibility that once a customer has switched to dual-play they may be unlikely to return to standalone voice in response to a change in the relative price (e.g. a reduction in the price of standalone voice).
- 3.36.5 We also note that all providers of SFV access to voice-only customers also offer dual-play bundles. A hypothetical monopoly provider of SFV access to voice-only customers could therefore expect that if any of these customers switched to dual-play in response to a SSNIP, some of these would switch

<sup>37</sup> 2015 Jigsaw residential survey (wave 1).

<sup>38</sup> [redacted].

to its own (the hypothetical monopolist's) dual-play service.<sup>39</sup> Offering competitive dual-play prices alongside line rental price increases may be a more effective way for SFV suppliers (or a hypothetical monopolist in SFV) to compete for voice-only customers who are considering buying fixed broadband as well, compared to keeping line rental prices lower. This would be consistent with the historical pattern of price changes.

- 3.36.6 In addition, as explained above, the availability of dual-play has not prevented SFV price rises from taking place in practice.
- 3.37 In some instances, dual-play bundles have been sold at prices that are close to or below landline-only packages.<sup>40</sup> If such offers were widely available, SFV service customers could save money by switching to a dual-play bundle at a lower price, even if their valuation of the broadband element of dual-play were zero. However, we do not consider that dual-play offers priced below landline-only packages place a competitive constraint on the price of SFV services in practice, because:
- 3.37.1 To the extent that such offers have been available, this has been in the context of introductory or promotional prices which were available for a limited period.
- 3.37.2 While it is possible that former SFV access customers have responded to such dual-play offers (i.e. those priced close to or below landline-only packages) by switching to dual-play, the evidence we have does not provide support for this point. While the number of SFV access customers has been declining over time, the rate of decline has slowed from 20% year on year up to Q4 2015, to around 15% year on year up to Q3 2016 (see Figure A8.4 in Annex 8), which does not appear to provide clear support for the proposition that SFV customers respond in large numbers to specific dual-play offers.
- 3.37.3 As we have set out in paragraphs 6.3-6.6, our view is that prevailing line rental prices are well above competitive levels for SFV access. We estimate later in this document that competitive line rental prices for SFV access would be more than £5-£7 per month below current levels (see paragraphs 8.19-8.30). With line rentals at these levels, no currently or recently available dual-play offers would be cheaper than SFV prices.
- 3.38 We provisionally conclude that dual-play services are not in the same market as SFV services bought by voice-only customers. In particular, this is supported by our assessment that SFV access prices (and profits) are substantially above competitive levels, which would not be sustainable if they were constrained by competition from dual-play.

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<sup>39</sup> The extent of this would depend on (a) the competitiveness of the hypothetical (SFV) monopolist's dual-play offers and its prominence in the dual-play market, and (b) the extent to which its voice-only customers contacted it before switching, giving it the opportunity to upsell them to dual-play as a retention activity.

<sup>40</sup> For example, in Ofcom's Consumer Experience Report 2015 (p. 26) we noted that Sky offered ADSL broadband free for a year (with line rental payable) increasing to £10 a month thereafter. [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0023/38543/annex.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0023/38543/annex.pdf)

### Dual-play services are not in the same market as SFV services bought by split purchase customers

- 3.39 As set out above (paragraph 3.21), SFV access is bought by two different types of customers: voice-only customers, and split purchase customers – i.e. customers who also purchase broadband services either from a different supplier (split-supplier customers) or on a standalone basis outside a bundle from the same supplier (split-service customers). Although split purchasers buy the same SFV access product as voice-only customers, the combination of products that they purchase (SFV and broadband services) could be considered as functionally equivalent to dual-play services. We have therefore considered these two services in reaching our view on the boundaries of the relevant product market.
- 3.40 There is evidence that split-supplier customers<sup>41</sup> are on average younger and of higher socioeconomic grade than voice-only customers (see Figure A8.49 of Annex 8), and, by definition, have internet access (unlike the majority of voice-only customers<sup>42</sup>). For these reasons, they are arguably more likely to be aware of alternative offers and/or engaged in the market. Consistent with that, we set out in Annex 8 some survey-based evidence that split-supplier customers may be more engaged than voice-only customers (15% compared to 6%),<sup>43</sup> with broadly similar levels of engagement to dual-play customers (20%) (see figure A8.51).
- 3.41 However, we consider that observed outcomes are not consistent with the existence of a competitive constraint from dual play services to the prices for standalone services paid by split purchasers:
- 3.41.1 Our analysis (see Annex 8, Figure A8.43) shows that on average a split purchaser paying a combined price for standalone voice from BT<sup>44</sup> and standalone broadband from BT, Sky or TalkTalk could save £8 per month (more than 20%) by switching to an equivalent dual-play service from their broadband provider at standard prices, and just over £14.50 per month (more than 35%) at promotional dual-play prices. If dual-play was a close enough substitute to competitively constrain the combined prices for functionally equivalent voice and broadband services purchased on a standalone basis by split purchasers, we would not expect these price differences to be sustainable.<sup>45</sup>

<sup>41</sup> As explained in Annex 8 when discussing survey evidence, we refer to split-supplier customers, who account for around 80% of split purchasers.

<sup>42</sup> 4% of voice-only customers reported having mobile broadband in the Jigsaw residential survey. See paragraph A8.128, in Annex 8.

<sup>43</sup> This difference is statistically significant (at the 95% confidence level). Unless otherwise stated, all direct comparisons of survey evidence between customer groups in this section are statistically significant.

<sup>44</sup> The evidence (discussed in more detail in Section 4, paragraph 4.22-4.23 and Annex 8 – supporting evidence is that nearly all split purchasers buy standalone voice from BT, whereas they buy standalone fixed broadband from a range of broadband suppliers.

<sup>45</sup> The number of SFV service customers has been declining over time, at a broadly consistent rate (although a slower rate in recent quarters). While we do not have clear evidence on this point, it is possible that a substantial number of split purchase customers have switched to dual-play services. However, this has not led to a competitive outcome of the remaining split purchasers paying similar combined prices to dual play customers. If we consider split purchasers taking SFV from a hypothetical monopolist, if some of those customers are marginal – i.e. willing to switch in response to a SSNIP on SFV – one of their choices is to switch to a dual-play service from their supplier of SFV,

- 3.41.2 In addition, as noted above, prices for SFV access have been increasing on an annual basis. This has not been prevented by the potential for, and existence of, split purchasers switching to dual play bundles over this period (such switching is likely to explain, to some extent, the material decline over time in the number of SFV customers).
- 3.41.3 While the number of SFV customers has been falling over time, and this is likely to include a proportion of former split-purchase customers switching to dual-play, there remains a sizeable group of split purchasers (about 1.2 million) who have not responded to these price increases by switching to dual-play. Reported annual switching rates are equally low for both voice-only and split supplier customers (3%) compared to dual play (12%) (see Annex 8, Figure A8.55). In view of this, on a forward-looking basis we consider that the remaining split purchasers are unlikely to switch to dual-play in response to a SSNIP in sufficient numbers to constrain SFV prices to competitive levels.
- 3.42 We also note that:
- 3.42.1 We have attempted to compare the changes over time in the combined price paid by split purchasers for standalone voice and broadband with the changes over time in prices for comparable dual-play bundles. However, we do not have data on the change in prices of standalone broadband services over time.<sup>46</sup> Based on the available evidence (see paragraph 3.34 above), we note that the prices of SFV services have increased by a faster rate than the price of ADSL dual-play services. Whether the combined price to split purchasers has increased at a faster rate than comparable dual-play services turns on the change in standalone broadband prices, on which we do not have evidence. However, we note that, unless standalone broadband prices to split purchasers have been (at most) increasing at a somewhat slower rate than dual-play prices over this period, the services bought by split purchasers may be increasingly poor value relative to dual-play services;
- 3.42.2 As set out in Section 8, our analysis indicates that SFV services for both voice only and split-purchase customers have been highly profitable. We would not expect providers of SFV services to split purchasers to be able to sustain such a high level of profitability if they were facing competitive constraints from dual-play services; and
- 3.42.3 [redacted].<sup>47</sup>
- 3.43 For these reasons, we consider that SFV services bought by split purchasers are not in the same market as dual-play services.

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instead of switching their SFV service. A possible implication of this is that, from the perspective of the hypothetical monopolist, the more effective way of retaining any marginal split purchase customers may be to offer them a competitive dual-play bundle, rather than holding down the price of SFV services.

<sup>46</sup> However, we note that TalkTalk's standalone broadband price has recently increased from £20.30 to £22.30 – a 10% increase.

<sup>47</sup> [redacted].

SFV access bought by split purchasers is in the same market as SFV access bought by voice-only customers

- 3.44 The provision of access as part of a SFV service is the same product at the same price regardless of whether the customer is a voice-only consumer or a split purchaser buying standalone broadband separately. Given that they purchase identical products under identical terms, voice-only customers and split purchasers would in principle fall under the same market.
- 3.45 We recognise, however, that there might be reasons to exclude different customer groups from the relevant market even where such groups purchase the same service. For example, the OFT market definition guidelines mention that “*Where a hypothetical monopolist would (or would be likely to) price discriminate significantly between groups of customers, each of these groups may form a separate market. If so, a relevant market might be defined as sales of the relevant product in the relevant geographic area to a particular customer group.*” (para 3.19). In such circumstances of price discrimination, the two groups of customers would not face a common pricing constraint.
- 3.46 CPs are not generally sure which of their customers are voice-only customers or split-supplier customers (i.e. they do not necessarily know whether customers are getting a standalone broadband service from elsewhere). Accordingly, to date BT and other CPs have not charged different prices for SFV services depending on whether the customer is voice-only or a split purchaser.
- 3.47 In the case of split-service customers, who take both SFV and standalone broadband services from the same provider, the CP should be aware that they are split-purchase customers. However, we understand that to date these customers have paid the same price for SFV services as voice-only customers.
- 3.48 It is possible that CPs could take steps to identify which of their SFV customers also buy broadband separately, and price discriminate between these customers and voice-only customers. However, to date CPs have not done this, nor have they price discriminated where they already know this (i.e. in the case of split-service customers). While we cannot rule out the possibility of such price discrimination taking place in future, we do not consider that this evidence indicates that a hypothetical monopolist of SFV services would, or would be likely to, price discriminate significantly between voice-only and split purchase customers.<sup>48</sup>
- 3.49 We therefore provisionally conclude that the relevant market is at least as broad as the provision of SFV services (i.e. to both voice-only and split purchase customers).<sup>49,50</sup>

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<sup>48</sup> If there was such price discrimination between voice-only and split purchase customers, it might imply two narrower, separate markets for SFV access services, one for voice-only and the other for split purchasers (noting our provisional conclusions above that dual play bundles are unlikely to competitively constrain SFV to either voice-only or split purchase customers).

<sup>49</sup> In the case of BT, this includes the Standard Line Rental, Standard Line Rental Saver and Home Phone Saver 2019 as per the current BT Consumer Price List (effective from 10 February 2017).

<sup>50</sup> As customers of standalone voice services comprise two distinct groups – voice-only and split purchasers – it is possible in principle that enough marginal customers from either group (or both groups in combination) would be willing to switch to dual-play in order for us to include dual-play in the relevant market. We have considered separately the willingness of each group to switch to dual-play. However, on the basis of the above analysis, our view is that not enough marginal customers in either

### The relevant market does not include BT Basic

- 3.50 BT Basic is a product that is available to consumers who are on specific low income government benefits and offers a limited service at a much lower price than a comparable service at standard prices. It is offered at £5.10], which is 27% of BT's standard monthly line rental of £18.99 – see paragraph A8.112, Annex 8). This includes a £1.50 monthly call allowance, which would allow the customer to make around ten one-minute calls or one thirteen-minute call in a month. Subsequent calls are charged on a per-minute rate, up to a £10 per month cap for calls to UK geographic and UK mobile numbers which is subject to a fair-use policy.
- 3.51 There are a number of barriers to SFV customers switching to BT Basic in response to a SSNIP:
- 3.51.1 Many SFV customers would not be able to switch to BT Basic due to the eligibility criteria.
- 3.51.2 The restricted features of BT Basic, in comparison to other packages, are likely to make it unattractive or unsuitable for at least some of those who are eligible but have not yet switched.<sup>51</sup>
- 3.51.3 Awareness of BT Basic is limited. Ofcom research in 2014 found that 70% of those eligible for BT Basic were unaware of it.<sup>52</sup>
- 3.52 To the extent that there are any SFV customers who (a) are eligible for BT Basic, (b) are aware of it, and (c) do not consider it unsuitable for their needs, such customers already have a strong incentive to switch to it in the large price discount available relative to other SFV services, and hence the large savings they could potentially make by switching.<sup>53</sup> The fact that they have not responded to this incentive by switching makes it unlikely that they would respond to a SSNIP by switching to BT Basic, to an extent that would constrain the price of SFV services. Even if awareness and take-up of BT Basic increases in future, any potential constraint on SFV prices will be limited by the sharp differences in terms and conditions from SFV packages and the associated barriers to switching due to eligibility and suitability.
- 3.53 In light of this, we do not consider that the price of SFV access is constrained by the ability of consumers to switch to BT Basic in response to a SSNIP on the price of their package.

### The relevant market does not include business SFV access

- 3.54 SFV access services are available to business customers with broadly comparable line rentals but different call packages – for example, BT offers 100 free UK calls per month or unlimited UK calls for an extra £10, rather than having free calls at evenings and/or weekends (which would be unsuitable for many businesses). We also note

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group, or across both groups in combination, are willing to switch to dual-play to constrain SFV prices to competitive levels.

<sup>51</sup> The £10 per month cap, which was introduced in December 2016, may make the service suitable for some eligible consumers for whom it was not previously suitable.

<sup>52</sup> See Ofcom, *Results of research into consumer views on the importance of communications services and their affordability*, 22 July 2014

[https://www.ofcom.org.uk/data/assets/pdf\\_file/0010/40231/affordability\\_report.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0010/40231/affordability_report.pdf)

<sup>53</sup> If most eligible customers had switched, there would be little scope for prices to be constrained by the prospect of further switching in future.

differences in competitors, with the largest competitors to BT in the residential market those leveraging a retail brand (such as SSE and Post Office), in contrast to specialist CPs in the business market.

- 3.55 However, there is limited scope for demand-side substitution from residential to business services because in order to purchase a business access line from BT a customer is required to submit a company registration number, which would prevent a residential user from acquiring a business line.<sup>54</sup>
- 3.56 Overall, we do not consider we have a basis for believing that a SSNIP in SFV access would lead to material numbers of SFV customers switching to business services. We therefore do not include business SFV services in the market.<sup>55</sup>

### The relevant market does not include mobile access

- 3.57 We consider whether mobile access imposes competitive constraints on the provision of SFV access service. The strength of this constraint will depend on the willingness of SFV customers to abandon their fixed voice service and rely entirely on mobile access (i.e. become mobile-only customers).<sup>56</sup> The many consumers that continue to buy both fixed and mobile access are demonstrably willing to pay access prices for both, suggesting that, for these customers, mobile access does not provide a competitive constraint on fixed access prices.
- 3.58 Around 70% of SFV customers have access to mobile phones; however, this is lower for voice-only customers compared to split-supplier customers (58% and 95%, respectively).<sup>57</sup> The relevant question is whether, at competitive landline prices a SSNIP would lead enough SFV customers to switch to becoming mobile-only customers.
- 3.59 It is challenging to define and compare typical retail access prices because both fixed and mobile access are generally bundled with calls. However, survey evidence and actual past behaviour of SFV customers suggest that they have low willingness to switch to mobile-only in response to changes in relative prices:
- a) Willingness to give up landline: Survey evidence suggests that 61% of SFV respondents slightly or strongly disagreed that they would be willing to give up their landline under certain circumstances. If broken down by customer type, results are 63% for voice-only customers, and 54% for split-supplier customers.<sup>58, 59</sup>

<sup>54</sup> As set out above, a number of SMEs purchase residential SFV services, raising the possibility that they could switch to a business SFV service in response to a SSNIP on residential SFV services. As noted above, around 30% of SMEs report that they use a residential fixed line.

<sup>55</sup> We also note that BT is the main line rental provider to around half of UK SMEs, which would further reduce any pricing constraint on SFV access from switching to business services. (See Jigsaw Market Research Report, *Narrowband Market Review 2016*, <https://www.ofcom.org.uk/consultations-and-statements/category-1/narrowband-market-review>)

<sup>56</sup> We consider substitution between mobile calls and fixed calls later under our analysis on product market definition for the calls market.

<sup>57</sup> *Ofcom*, Technology Tracker H2 2016.

<sup>58</sup> There may be some small differences in the voice-only figures reported from the 2015 Jigsaw residential survey between this chapter and the 2016 NMR Consultation, due to a revised approach to isolating these customers (see Annex 8).

<sup>59</sup> 2015 Jigsaw survey (wave 1).

- b) Response to hypothetical SSNIP: Only 9% of SFV survey respondents reported that they would be ‘certain or very likely’ to give up their landline and switch to using mobile only in response to a 10% price increase in their total landline bill.<sup>60</sup>
- c) Past behaviour: Despite the significant increase in retail line rental prices over the past six years and decreasing mobile price,<sup>61</sup> the share of mobile-only consumers in the UK has remained stable (15% of adults).<sup>62</sup> As set out in Annex 8 (Figure A8.23), fixed line rental from most CPs has been increasing by more than 5% annually (about £1 per year). Despite these price increases, take-up of fixed telephony has remained relatively stable (at between 84% and 87% of households from 2009 to 2016)<sup>63</sup> – and has not experienced as marked a decline as we might expect if mobile were a close substitute (especially given the decrease in mobile prices noted above). In addition, the proportion of adults in mobile-only homes did not change over the same period at 15%. This also suggests more generally that residential consumers only display limited responsiveness to price changes for fixed lines.

- 3.60 This analysis of past behaviour provides evidence on actual customer responses to the recent changes in relative prices. We recognise that this evidence relates to all types of fixed voice services. Nevertheless, it is appropriate to use it as a proxy for past behaviour of SFV customers. This is because survey evidence suggests that they are likely to be less price sensitive compared to the average residential fixed voice customer. For example, 9% of SFV customers reported they would be certain or very likely to give up their landline in a response to a 10% price increase in their total landline bill. This compares to 19% of all fixed voice customers (i.e. standalone and bundle customers).<sup>64</sup>
- 3.61 Overall, evidence suggests that while there is a degree of substitutability between fixed and mobile access, standalone consumers predominantly view the two types of access as meeting different needs and do not regard them as close substitutes.
- 3.62 Therefore, we provisionally conclude that it is more appropriate to consider that fixed and mobile access are in separate markets.

### Fibre based services

- 3.63 At present the roll-out of fibre based broadband services has largely been as an adjunct to the existing copper based telephone network. BT and other CPs continue to use the copper lines for the delivery of voice.
- 3.64 There is likely to be an increased trend to the provision of voice services over broadband as we see the roll-out of fibre connections which are either not reliant on the copper network (Fibre to the Premise) or do not provide voice connections over the copper network.

<sup>60</sup> 2015 Jigsaw survey (wave 1).

<sup>61</sup> The ‘weighted average’ price of a mobile connection with 50 minutes of voice, 0 SMS and 0 data has fallen by 5% for a mobile connection (excluding handset cost), and up to 12% on prepay, between 2012 and 2016. Mobile packages including more data have fallen by a greater amount over this period. Source: Ofcom using data supplied by Teligen.

<sup>62</sup> Ofcom, *Communications Market Report 2012* and *Communications Market Report 2015*.

<sup>63</sup> Ofcom Technology Tracker. Data from Q1 for 2009-2014, then H1 for 2015-16. See Figure 4.35 of Ofcom’s *Communications Market Report 2016* (“CMR 2016”), available here: [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0026/26648/uk\\_telecoms.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0026/26648/uk_telecoms.pdf).

<sup>64</sup> 2015 Jigsaw survey (wave 1).



- 3.65 BT envisages that by 2025 it will move to replace the traditional copper based voice network with a next generation service based on fibre. It is likely that this could mean a material transformation of the nature of standalone voice provision – it may not be practical to limit service provision purely to voice.
- 3.66 However, we are not aware of any plans for a significant programme of traditional voice service replacement within the forward look of this review. Equally, existing SFV customers are unlikely to seek out a fibre based service unless they were planning to move to a bundle which includes broadband.<sup>65</sup> Accordingly, we do not consider that this is a material consideration for our market definition in this review.

### No supply-side substitution

- 3.67 In this sub-section, we consider whether there is scope for supply-side substitution from other services – i.e. suppliers of those services switching to supply of SFV services in response to a price increase.
- 3.68 As noted in Annex 7, paragraphs A7.17 – A7.18, for supply-side substitution to be relevant suppliers must be able to enter the market quickly and at low cost by virtue of their existing position in the supply of other products or geographic areas, and there must also be an additional competitive constraint arising from such entry into the supply of the service in question, beyond that imposed by demand-side substitutes which those firms already produce.
- 3.69 The wholesale products needed for the physical supply of SFV access and calls services are widely available in the UK. Current providers of fixed telecoms services, and potentially new entrants, could use these wholesale products – or in Virgin’s case its own network – to supply SFV access and calls. In fact, the main telecoms providers already supply some SFV customers.
- 3.70 However, the scope for expansion by these firms, or new entry, in the supply of SFV services is limited by the barriers to, and high cost of, acquiring new customers. We discuss these barriers to entry further in Section 4, paragraphs 4.29-4.46. Due to these barriers, in our view it is not possible for new firms to enter, or for current providers to expand in, the market quickly and at low cost by virtue of their existing position in the supply of other products or geographic areas.
- 3.71 We do not therefore propose to broaden the market based on supply-side substitution.

### **Product market definition for calls**

- 3.72 As discussed above, our focal product for access was the supply of SFV to voice-only customers, and we then extended this to include SFV to split purchase customers. We consider that for similar reasons split purchase customers should be included in the market for calls:
- 3.72.1 The only way for a voice-only or split purchase customer to receive calls within a dual-play bundle would be to switch to receiving access within a dual-play bundle. In light of our analysis that dual-play bundles are not in the same market as voice-only or split-purchase services for access, we consider it appropriate to treat them similarly for calls.

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<sup>65</sup> [§<].

- 3.72.2 To date voice-only and split-purchase customers have been charged the same prices for calls, and we do not have evidence that a hypothetical monopolist of SFV calls would, or would be likely to, price discriminate significantly between voice-only and split-purchase customers.
- 3.73 Accordingly, the starting point for our analysis of the product market definition for calls is fixed voice calls sold to SFV access consumers, i.e. including voice-only and split-purchase customers. However, as we discuss below, there may be differences in the scope for voice-only and split purchase customers to substitute between SFV calls and other services.
- 3.74 We consider whether there is a case for including any of the following in the relevant market:
- Different call plans;
  - Different types of calls;
  - Fixed voice calls sold to dual-play/multi-play customers;
  - Mobile calls;
  - VoIP services;
  - Other means of communication (e.g. email, text);
  - Business services.

The relevant market includes all call plans and out-of-plan calls

- 3.75 As noted above, a range of call plans are available to voice-only customers which differ in their call allowances, as well as out-of-plan calls. This raises a question of whether they are all part of the same product market for calls purchased by voice-only customers. CPs broadly offer three different types of call plan. These are plans that include unlimited weekend calls, unlimited evening and weekend calls, and unlimited anytime calls. The main difference between them is the restrictions around the allowance of ‘free’ calls included in the plan (i.e. type and number of minutes included and the timings allowed to make calls).
- 3.76 We consider different call plans to be close demand-side substitutes for each other and for out-of-plan calls. Marginal SFV customers may trade-off between the price and quality of different plans or out-of-plan calls in response to a SSNIP. For example, if the price of the most restrictive plan increases by a 5-10% relative to other plans, it is likely that some marginal consumers may switch to less restrictive plans, and vice versa.
- 3.77 This is consistent with CPs’ pricing strategies, which suggest that different call plans face similar pricing constraints. The increases in prices for calls over time were equally applied to all packages, leading to broadly similar absolute increases in the prices of the plans (albeit with larger proportionate increases for cheaper plans than for more expensive plans). We also note that [3<].

The SFV market includes all types of calls

- 3.78 Retail consumers use their fixed lines to make various types of calls, including calls to other geographic numbers, mobile numbers, international numbers and non-geographic numbers. We propose defining a single relevant market including all types of calls (i.e. geographic, fixed to mobile calls, international and other calls) made by SFV customers as the starting point for our analysis.
- 3.79 The main reason for this is that consumers, with very limited exceptions, choose a single fixed line provider to meet all of their call type needs. Therefore, they will select their calls provider on the basis of which one provides the best value for money tariff given their particular pattern of calls.
- 3.80 To illustrate this, suppose a provider were to increase the price of calls to mobile numbers by 5-10%. A consumer who wished to switch to another provider of calls to mobile can only do so either by switching all of their call needs, or by purchasing additional fixed line access. The latter would tend to incur a substantial additional connection and rental cost and is unlikely to provide a realistic alternative for the consumer. Competition therefore takes place primarily on the basis of the overall value for money of the call package.
- 3.81 While retailers compete by offering a tariff package, the competitive conditions may vary to some extent across different call types. For example, high volume users of international calls will often choose to use a calling card or VoIP, while the price of calls to mobile will be limited to a significant extent by the ability of consumers to use a mobile phone for the same call. We take this into account in the SMP assessment at Section 5, paragraphs 5.31-5.35.

The relevant market does not include dual-play/multi-play calls

- 3.82 We have already noted that for suppliers to compete for calls generally means them competing for access to the relevant consumers, because access and calls are mostly bought from the same provider in a package. As explained above, in our view, SFV access is in a separate market from dual-play and other multi-play bundles. It would seem therefore that competition for SFV calls is similarly distinct from calls offered to other customers such as in bundles. However, we consider here whether there is a reason to define a broader market on the basis of a common pricing constraint.
- 3.83 The potential for a common pricing constraint is that CPs offer similar call plans to all types of fixed voice consumers. Customers who buy SFV access services and those who buy dual-play/multi-play access packages purchase the same call plans and under similar terms. This raises the question of whether the relevant market for calls includes all types of voice customers.
- 3.84 We consider that a hypothetical monopolist of the fixed calls market would be able to price discriminate significantly between SFV access consumers and other types of fixed voice consumers. As most consumers purchase access and calls from the same supplier, the provider can distinguish whether a customer purchases fixed voice access on a standalone basis or bundled. There is no reason why the CP could

not accordingly offer different prices for call plans and out-of-plan calls to different customers based on this and there is at least one example of this.<sup>66</sup>

- 3.85 Therefore, given the reasons to limit the scope of the market for SFV calls, distinct from calls by other customers in dual or multi play bundles, similarly as for SFV access, we provisionally conclude that the relevant market for SFV calls does not include calls by customers on dual-play/multi-play bundles.

### The relevant market does not include mobile calls

- 3.86 The 70% of SFV access consumers in the UK who also have mobile access have a degree of choice as to whether to make a call on their mobile or fixed line.<sup>67</sup> To define the relevant market for calls, we consider whether SFV access users are likely to substitute enough calls from landline to mobile services in order to make a SSNIP by a hypothetical monopolist of voice calls unprofitable.
- 3.87 In our Narrowband Market Review consultation<sup>68</sup> (paragraphs 4.136 to 4.156) we considered whether retail prices of fixed voice calls were constrained by competition from mobile.
- 3.88 We noted that the constraint from mobile would depend on the willingness of consumers to do the following:
- Partially or completely substitute from fixed voice calls to mobile calls. This may include reducing the calls made within the inclusive calls allowance, downgrading the calls package, making fewer out-of-bundle calls, or some combination of these.
  - Give up the bundle of fixed voice access and calls and become mobile-only. For those who have fixed broadband this would involve giving it up and relying either on mobile broadband or other alternatives to fixed internet access.
- 3.89 We noted that call-by-call substitution alone can provide a degree of indirect constraint, particularly if consumers are also willing to downgrade a calls package. However, a significant share of total fixed voice minutes are made within an allowance. In addition, some consumers will already have the most basic calls package and so are unable to downgrade further. We therefore considered that the competitive constraint would depend to some extent on consumers' willingness to give up their bundle of fixed access and calls altogether (and broadband if they have it) and become mobile only.
- 3.90 We noted that mobile calls made at a fixed location (the home for residential customers, or the place of work for business customers) respond to the same need as fixed calls, which indicates there is potential (one-way) substitutability from fixed to mobile. However, survey evidence suggested that some consumers continue to view mobile calls as inferior in quality or less reliable. For example, a significant minority of SFV respondents said they do not make all their calls by mobile when at home

<sup>66</sup> There are examples of such discrimination today – BT's Home Phone Saver product is only available to SFV customers and includes a unique calls offering.

<sup>67</sup> Ofcom, *Technology Tracker, H2 2016*.

<sup>68</sup> Ofcom Narrowband Market Review consultation, 1 December 2016, [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0016/95011/Narrowband-Market-Review.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0016/95011/Narrowband-Market-Review.pdf).

because of ‘Reliability of connection’ (14%), ‘Quality of line/calls’ (15%), ‘Inconvenient/Difficult to use’ (9%), ‘Coverage/can't get a signal’ (8%).<sup>69</sup>

- 3.91 We noted that 11% of voice-only survey respondents reported that they would be certain or very likely to give up their landline in response to a SSNIP of their landline, while 14% would be certain or very likely to switch some calls to mobile in response to a SSNIP of their landline calls<sup>70</sup> (in these responses, voice-only customers appeared to be less price-responsive than fixed voice customers generally). We said that overall, the evidence was consistent with residential consumers showing a degree of attachment to their landlines and only a limited willingness to give up the bundle of access and calls and become mobile-only consumers, but that there may be a strong degree of substitutability on a call-by-call basis. We noted a significantly lower degree of reported substitutability by SMEs than residential consumers.
- 3.92 We observed a marked decline in the volume of voice calls originated on fixed lines and an increase in calls originated on mobiles by both residential consumers and businesses. However, we said that, overall, calling patterns suggested that fixed and mobile were more typically used for different types of calls rather than as substitutes for the same type of calls. Most calls to mobiles were from other mobiles whereas landlines were used more heavily for calls to other landlines, calls to Freephone numbers and calls to non-geographic numbers. For example, in 2015, 60% of calls terminating on fixed lines originated from a fixed line whereas only 7% of calls terminating on a mobile device originated from a fixed line.
- 3.93 We compared residential fixed and mobile prices, and noted that the price of calls has been decreasing for both fixed voice and mobile, although there was a greater decrease for mobile. The current analysis does not show a clear decrease in fixed voice call prices (see Annex 8 paragraphs A8.80 – A8.108). However, the pence per minute price of out-of-plan mobile calls was still materially higher than the price of out-of-plan fixed calls. The leading reason cited by 37% of respondents to our residential survey for not making all calls by mobile at home was the price of calls being too high.<sup>71</sup>
- 3.94 In conclusion, we considered that, from a forward looking perspective, the evidence on the strength of fixed-to-mobile substitutability was mixed. Consumers had a limited willingness to abandon their landline (i.e. access and calls) and this is likely to limit the overall indirect constraint from mobile. Nevertheless, mobile appeared to be a relatively close substitute on a call-by-call basis with respect to some call types by certain groups but a more limited substitute for others. Mobile call prices had fallen in relative terms and call volumes had increased, and this appeared to be at least a partial driver of the fall in fixed voice volumes.
- 3.95 Balancing these various factors, we considered that mobile calls are not a sufficient indirect constraint on fixed calls to be included in the relevant product market (at the wholesale level), although we recognised the increasing competitive constraint for calls – if not in access – in our assessment of market power.
- 3.96 Much of our assessment in the NMR consultation related to fixed calls generally, rather than SFV calls in particular. However, we consider that the considerations

<sup>69</sup> 2015 Jigsaw survey (wave 1), Figure 9 and 46.

<sup>70</sup> We do not have robust evidence on split-purchase customers 2015 Jigsaw residential survey (wave 1).

<sup>71</sup> 2015 Jigsaw residential survey (wave 1).

supporting our position in NMR also apply in the case of SFV customers, noting that SFV customers are less likely than fixed voice customers generally to have mobile phones, and that in the survey evidence discussed above they appear to be less price-responsive than fixed voice customers generally.

- 3.97 Consistent with our assessment in the NMR consultation, we consider that mobile calls are not a sufficient constraint on SFV calls to be included in the relevant product market. However, we consider the potential for mobile calls to provide an increasing (out-of-market) constraint for SFV calls – if not in SFV access – in our assessment of market power. The relevant market does not include VoIP
- 3.98 VoIP calls can be a potential substitute for fixed voice calls, where they are made over broadband access (or a mobile device) rather than an analogue fixed voice service.
- 3.99 We do not propose to include VoIP using broadband or mobile devices in the product market for SFV calls based on the following survey evidence:
- a) The majority of SFV customers do not have fixed broadband access (i.e. voice-only customers who account for 60% of SFV customers), hence they are unable to use VoIP over broadband at home.
  - b) Only a minority of SFV customers reported having VoIP at home (2%).<sup>72</sup>
  - c) Only 5% of SFV survey respondents said they would be certain or very likely to switch some calls to VoIP in response to a SSNIP for calls.<sup>73</sup> Results were broadly similar for voice-only and split supplier customers (5% and 6%, respectively).<sup>74</sup> This suggests a limited degree of substitutability between SFV calls and VoIP.
- 3.100 Based on this evidence, it appears that a minority of SFV customers use VoIP and it is mainly for a limited range of call types (international calls and calls to other VoIP users).

#### The relevant market does not include other means of communication

- 3.101 The fall in fixed voice call volumes has been accompanied by a rise in alternative modes of communication. The average adult reported spending more time per day using email (60 minutes), instant messaging (48 minutes) and social networking (45 minutes) than making phone calls (27 minutes) in 2016.<sup>75</sup> The share of adults using mobile messaging rose slightly from about 80% of adults in 2012 to about 83% in 2016.<sup>76</sup>
- 3.102 However, the number of outgoing SMS and MMS fell from its peak of 151 billion in 2012 to 101 billion in 2015<sup>77</sup> and the number of minutes spent texting per day fell by 14 minutes (40%) between 2014 and 2016. The share of residential consumers using email weekly fell from 77% to 70% between 2014 and 2016 and the share using SMS weekly fell from 71% to 63% in the same period.

<sup>72</sup> 2015 Jigsaw survey (wave 1).

<sup>73</sup> 2015 Jigsaw residential survey (wave 1).

<sup>74</sup> 2015 Jigsaw residential survey (wave 1).

<sup>75</sup> Ofcom, *CMR 2016*, figure 1.18.

<sup>76</sup> Ofcom, *CMR 2012*, figure 5.18; Ofcom, *CMR 2016*, figure 4.36.

<sup>77</sup> Ofcom, *CMR 2016*, figure 4.1.

3.103 These activities may have been displaced by increased use of OTT instant messaging applications. The share of residential consumers using instant messaging rose by 15% to 43% between 2014 and 2016.<sup>78</sup>

3.104 However, survey data suggests that substitutability for SFV calls is likely to be limited:

- SFV customers value voice calls for the personal contact involved, with SMEs also valuing their convenient and real-time nature compared to text-based communication. Survey respondents were asked why they do not use SMS/Email/Instant Messaging often at home, instead of making calls on their landline. The top two responses were that 20% of SFV respondents said they prefer to talk to the other person and 14% said they are not suitable for certain types of conversation.<sup>79</sup>
- A small proportion of SFV residential survey respondents (9%) said they would be certain or very likely to switch some landline calls to email, mobile phone texts or instant messages in response to a SSNIP for landline calls.<sup>80</sup>

3.105 Based on the above, we do not consider that retail switching to text-based messaging (including SMS via a mobile device, instant messaging and OTT-based messaging services), email and social media would be sufficient to make a price increase in SFV calls unprofitable. We consider that such services are outside the relevant product market.

#### The relevant market does not include business SFV calls

3.106 In paragraphs 3.54-3.56 we set out a number of differences in the prices and quality characteristics of residential and business services and the limited scope for substitution of residential products with business products. We concluded that in light of this, we do not consider that business SFV access services should be included in the relevant market. For the same reasons, we consider that business SFV call services should be excluded from the relevant market for SFV calls.

#### **Provisional conclusion for product market definition**

3.107 We have provisionally concluded that there are two relevant markets; residential SFV access and fixed voice calls sold to SFV access customers.

3.108 We have considered whether there are any effective substitutes:

- For SFV access: we have provisionally concluded that dual-play access packages, mobile access and business services are not effective demand-side substitutes. Therefore, they are not part of the market.
- For calls to SFV access customers: we have provisionally concluded that all call packages and all types of calls fall within the same relevant market. We have also provisionally taken the view that the provision of calls to customers who purchase multi-play packages is not in the same market. In addition, we do not consider that mobile access, VoIP or other communication services are part of

<sup>78</sup> Ofcom, *CMR 2016*, page 16.

<sup>79</sup> 2015 Jigsaw residential survey (wave 1).

<sup>80</sup> 2015 Jigsaw residential survey (wave 1).

the same market. However, we take into account out of market constraints from mobile calls in our SMP assessment.

- 3.109 We note that our proposals are consistent with other regulatory practice. Historically, retail fixed voice access was identified by the EC as one of the relevant markets susceptible to *ex-ante* regulations (Market 1). The Commission for Communications Regulations (ComReg) reviewed this market in August 2014 as part of its duties under the European Framework for Economic Communications at the time. ComReg defined two relevant markets for residential consumers; which are equivalent to SFV access and SFV calls markets (i.e. both include split purchasers and excluded other potential substitutes such as dual-play packages, mobile services and VoIP).<sup>81</sup>

## Retail geographic market definition

- 3.110 According to the 2014 EC Recommendation, when defining relevant markets “national regulatory authorities should identify a geographic area where the conditions of competition are similar or sufficiently homogeneous and which can be distinguished from neighbouring areas in which the prevailing conditions of competition are appreciably different, having particular regard to the question whether the potential SMP operator acts uniformly across its network area or whether it faces appreciably different conditions of competition to a degree that its activities are constrained in some areas but not in others”.<sup>82</sup>
- 3.111 In the UK excluding the Hull Area, we consider that competitive conditions are broadly similar and there is a clear national dimension in competition for SFV services. In particular, evidence shows that price is the main mode of competition and CPs have national uniform pricing policies:
- 3.111.1 Survey data suggests that price is a significant factor when customers switch telecoms providers<sup>83</sup>;
  - 3.111.2 the USC requires BT to provide retail telephony services that are priced uniformly, irrespective of geographic location. Furthermore, we observe that competing CPs price uniformly across the UK.
- 3.112 We recognise that CPs can also compete on non-price factors (e.g. quality of retail customer service). However, we do not have evidence of material geographic variation in non-price elements of SFV services.
- 3.113 In the Hull Area, the absence of BT means that competitive conditions differ from the rest of the UK. While BT is the largest SFV provider in the UK, KCOM is the largest provider in the Hull Area with a share of 97% of fixed analogue lines as of March 2016.<sup>84</sup>

<sup>81</sup> <https://www.comreg.ie/publication/market-review-retail-access-to-the-public-telephone-network-at-a-fixed-location-for-residential-and-non-residential-customers-2/>

<sup>82</sup> The 2014 EC Recommendation, Point 7.

<sup>83</sup> 2015 Jigsaw residential survey (wave 1).

<sup>84</sup> See 2016 NMR



## Provisional conclusions on geographic markets

3.114 In light of the above, we propose defining the relevant geographic area for this review as the UK excluding the Hull Area.<sup>85</sup>

3.115 This is consistent with the findings of 2009 Retail Narrowband Review, which is summarised in Section 2.

## Three criteria test for retail standalone fixed voice market(s)

3.116 In carrying out a market review, we are required to take due account of the European Commission's (EC) Recommendation on relevant product and service markets ("the 2014 EC Recommendation") and its SMP Guidelines. More broadly, in carrying out a market review (including assessing appropriate remedies), we are required to take utmost account of all applicable opinions, common positions, recommendations, guidelines, advice or regulatory best practice adopted by BEREC.<sup>86</sup>

### The 2014 EC Recommendation

3.117 The 2014 EC Recommendation, which replaced the 2007 EC Recommendation, sets out a list of those product and service markets which the Commission has identified, at an EU level, as being susceptible to *ex ante* regulation. These markets are identified on the basis of the cumulative application of three criteria:<sup>87</sup>

- a) the presence of high and non-transitory structural, legal or regulatory barriers to entry;
- b) a market structure which does not tend towards effective competition within the relevant time horizon, having regard to the state of infrastructure-based and other competition behind the barriers to entry;
- c) competition law alone is insufficient to adequately address the identified market failure(s).<sup>88</sup>

3.118 NRAs may identify markets other than those listed in the 2014 EC Recommendation, on the basis of the application of the above criteria. In what follows, we apply the three-criteria test to the standalone fixed voice access and calls markets.

## Presence of high and non-transitory barriers to entry

3.119 Our analysis of barriers to entry and expansion are set out in the SMP assessments for SFV access and SFV calls in Sections 4 and 5, respectively.

3.120 In summary, our analysis shows that there are high barriers to entry (and particularly to expansion) in both markets, which are likely to remain over the period of this review (in the absence of regulation). Service providers face difficulties and high

<sup>85</sup> We explain why at this time we are not also reviewing relevant markets in the Hull Area in Section 2.

<sup>86</sup> Body of European Regulators for Electronic Communications. See Article 3(3c) of the Framework Directive. See also Article 3(3) of the BEREC Regulation (Regulation (EC) No 1211/2009 of the European Parliament and of the Council of 25 November 2009 establishing the Body of European Regulators of Electronic Communications and the Office).

<sup>87</sup> Recital 19 to the 2014 EC Recommendation.

<sup>88</sup> Paragraph 2 of the 2014 EC Recommendation.

acquisition costs to reach SFV customers and to convince them to switch away from their current suppliers (see full assessment in Section 4, paragraphs 4.29 - 4.46 and Section 5, paragraphs 5.23 - 5.26).

- 3.121 We note that, if we were to define separate markets for SFV services (both access and calls) for voice-only and split purchase customers, this criterion would be met in each of the resulting markets, as we have not identified substantial differences between the level or duration of barriers to entry and expansion for different customer groups.

### **A market structure which does not tend towards effective competition**

- 3.122 We have assessed competition in the SFV access market as part of our SMP analysis in Section 4. In particular:

3.122.1 the SFV access market is highly concentrated. BT has a high market share of 79%. The next largest provider has a share of 5%-15 (see paragraphs 4.18);

3.122.2 there is limited scope for strong potential competition as other CPs face significant barriers to entry and expansion as discussed above (see paragraphs 4.29 – 4.46);

3.122.3 the declining market size is likely to reinforce BT's market power as it creates a further barrier to entry – CPs have less incentive to enter the market if it is declining (see paragraphs 4.4 – 4.6); and

3.122.4 an absence countervailing buyer power (see paragraphs 4.72 – 4.73).

- 3.123 For these reasons, we consider that the market structure for the provision of SFV access will not tend towards effective competition in the review period (in the absence of regulation).

- 3.124 We note that, if we were to define separate markets for SFV access for voice-only and split purchase customers, we would reach a similar conclusion in each case (i.e. of neither tending towards effective competition in the review period), and in particular: (a) we estimate BT accounts for 66% of SFV access for voice-only customers and 97% of SFV access for split-purchase customers; (b) barriers to entry and expansion apply to both groups in a broadly similar way; (c) our understanding is that the number of customers in both groups is declining; and (d) neither group has countervailing buyer power.

- 3.125 We have also assessed competition in the SFV calls market as part of our SMP analysis in Section 5 and reached similar views. In particular:

3.125.1 despite the decline in the SFV calls market, BT has a high market share of [X]%. The next largest provider has a share of 5%-15% (see paragraphs 5.12-5.18);

3.125.2 there are barriers to entry and expansion, which are reinforced by the market decline for calls (see paragraphs 5.19-5.22);

3.125.3 although there is some substitution from fixed to mobile and VoIP by some types of users for some types of calls, the overall constraint imposed by such switching is limited (see paragraphs 5.31-5.35); and

- 3.125.4 an absence of countervailing buyer power (see paragraph 5.11).
- 3.126 For these reasons, we consider that the market structure for the provision of SFV calls will not tend towards effective competition in the review period.
- 3.127 Again, if we were to define separate markets for SFV calls for voice-only and split purchase customers, we would reach a similar conclusion in each case, of neither tending towards effective competition in the review period, for similar reasons to those set out in paragraph 3.124 above in relation to access.

### **Competition law alone would not adequately address the market failure(s)**

- 3.128 As set out in Section 6, we have concerns about the increasing direct and indirect harm that results from the lack of competition due to BT's SMP. We consider that competition law alone would not adequately address the market failures that we have identified for the following reasons:
- 3.128.1 *Ex ante* regulation allows for the imposition of specific and targeted SMP remedies to address the competition problems identified and for the ongoing monitoring of those remedies. This is particularly relevant in relation to the concerns we have identified in this review and the package of SMP remedies we consider appropriate (as discussed in later sections).
- 3.128.2 As set out in Section 4 and 5, we consider that one of the sources of SMP in this market is low consumer engagement. Part of the package of remedies we are proposing to impose is therefore designed to promote competition, rather than dealing with specific anti-competitive practices. These types of remedies would be difficult to introduce under a competition law analysis.
- 3.129 In the light of this, we cannot be confident that *ex post* competition law alone would be sufficient, particularly given the high barriers to entry and expansion and a market structure which does not tend towards effective competition.

### **Provisional conclusions**

- 3.130 In accordance the analysis set out above, we provisionally conclude that
- 3.130.1 There is a relevant product market for SFV residential access services in the UK (excluding Hull).
- 3.130.2 There is a relevant market for SFV residential calls service in the UK (excluding Hull).
- 3.130.3 Our proposed market definitions satisfy the three-criteria test set out in the 2014 EC Recommendation such that these markets are suitable for *ex ante* regulation.

### **Consultation questions**

*Question 3.1: Do you agree with our provisional conclusion that there is a separate market for Standalone Fixed Voice residential access which includes both voice-only and split purchase consumers? Please provide reasons and evidence in support of your views.*

*Question 3.2: Do you agree with our provisional conclusion that there is a separate market for Standalone Fixed Voice residential calls? Please provide reasons and evidence in support of your views.*

## Section 4

# Retail market power assessment: Access

## Introduction and summary

- 4.1 As set out in Section 3, we have identified a separate market for residential Standalone Fixed Voice (SFV) access.<sup>89</sup> This Section sets out our market power assessment for that market.
- 4.2 Our assessment follows the market analysis framework set out in Annex 7. We provisionally conclude that BT has SMP in this market, based on our analysis of market shares, barriers to entry and expansion, pricing, profitability and countervailing buyer power.

## Introduction to our assessment of competition in the residential SFV access market

- 4.3 We begin by setting out an overview of:
- 4.3.1 The evolution of the SFV market;
  - 4.3.2 Key characteristics of SFV customers; and
  - 4.3.3 Characteristics of SFV suppliers.

## Ongoing decline in SFV

- 4.4 As broadband take-up has grown (from 65% of households in 2009, to 79% in 2016<sup>90</sup>), there has been a general move from a focus on offering separate voice and broadband services to one in which these services are predominantly offered in a bundle, in some cases also including TV and/or (to a lesser extent to date) mobile in the same bundle. Now the large majority of consumers buy landlines in a bundle with other services.
- 4.5 The number of SFV access lines, i.e. bought outside a bundle, is in a steady long-term decline. This is primarily driven by customers who upgrade to bundled communication services (e.g. dual-play). In addition, since the customer base purchasing retail SFV access consists of a large number of older customers, this base has declined over time.
- 4.6 As set out in Annex 8, paragraphs A8.15-A8.17, the number of residential SFV lines is currently declining at a rate of around 15% per annum, and we estimate that by September 2016 it had fallen to 2.9 million, or around 11% of the 26.4 million residential lines in the UK (excluding Hull). This comprised about 1.7 million voice-

<sup>89</sup> As set out in Section 2 and 3, SFV access refers to the provision of standalone fixed voice access (i.e. line rentals) to residential consumers in the UK, excluding Hull. This includes three consumer groups; namely voice-only, split-service and split-supplier.

<sup>90</sup> Ofcom, *Technology Tracker*.

only customers, 0.9 million split-supplier customers and 0.2 million split-service customers.<sup>91</sup>

## Key features of SFV customers

- 4.7 SFV customers have, by definition, not adopted dual-play bundles in recent years. Our research indicates that these customers differ – on average – from the larger group of dual-play customers in a number of ways. Taken together, we consider that these differences present obstacles to SFV customers optimising their telecoms purchases and shopping around for the best deal:
- 4.7.1 **Demographics:** As noted SFV customers tend to be older, and may have a lower household income than dual-play customers.<sup>92</sup> This is particularly the case for voice-only customers, but our evidence is that split purchase customers are also older than average (See Annex 8, Figures A8.49 and A8.50).
- 4.7.2 **Experience of switching:** Around 70% of SFV<sup>93</sup> customers report that they have never switched provider. Many of these respondents are likely to have been with BT since it was the monopoly provider of fixed line services (see paragraph 4.39.1 below). In contrast, dual-play services are relatively new, and 26% have switched provider in the past 3 years.
- 4.7.3 **Online access to information on competing offers:** Among SFV customers, a substantial proportion of voice-only customers (as opposed to split purchase customers) do not have direct broadband access, although some have internet access via mobile phones and some may have access via family, libraries or internet cafés.
- 4.8 Survey evidence suggests that SFV customers have relatively low levels of engagement in the market. For example:
- 4.8.1 Around 70% of SFV customers report that they have never switched their landline provider, and only 14% report switching supplier within the past 3 years. These figures compare to 45% and 26% of dual-play<sup>94</sup> respondents, respectively.<sup>95</sup>
- 4.8.2 In our switching tracker survey only 9% of SFV customers are classified as engaged, compared to 20% of consumers purchasing bundles. Comparing

<sup>91</sup> These three segments do not sum to 2.9 million due to rounding.

<sup>92</sup> For SFV customers, 23% have a household income of less than £11,500 per annum, compared to 10% of dual-play (source: Ofcom Technology Tracker H2 2016). However, we note the non-response rates to questions around household income are high (48% for SFV and 37% for dual-play) and so these results should be interpreted with caution.

<sup>93</sup> As explained in Annex 8 Figure A8.46, in the context of survey evidence, SFV refers to voice-only customers and split-supplier customers (92% of all SFV lines).

<sup>94</sup> As explained in Annex 8, Figure A8.46, in the context of survey evidence, dual-play refers to respondents who take landline and broadband from the same CP. This includes an immaterial number of split-service customers, which does not affect our analysis of this group.

<sup>95</sup> These differences are statistically significant (at the 95% confidence level). Unless otherwise stated, all direct comparisons of survey evidence between customer groups in this section are statistically significant.

the customer segments, 6% of voice-only consumers and 15% of split-supplier<sup>96</sup> customers are classified as “engaged”.

- 4.8.3 SFV customers are particularly likely to cite trust in their current supplier as a reason not to switch (62%, compared to 46% of dual-play customers) (Figure A8.59 in Annex 8).<sup>97,98</sup>
- 4.9 Survey evidence also suggests that SFV access customers show a high level of satisfaction with their landline provider. Figure A8.62 in Annex 8 describes the reported levels of satisfaction with the overall landline service provided. It suggests that voice-only customers are generally more satisfied, the majority of voice-only and split-supplier customers reported being very satisfied (74% and 58% respectively, compared to 54% for dual-play).<sup>99</sup>
- 4.10 Further, many split purchase customers could make significant savings by bundling their fixed voice and fixed broadband services into a single package with the same (or a different) provider. On average a split purchaser buying SFV from BT<sup>100</sup> and standalone broadband from BT, Sky or TalkTalk could save £8 per month (more than 20%) by switching to an equivalent dual play service from their broadband provider at standard prices, and just over £14.50 per month (more than 35%) at promotional prices (see Annex 8 for more details).
- 4.11 In Annex 6, we discuss the elements of consumer engagement and our understanding of the underlying reasons for SFV customers being relatively disengaged, such as characteristics of the customers themselves, and their perception of barriers to switching.

## Market players

- 4.12 BT is the largest supplier of SFV lines and accounts for a large majority, with no other provider having a share above 5-15% (as we discuss below). Reflecting the different nature of competition in the SFV access market and in bundles, different types of market players are more prominent in each.
- 4.13 BT’s largest competitors in the SFV access market, such as Post Office and SSE, are not significant players in the market for bundled services.<sup>101</sup> Those who compete most strongly in providing bundled services have often invested in LLU and so try to leverage this to their advantage in providing a range of services. Providers such as Post Office do not have LLU assets, but may have advantages for the specific SFV access consumer such as brand recognition.

<sup>96</sup> As explained in Annex 8 Figure A8.46, when discussing survey evidence, we refer to split-supplier customers, who account for around 80% of split purchasers.

<sup>97</sup> As noted in paragraph A6.9 this high level of reported trust in the current provider could have a number of interpretations.

<sup>98</sup> The base is of those who have not switched or considered switching; not looking for a new provider; do not agree their landline provider is the best.

<sup>99</sup> The comparison between split supplier and dual-play is not statistically significant (at the 95% confidence level).

<sup>100</sup> The evidence (discussed in more detail in paragraph 4.22-4.23 and Annex 8 is that nearly all split purchasers buy SFV from BT, whereas they buy standalone broadband from a range of broadband suppliers.

<sup>101</sup> [3<].

4.14 On the other hand, the larger providers in bundled services are much less significant in SFV access. Sky, Virgin and TalkTalk all compete strongly in providing bundles. However, in the case of SFV services these operators are less active as shown by their low market shares (discussed in paragraphs 4.17-4.19 below) and the fact [3<] does not offer SFV services to new customers (as noted in paragraph 4.78).

## SMP assessment

4.15 Our approach to market power assessment is set out in Annex 7. In assessing SMP we base our analysis on a forward-looking evaluation of competition in the SFV access market, taking into account existing wholesale regulations (i.e. *ex ante* wholesale regulations arising from an SMP finding at the wholesale level).<sup>102</sup>

4.16 We assess SMP in SFV access using the following criteria:

- Market shares;
- Barriers to entry and expansion;
- Pricing;
- Profitability; and
- Countervailing buyer power.

## Market Shares

4.17 We set out in Figure 4.1 the market shares of the main suppliers of SFV services by number of lines purchased over the period 2013-2016.<sup>103</sup>

**Figure 4.1: Market shares of SFV lines by CP (in ranges)**

	BT	Post Office	SSE	TalkTalk	Virgin Media	Sky	Phone Co-op
<b>2013</b>	85%	5% - 15%	< 5%	< 5%	< 5%	< 1%	< 1%
<b>2014</b>	83%	5% - 15%	< 5%	< 5%	< 5%	< 1%	< 1%
<b>2015</b>	81%	5% - 15%	< 5%	< 5%	< 5%	< 1%	< 1%
<b>2016*</b>	79%	5% - 15%	< 5%	< 5%	< 5%	< 1%	< 1%

Source: S135 data response

\* Market shares for 2016 are averaged across January-September

4.18 BT has a very high market share of 79%, while the next largest provider has a share of 5-15%. BT's market share has remained at 79% or above throughout the period

<sup>102</sup> The wholesale regulation currently in place is set out in the 2013 Narrowband Market Review Statement (<https://www.ofcom.org.uk/consultations-and-statements/category-2/nmr-13>) and 2014 FAMR Statement (<https://www.ofcom.org.uk/phones-telecoms-and-internet/information-for-industry/telecoms-competition-regulation/narrowband-broadband-fixed/fixed-access-market-reviews-2014/statement>). Our proposed regulation for the next three-year market review period is set out in our 2016 NMR Consultation (<https://www.ofcom.org.uk/consultations-and-statements/category-1/narrowband-market-review>).

<sup>103</sup> Details of which CPs were included and excluded from this analysis is set out in Annex 8 and represent the providers of SFV services of which we are aware. We recognise that there may be some smaller providers that are not captured within these market share figures, however, we are not aware of any other CP with a significant SFV base that would affect the market share figures set out to any meaningful extent.



2013-2016. Whilst BT's market share has fallen by six percentage points and those of Post Office and SSE have increased by [x] percentage points respectively, (to [x]% and [x]% respectively), the fall in BT's market share is primarily due to BT customers leaving the market (through taking dual play or decline of overall customer base) at a faster rate than customers of other CPs, rather than being due to switching away from BT to other firms. As set out in Annex 8, acquisition of switching customers by these other CPs accounts for at most a small proportion of BT's customer losses. BT's share remains far higher than its nearest rival, and we expect this to remain the case over the review period, absent significant changes to the market.

- 4.19 BT's market shares (by number of lines and by revenue)<sup>104</sup> are consistent with a finding of dominance in the absence of other factors. As set out in the SMP Guidelines, very large market shares, in excess of 50%, are in themselves evidence of the existence of a dominant position, and therefore SMP.<sup>105</sup> Whilst this is not the sole basis on which a finding of SMP may be reached, it provides an indicator of the market power which BT may enjoy in the SFV access market.

### Analysis of market segments

- 4.20 As we set out at paragraph 4.6, there are different customer groups within the SFV access market – split-supplier customers, split-service customers and voice-only customers. While we include these customers within the same market, we have also considered BT's share of supply within each of these segments of the market.
- 4.21 For voice-only lines (about 1.7 million), BT has a share in excess of 60% (allowing for sensitivity checks as set out in Annex 8). Post Office, SSE, TalkTalk and Virgin Media have a share of 15% or below each. Sky and the Phone Co-op also have a small number of voice-only customers (less than 1% share).
- 4.22 In respect of split-supplier SFV access lines (about 0.9 million), BT has a share approaching 100% with less than 5% of such SFV access lines provided by other providers.
- 4.23 Similarly, for split-service customers (about 0.2 million), BT has a share approaching 100%, with the only other provider of SFV access lines to split-service customers being [x], with a share of less than 1% of these lines.<sup>106</sup>

<sup>104</sup> We set out an analysis of revenue market shares in Annex 8. As noted in Section 3, paragraph 3.25 we recognise that our revenue market shares for access includes some revenues which are attributable to calls (and our revenue market shares for calls do not include these revenues). However, this does not make a material difference to our analysis of market shares. (particularly as a similar effect will apply to BT and other CPs), or to our overall SMP findings.

<sup>105</sup> SMP Guidelines, paragraph 75.

<sup>106</sup> We included different estimates for the total numbers of voice-only and split purchase customers in the NMR Consultation, and this also implied different market shares for BT (although in all cases, BT's market share was above 50%). We set out in Annex 8 our approach to estimating the size of the different segments and supplier shares in each. In terms of total size of the different segments, we consider this data to be more reliable than that used in the NMR Consultation, as it is based on information provided by CPs (instead of survey evidence). With regard to the estimation of supplier shares of the different segments, we note that both the survey data and our estimates could potentially have different issues. For example, in our estimates we assume that there is an immaterial number of split-supplier customers who purchase neither SFV services or standalone fixed broadband services from BT. As noted in Annex 8 paragraph A8.39, we conducted sensitivity checks regarding

- 4.24 Further detail of shares in these market segments is set out in Annex 8 paragraphs A8.39-A8.43.

#### Comparison to overall residential fixed line provision

- 4.25 The number of residential lines in the UK has consistently increased since Q4 2009, from 23.4 million in Q4 2009 to 26.4 million in Q3 2016 (see Figure A8.2 in Annex 8).
- 4.26 BT, however, has seen a decrease in residential lines (from 13.3 million in Q4 2009 to 9.4 million in Q3 2016),<sup>107</sup> with its share falling from 57% in Q4 2009 to 36% in Q3 2016.<sup>108</sup> BT's share of all residential lines has fallen from 41% in Q1 2013 to 36% in Q3 2016.

#### Provisional view on market shares

- 4.27 BT has maintained a market share at or above 79% in SFV access. While its market share has declined to some extent in recent years, it is still by far the largest supplier in the market and is likely to remain so over the market review period. Its market shares remain well in excess of 50% within all segments of the market.
- 4.28 We now consider whether barriers to entry or expansion prevent others from challenging this high market share.

#### **Barriers to entry and expansion**

- 4.29 In principle, ease of entry, or expansion by rivals, can deter a company with high market share from raising prices above competitive levels. Barriers to entry or expansion can limit the competitive pressures faced by a CP with a high market share; whether from potential entrants or smaller CPs in the market.
- 4.30 We set out in this section the factors we have taken into account in assessing the extent to which there are barriers to entry and expansion in the SFV access market.

#### Low investment costs due to wholesale regulations

- 4.31 There are two ways to provide SFV access in the UK. A CP can either build its own network (i.e. self-supply) or provide the service over BT's network using regulated wholesale products.
- 4.32 To self-supply, a new entrant would incur significant costs to create an efficient telecommunications network. This is a high cost and risky means of entry, particularly as a large part of the investment would be sunk costs (i.e. cannot be recovered if the entrant decides to exit the market). In addition, telecommunications networks benefit from significant economies of scale, which means that average costs fall as output increases. Therefore, it is difficult for new, smaller firms to enter the market and be competitive as they will have a higher cost base compared to the incumbent CP. This

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the total number of split-supplier customers, and the proportion that take a SFV line from BT. Altering this assumption would affect BT's market shares within different segments, though under a range of sensitivities, BT's market share across segments remains high (> 60%). This is also the case for the Jigsaw survey data, although we place less weight upon this.

<sup>107</sup> Virgin Media has had a relatively stable number of residential lines (from 4.2 million in 2009 to 4.4 million in Q2 2016) (Source: Ofcom telecoms data updates).

<sup>108</sup> Shares of access revenues show a similar trend.

is particularly true for SFV, where the addressable base is declining (as discussed in paragraphs 4.4 - 4.6).

- 4.33 On the other hand, the use of wholesale inputs over BT's network provides a relatively easy route to entry as retailers do not have to incur any sunk costs in infrastructure. Wholesale products have been successfully developed and deployed and retailers no longer need to have their own access infrastructure.
- 4.34 CPs can rent lines by using Openreach's wholesale product; namely Wholesale Line Rental (WLR). This has enabled retailers to emerge over time. They can either buy WLR directly from Openreach or buy a "white label" access product from another CP.<sup>109</sup> We also observe that in the event that wholesale customers are not satisfied with the terms of the Openreach regulated WFAEL market wholesale line rental product, there are alternatives including seeking wholesale services from other network operators such as those that use local loop unbundling services.
- 4.35 Wholesale inputs, in particular WLR, are available to competing CPs as a result of regulation which has been in place for a number of years. BT has been required to provide WLR to competing providers since 2002<sup>110</sup> and we are proposing to retain a requirement on BT to offer WLR in our latest market review.<sup>111</sup> CPs would therefore continue to be able to benefit from the availability of regulated wholesale products to offer retail SFV access products to consumers.

#### Barriers to customer acquisition

- 4.36 However, whilst entry and expansion may be possible in principle through the use of wholesale inputs, the intensity of competition depends to a large extent on a CPs' ability in practice to win more retail customers and grow in the market. We have identified barriers to the acquisition of new customers in the SFV access market which may limit the ability of providers to compete effectively and expand in the market.

#### *Ability to reach customers*

- 4.37 CPs face barriers to effectively market their services to SFV customers for the following reasons:
- 4.37.1 The relatively small size of the SFV access market compared to the total number of households in the UK. A relatively small minority of UK households purchase SFV access services (around 3 million out of 26 million households).<sup>112</sup> Therefore, in order to run an efficient marketing campaign, a supplier would need to find a cost-effective way of identifying customers within the SFV access market.

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<sup>109</sup> By white label access product, we mean buying a wholesale product from another CP (who is buying WLR from Openreach) and rebranding it. It allows the CPs to offer a retail service at low risk and they can focus on other elements of either the service or their business.

<sup>110</sup> On 20 June 2002, the Director General of Telecommunications (the "DGT") published the statement entitled *Protecting consumers by promoting competition: Ofcom's conclusions* in which he modified BT's licence to, inter alia, require BT to provide WLR services and also set the charges for certain WLR services. The first basic WLR product (WLR1) was available from September 2002.

<sup>111</sup> See 2016 NMR Consultation, Figure 1.1.

<sup>112</sup> Our estimates of UK households with SFV services is shown in Annex 8 paragraph A8.15. For the number of UK households, see Ofcom, *CMR 2016*.

- 4.37.2 One of the common marketing channels – namely online marketing – is unlikely to be suitable for targeting these customers. A substantial proportion of SFV customers have limited internet access. While split purchasers have fixed broadband access at home, voice-only consumers – who represent almost 60% of the SFV access market – do not. Whilst some voice-only consumers may use the internet outside home (e.g. in libraries or internet cafés) and around 58% of voice-only consumers have mobile phones, there is limited evidence that internet marketing would be an effective way of reaching these customers.

*Ability to convince customers to switch suppliers*

- 4.38 CPs other than BT are also likely to face particular barriers in convincing SFV access customers to switch away from their current supplier.
- 4.39 Firstly, the evidence we have suggests that SFV access customers typically show low levels of engagement and low willingness to switch suppliers (see Annex 8 paragraphs A8.153-A8.176). Of those customers, BT’s customers appear to be even less engaged:
- 4.39.1 Before the introduction of competition, BT had a near monopoly on fixed voice access. Whilst some of its customers have switched away over time, those that have not may have never switched suppliers, and consequently may be particularly disengaged, whereas those that have switched to other CPs will have engaged with the switching process at least once (i.e. from BT);<sup>113</sup> and
- 4.39.2 Results from the 2016 Switching tracker and the 2015 Jigsaw survey indicate that BT’s SFV customers have lower switching rates and levels of engagement compared to non-BT customers. We set out the evidence in detail in Annex 8 paragraphs A8.153-A8.171 as above.
- 4.40 There may also be scope for BT to engage in targeted retention activities that limits other CPs’ ability to attract new customers.<sup>114</sup> A smaller provider of SFV services ([S&C]) noted this as a barrier to gaining market share, as discussed in paragraph 4.79.4. While this may be a relatively good outcome for the customer concerned, such retention activity further raises the costs to rivals of acquiring new customers, and hence the barriers to market expansion.
- 4.41 Third, evidence suggests that BT may enjoy a higher degree of brand loyalty compared to other CPs. The 2015 Jigsaw survey shows that a large proportion of BT consumers perceive their supplier as a more trusted brand. Respondents were asked about the reasons for choosing their current supplier. 30% of BT voice-only customers cited “Trusted brand” compared to only 6% for non-BT. In addition, 42% of BT voice-only customers cited ‘Always been my landline provider’ as the reason compared to 8% for non-BT. We currently have limited evidence on the underlying reasons for these survey results (although we intend to conduct further research).

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<sup>113</sup> [S&C].

<sup>114</sup> As we discuss below, BT has a Home Phone Saver tariff which is substantially cheaper than its Anytime tariff. Home Phone Saver is not prominently advertised (for example, it is not one of the three main tariffs on offer on BT’s website), but it can be used by BT selectively as a retention tool – i.e. offered to a customer who is considering switching.

- 4.42 Taken together, we consider that the factors identified result in particularly high acquisition costs for BT's rivals to win new SFV customers from BT. Those CPs face barriers in being able to target these customers effectively as well as difficulties in persuading them to switch away from BT as a result of low consumer engagement, BT's retention strategies and BT brand loyalty.

#### Declining market and competition for bundles

- 4.43 The fact that the SFV access market is declining over time is likely to be a further disincentive to a CP thinking of investing in marketing to expand its SFV access customer base. CPs' willingness to incur acquisition costs depends on the relative value of the acquired customer. The higher the expected value of the customer, the higher the willingness to compete. The nature of the SFV access base is likely to have a negative impact on a CP's willingness to invest for the following reasons:
- 4.43.1 There may be relatively limited scope for upselling additional services to SFV customers. This may particularly be the case for voice-only customers who may not have a need for broadband, although less relevant in the case of split purchase customers who could potentially be persuaded to switch to dual play.
- 4.43.2 As the SFV market shrinks, customer acquisition costs are likely to increase as remaining customers are likely to be even less engaged than those who ultimately choose to upgrade to dual-play and other bundled services.
- 4.43.3 The length of the supply relationship could be shortened by the age profile of SFV customers.

#### Provisional conclusion on barriers

- 4.44 Our analysis shows that potential competition from new entrants or expansion by existing CPs does not impose a strong constraint on BT.
- 4.45 The main barrier to entry and expansion is the ability of other CPs to reach customers and convince them to switch away from BT. SFV customers in general are relatively disengaged and unwilling to switch compared to other types of fixed voice customers. CPs other than BT face additional obstacles in that BT customers appear to be particularly loyal and less engaged than non-BT SFV customers.
- 4.46 In the absence of SMP remedies, we do not expect potential competition from other CPs to get significantly stronger over this market review period. If anything, it is more likely to be weaker as a result of the decline in the size of the market. As the addressable customer base declines, CPs will have a reduced incentive to incur the acquisition costs and compete for SFV access customers since the returns on investment available to them will be further reduced.

#### **Price Analysis**

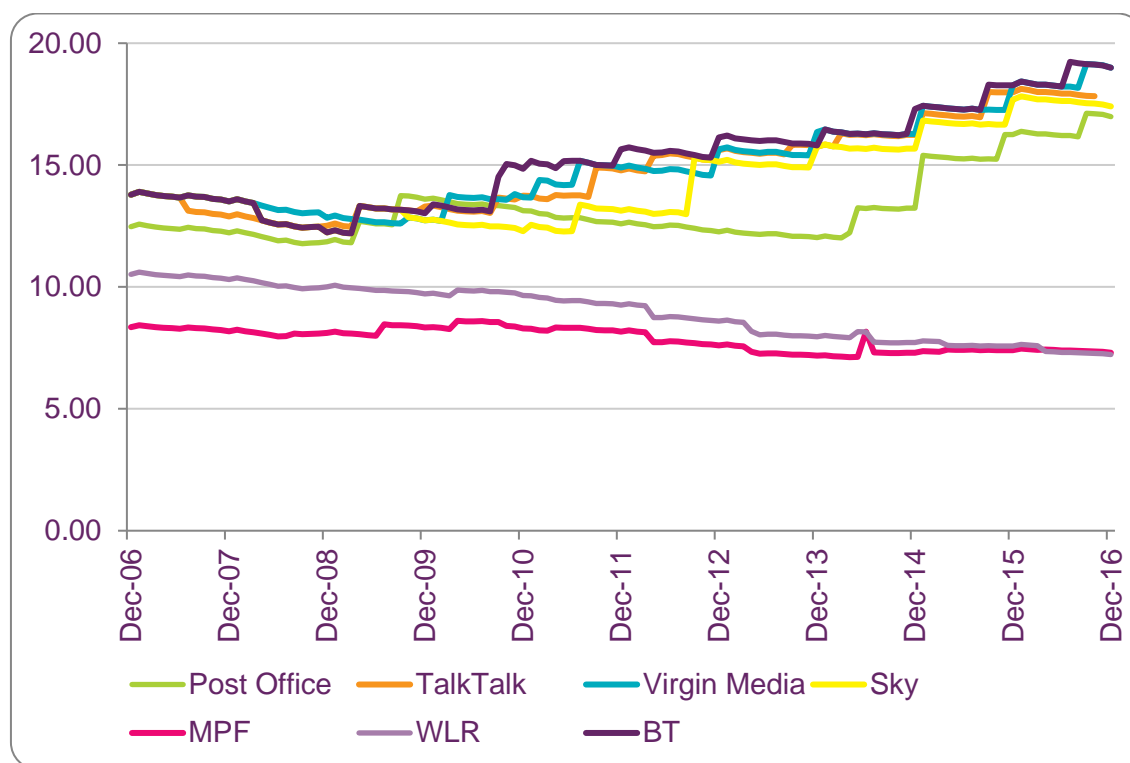
- 4.47 The ability to price persistently and significantly above the competitive level is an indicator of market power. In a competitive market, individual firms should not be able to persistently maintain prices above costs (including a normal return) and thus sustain excessive profits.

4.48 We first examine changes in the price of retail access i.e. line rental prices, and the evidence of other CPs following BT in changing these prices. We then consider whether these changes result from a rebalancing of revenues from calls to line rental, given changes in the usage of fixed calls. We also consider whether price changes may have been driven by changes in costs – either variable costs (such as WLR) or fixed costs. We then consider BT’s argument that it continues to add value for SFV customers, before considering the implications of price discrimination for our analysis.

### Line rental prices

4.49 We have examined residential line rental prices compared to (regulated) wholesale costs. Figure 4.2 shows the residential line rental prices charged by CPs from December 2006 to December 2016. This also shows the wholesale charges for MPF LLU and WLR. A CP generally needs one or other of these wholesale inputs to provide retail voice services to customers (if the CP does not have its own access network).<sup>115</sup>

**Figure 4.2: Wholesale and retail line rental price movements (£/month at December 2016 prices)<sup>116</sup>**



Source: PurePricing broadband updates

Notes: Adjusted for CPI; excludes line rental saver pre-payment tariffs

4.50 As can be seen, each CP has increased line rental prices a number of times over the period shown. For example, since December 2009 BT has increased prices 10 times over the seven-year period. The extent of BT’s increases to monthly prices has

<sup>115</sup> Most SFV services, particularly for voice-only customers, are provided using WLR (see 2016 NMR Consultation, paragraph 4.40).

<sup>116</sup> This chart is also shown in nominal terms in Figure A8.24 in Annex 8.

varied, from c.£0.30 up to £1.25 in nominal terms. More recently, starting in 2014, there is a pattern of annual price increases of £1 in the monthly line rental. As noted in paragraph 4.52 below and in Annex 8, these are generally followed both in timing and magnitude by other CPs.

- 4.51 BT's prices have generally been higher than those of other CPs. In 71 of the 85 months shown since December 2009, BT was either singly or jointly offering the most expensive line rental (although Virgin's line rental is currently £0.01 more expensive than BT). However, line rental prices offered by these suppliers have converged to some degree in recent years, having diverged after 2009, due mainly to significant increases in price by Sky and Post Office.<sup>117</sup>
- 4.52 The fact that prices appear to be converging as a result of price increases (rather than more expensive providers reducing their prices to match lower priced competitors) suggests that this is not the result of the market moving to a more competitive equilibrium. Figure A8.25 in Annex 8 maps the dates different CPs have announced price changes over the past 3 years (from April 2014 to January 2017) and shows a clear pattern of other CPs following BT in changing prices. In addition, the value of the price increase is typically the same across providers at approximately £1.00 per month.<sup>118,119</sup> [×].
- 4.53 Overall, on average line rental prices have increased by between 25% and 49% in real terms between December 2009 and December 2016. These price increases were highest for Virgin (49%) and BT (46%).
- 4.54 Figure 4.3, below, presents the access revenue per SFV line by operator (in real terms).

#### Figure 4.3: Access revenue per SFV line (£/month in December 2016 prices)

[×]

Source: s.135 responses

- 4.55 Access revenue per line has [×] between [×]% for [×] and [×]% for [×] in real terms between 2009/10 and 2015/16. Overall, however, [×] had the highest access revenue per line in the six financial years between 2010/11 and 2015/16.

#### Total revenue per line

- 4.56 While we have identified separate markets for access and calls, line rental is generally sold as a package including calls. As noted in Annex 8 paragraph A8.18, the number of calls made per fixed line has fallen by 55% between the year to Q3 2010 and the year to Q3 2016. While the reduction does not appear to be as significant for SFV customers, call volumes are also declining from SFV landlines. CPs could potentially be rebalancing their revenues to reflect this reduction in call usage.
- 4.57 If this were the case, we would expect to see combined revenues across calls and access remaining broadly flat over time. We have therefore looked at trends in

<sup>117</sup> We discuss this further in Annex 8 paragraph A8.57-A8.79.

<sup>118</sup> Sky did not increase their line rental price in 2016.

<sup>119</sup> TalkTalk did not actively offer SFV services in 2016 and, following the ASA ruling outlined in paragraph 2.3, stopped advertising a distinct line rental price in November 2016. For this reason, TalkTalk have been excluded from Figure A8.28.

access and call revenues per line over time to establish the extent to which a rebalancing has occurred which results in similar revenues across calls and access, taken together. This analysis is set out in Figure A8.39 of Annex 8.

- 4.58 This analysis covers all voice subscribers, not just those taking SFV. As set out in A5.34, BT does not hold revenue or cost data on its standalone fixed voice customers, instead it provided data for all of its fixed voice customers regardless of whether they also bought fixed broadband.<sup>120</sup> Other CPs also did not provide revenue data differentiated between SFV and other voice customers. While it is possible that there are differences in call usage between the groups, we do not have clear evidence on this point. We note that there appears to be only a relatively small difference in revenue per line between all voice customers and SFV customers. As set out in A5.43-A5.52, BT's revenue per line for SFV customers is £[redacted] compared to its average revenue per line across all voice customers in financial year 2015/16.<sup>121</sup> We therefore consider revenues across all voice customers are likely to be a reasonable proxy for the revenue per line earned from SFV customers.
- 4.59 Overall, the comparative levels of revenue per line for different CPs, and changes in this over time, suggest that [redacted]. Given that [redacted], we do not consider that it is likely that the increase in line rental can be attributed purely to a rebalancing of revenue between access and calls (even if this may be a contributing factor).

#### Changes in cost and added value services

- 4.60 Turning to costs, WLR charges have fallen by 26% in real terms between December 2009 and December 2016. This contributed to [redacted]. [redacted].<sup>122</sup> [redacted].
- 4.61 In addition, BT claims that it continues to add value for voice customers by including additional services in the package (e.g. including more call types in packages, and features to reduce nuisance calls) or improving service quality.<sup>123</sup> BT provided an estimate of the costs to it of various improvements it is making, such as moving all customers from Care Level 1 to Care Level 2 to shorten repair times, introducing new services including measures to allow consumers to avoid nuisance and scam calls, and investing in customer care (including answering more calls in UK call centres and improving the systems agents use). It estimated these would lead to an effective incremental monthly cost per line of £[redacted] (excluding VAT).<sup>124</sup> Therefore, this does not account for the size of BT's price increases or increased profit margin per line. [redacted].<sup>125</sup>
- 4.62 We recognise that, while WLR costs have gone down, [redacted], and there is some cost associated with new features. However, the net effect of the wholesale and retail cost

<sup>120</sup> We note that revenue per line for dual-play customers takes the nominal line rental included in a dual play bundle as the access element of revenue. We recognise this is to some degree artificial, and from the CP's perspective the overall revenue for the bundle is more important.

<sup>121</sup> This takes into account the adjustment to remove BT Basic customers and to account for SFV customers making slightly [redacted] volumes of calls than BT's other fixed voice customers (see Annex 5 paragraph A5.43-A5.50). Given that BT Basic was a [redacted] proportion of BT's customer base in the past, the difference between revenue per line for SFV customers and all voice customers was likely [redacted] in previous years.

<sup>122</sup> Details of how costs have been allocated for this analysis are set out in Annex 5. We do not have similarly granular data for other operators.

<sup>123</sup> BT presentation to Ofcom 17 November 2016 and 30 November 2016.

<sup>124</sup> [redacted].

<sup>125</sup> [redacted]. This is discussed further in Annex 8, paragraphs A8.69-A8.74.



changes is that [3<]. Cost changes do not therefore explain the price increases observed. With the combination of cost changes and price increases, the evidence suggests that the provision of SFV services is highly profitable, and profitability per line has been increasing.

### Effect of price discrimination and discounting

- 4.63 In 2009, we argued that an attempt by BT to raise prices might result in significant switching to alternative providers. We suggested that as those who were less active in the market did not belong to any clearly defined social, economic or demographic grouping, BT might have difficulty targeting these consumers through price discrimination. In addition, we argued that some consumers who were inactive but aware of competition might well respond if prices increased significantly. These arguments supported our conclusion in 2009 that BT did not have SMP in retail fixed voice services.
- 4.64 However, we now observe that the number of SFV customers is falling, and those who remain as SFV customers are less engaged (see paragraphs 4.38-4.42). This is likely due to more engaged customers having progressively moved to bundled tariffs, which generally offer price savings. As discussed in Section 2 paragraph 2.3, traditionally, BT and other CPs stated that they charged the same line rental price to customers taking dual-play bundles as those taking voice on a standalone basis. However, the price to those customers taking dual-play bundles was the sum of the line rental and incremental broadband price (and the stated split of this total between these two parts had no effect on the price they paid). Therefore, dual-play bundle customers generally benefited from competition over the incremental price for broadband (see Annex 8). This offset increases in line rental prices for such dual play customers. By contrast, those taking SFV services just experienced the rising line rental prices without offsetting benefits on other prices.
- 4.65 More recently, as set out in Section 2 paragraph 2.3, the ASA has ruled that from 31 October 2016 broadband suppliers' price claims must show all-inclusive, up-front and monthly costs.<sup>126</sup> This means that CPs must show in their advertising the price charged for line rental and incremental broadband as a single overall price. This has led providers to start moving away from separating dual-play prices into separate line rental and broadband charges. As a result, it is possible that there may be less pressure on CPs to increase line rental prices for SFV services to match increases in line rental prices for dual play tariffs.<sup>127</sup>
- 4.66 Further, within the SFV market, there is evidence of price discrimination between engaged and unengaged customers. BT offers various ways for customers to save relative to their base prices, such as calling plan coupons.<sup>128</sup> BT also highlighted that it offers a Home Phone Saver tariff, which it launched in 2014 "in response to competitive pressure from the Post Office and other providers".<sup>129</sup> The Home Phone Saver tariff is at least £5.50 lower than standard BT prices and significantly more if

<sup>126</sup> [https://www.asa.org.uk/News-resources/~media/Files/ASA/Reports/Ofcom%20Fixed%20BB%20Advertising%20of%20prices\\_Futuresight\\_Final%20Report\\_FINAL.ashx](https://www.asa.org.uk/News-resources/~media/Files/ASA/Reports/Ofcom%20Fixed%20BB%20Advertising%20of%20prices_Futuresight_Final%20Report_FINAL.ashx)

<sup>127</sup> This also means that BT has scope to exercise SMP in SFV access through line rental, while competing in dual play by varying the incremental broadband price. As a result, even if there continued superficially to be common pricing of line rental, a finding that BT has SMP in SFV access would not have any implication for its market position in relation to bundles.

<sup>128</sup> BT presentation to Ofcom 30 November 2016, slide 6.

<sup>129</sup> BT presentation to Ofcom 30 November 2016, slide 7.

various opt-in features are included. For example, BT has stated that the Home Phone Saver tariff offers a discount of £11 compared to standard prices.<sup>130</sup> A relatively small proportion of BT's SFV customers take the Home Phone Saver tariff. This implies that relatively few of BT's SFV customers are sufficiently engaged to have sought out a lower price offer which is available (although not prominently advertised). However, by offering such a tariff, BT can respond selectively to customers seeking to switch to an alternative provider without having to reduce standard prices, which would reduce the revenue it earns from less engaged customers.

### Provisional conclusion on price analysis

- 4.67 Our analysis of the evidence on prices suggests that prices are significantly above costs (both the relevant wholesale input prices and other elements of cost as discussed further in Annex 5), and have been diverging further over recent years. BT's prices also appear to be above those of other operators without this materially affecting its position in the market in terms of market share (as set out in paragraphs 4.17-4.19). There is evidence that BT acts as a price leader, with other CPs following its increases in line rental in terms of both timing and magnitude. Price discrimination to offer greater discounts to more engaged customers (for example, through its Home Phone Saver tariff) allows BT to increase prices for (largely unengaged) SFV customers whilst limiting the risk to the revenues it earns from more active customer groups.

### **Profitability**

- 4.68 Annex 5 set out our profitability analysis for BT as well as other CPs. Our analysis shows that BT's profitability (per line) from selling SFV services increased from 2007/08 to 2015/16. Over the period, we estimate that BT's net margins from SFV services increased from approximately £[<] to £[<] per line per year in real terms (in December 2016 prices). This equates to EBIT margins increasing from [<]% to 34-42%. (See Annex 5, paragraph A5.59 and Figure A5.8).
- 4.69 We consider that our views on BT profitability hold for access and calls separately. We have considered the extent to which BT's line rental and calls products drove its fixed voice profitability in paragraphs A5.63-A5.69. As shown in Figure A5.10, we estimate that BT's gross margins per line from line rental have increased, from approximately £[<] per line per year to approximately £[<] per line per year (in real terms, December 2016 prices). If we were to allocate a much greater proportion of BT's retail costs to either line rental or calls, [<].
- 4.70 We consider that the fact BT's profitability per fixed voice line has been high and increasing over time, [<], is consistent with BT facing limited competitive pressure in the provision of these services to SFV customers.
- 4.71 We have some evidence on the profitability of other CPs, although not from all CPs and at an aggregate level. Therefore, we have therefore treated the results of our analysis of the profitability of other CPs with caution. Our analysis suggests that some of these CPs are making reasonably high profits from their fixed voice consumers. Data from [<] indicate that these CPs earn a profit of £[<] to £[<] per year, or [<]% to [<]% EBIT margins.

<sup>130</sup> BT presentation to Ofcom 17 November 2016, slide 10.

## Countervailing buyer power

- 4.72 We have considered whether consumers possess countervailing buyer power in each of the access and calls markets. Countervailing buyer power is the degree of restraint that a purchaser is able to place on the seller by imposing an effective counter on any attempt by the seller to set its prices above the competitive level. It is more likely when a customer accounts for a large proportion of a supplier's total output, is well informed about the alternative sources of supply and is able to switch at little cost.
- 4.73 However, individual retail SFV customers make up a negligible proportion of BT's revenues and output such that it is difficult to see how BT could be constrained in its behaviour by customers threatening to switch, and individual consumers cannot reasonably sponsor entry by alternative suppliers to challenge BT's position. Nor have we seen evidence of groups of SFV customers operating in way that could exercise effective countervailing buyer power. We therefore do not consider that countervailing buyer power provides an effective restraint on BT's market power.

## CPs' views on customer acquisition

- 4.74 BT claims that the market is competitive. BT argues that it sees a high churn of voice only customers, with churn of [X]% in Q2 2016/17 (above that for fibre or pay TV). BT adds that [X]% of these line ceases are due to competitive losses.<sup>131</sup> As explained earlier (see paragraph 4.18), BT's customer churn largely reflects the declining market (as many consumers exit the SFV market by moving to dual play packages or for other reasons) and a relatively small proportion is due to switching to SFV services from other providers. BT itself notes that upgrade to dual play accounts for three of the four categories of consumer losses BT identified.<sup>132</sup> While some customer churn is likely to include customers moving from a BT SFV service to dual play from another operator, as set out in Section 3 paragraphs 3.30-3.43 we do not consider dual-play exercises a competitive price constraint on SFV services.
- 4.75 [X].<sup>133</sup> We do not have time series data for the provision of SFV service to voice-only customers, however, our data for total SFV services does not show that Post Office is growing its customer base (despite the increase over time in its market share). Between April 2015 and September 2016 the number of SFV lines for BT and Post Office both fell, albeit the percentage decline in BT's base was [X] ([X]% fall for BT and [X] % for Post Office).
- 4.76 In addition, the evidence on market shares (presented in paragraphs 4.17-4. 28) and the price analysis (discussed in paragraphs 4.47-4.67) do not support the existence of strong competition. Despite the declining market, the marketing efforts and lower prices offered by some other CPs, and decline in BT's market share, BT has maintained a high market share of 79% and above over the past four years. Moreover, despite BT claiming it faces competition, it has still been able to raise line rental prices well above inflation year on year (see Figure 4.2 and paragraphs 4.50-451) and increase its SFV profitability.

<sup>131</sup> BT presentation to Ofcom 30 November 2016, slide 4.

<sup>132</sup> BT notes that its losses from the segment include: customers consolidating voice and broadband with other providers; customers consolidating voice and broadband with BT; customers choosing another provider for voice services; and customers leaving to take voice and broadband elsewhere as their first entry into broadband. (BT presentation to Ofcom 30 November 2016, slide 4).

<sup>133</sup> BT presentation to Ofcom 30 November 2016, slide 4.

- 4.77 We spoke to some CPs about their marketing efforts and the costs of acquiring SFV access customers. Overall, the views expressed by other CPs are consistent with our view on the existence of barriers to customer acquisition, which in turn limit their ability and/or appetite to compete in the market.
- 4.78 First, some CPs – particularly larger ones – expressed no interest in marketing to SFV access customers, saying that the focus of competition, and of marketing budgets, was on multi-play. In particular:
- 4.78.1 [X] no longer offers SFV access services to new customers and mentioned that it has no appetite for re-entering the market. It considers that while margins now look quite high, the low likely numbers of switchers – due to consumer inertia – do not justify the costs/complexity of pursuing the business.<sup>134</sup>
- 4.78.2 [X] said that it does not market to SFV access customers because the market is small and declining, there is limited scope to upsell services such as broadband and TV to SFV customers and it is hard to convince customers to switch away from BT as this customer group shows strong loyalty to the BT brand and is typically older in age profile. [X] added that it prefers to compete for multi-play customers (particularly those purchasing pay TV services), who are higher value customers because they take more services.<sup>135</sup>
- 4.79 Other CPs expressed interest in winning more SFV customers, but noted high acquisition costs, and BT retention activity as barriers to reaching them:
- 4.79.1 Post Office mentioned that it has three acquisition channels for voice-only customers: online (20%), call centre (40%) and in-branch (40%). It described customers as inert and noted that despite regular contact in Post Office branches Post Office struggles to gain much traction. It considered that inertia seems to come from concerns about the switching process even though the potential savings from switching are significant for some customers. However, it said it had successfully reached some of BT's SFV customers by launching various marketing campaigns.<sup>136</sup>
- 4.79.2 Post Office has recently launched an introductory offer to incentivise BT's SFV customers to switch. The offer entails paying a 12-month contract at a price £14.99 a month instead of the full monthly price at £16.99. At the end of the contract, the consumer will pay the full monthly price. Post Office marketing material also shows that they try to alleviate customer's concerns about the switching process. For example, in the marketing material for the new offer, Post Office notes that the end user will keep the same phone line so no engineer will need to visit at home, keep the same phone number that everyone knows and there will be no break in service as the switch takes place.
- 4.79.3 [X] mentioned that active marketing to potential customers of voice-only products is difficult. It considers that identifying and reaching voice-only customers can be challenging, acquisition costs are high and trust is a very

<sup>134</sup> [X] email to Ofcom, November 2016.

<sup>135</sup> Notes of phone conversation with [X] on 15 November 2016.

<sup>136</sup> Notes of phone conversation with Post Office on 20 October 2016.

important factor for the customer in choosing the supplier. [X] added that voice-only customers are more likely to be vulnerable, and it exercises particular caution in conducting sales to vulnerable consumers, including a policy that stops the sales process if the agent thinks potential customers are not comprehending the discussion.<sup>137</sup>

- 4.79.4 [X] considers telemarketing to be the most cost effective way to reach SFV customers. It identifies two main barriers to gaining market share in voice-only. First, BT's retention strategy, by having a team to convince customers not to switch away from BT, makes it difficult to win customers, particularly older ones who are very loyal to BT. It told us that in some cases BT's SFV customers whom it has contacted will call BT to inform it that they are switching, and be persuaded to stay in the course of the phone conversation. Second, [X] is not listed on some of the price comparison websites as it finds the costs of some sites to be prohibitive - some sites have greatly increased the cost of acquiring voice-only customers (£70-120 per customer).<sup>138</sup>

### Provisional conclusions on market power

- 4.80 We provisionally conclude that BT has SMP in SFV access. This is based on the following evidence collectively:
- 4.80.1 Even taking into account the recent decline in its market share, BT had and continues to have a high market share of 79% and above over the last four years for which data is available and a share of at least 60% across all three customer segments (voice-only, split-supplier and split-service customers);
- 4.80.2 Other CPs face barriers in acquiring new customers and some of them are not interested in marketing to SFV customers. This is mainly due to high acquisition costs (e.g. due to low levels of consumer switching and engagement, BT brand loyalty and BT's ability to launch successful retention policies);
- 4.80.3 There is evidence that BT acts as a price leader i.e. it sets its prices largely independently of other CPs, while other CPs generally follow BT's price increases;
- 4.80.4 Our profitability assessment shows that BT's profitability is increasing over time on a per line basis. Our analysis shows that this is true for SFV services (i.e. access and calls combined) as well as for SFV access alone; and
- 4.80.5 Countervailing buyer power does not provide an effective restraint on BT's market power.

<sup>137</sup> Notes of phone conversation with [X] on 1 December 2016.

<sup>138</sup> Notes of phone conversation with [X] on 21 November 2016.

## Consultation questions

*Question 4.1: Do you agree with our provisional conclusion that, during the period covered by this market review, BT will have SMP in the standalone fixed voice access market? Please provide reasons and evidence in support of your views.*

## Section 5

# Retail market power assessment: Calls

## Introduction and summary

- 5.1 This Section sets out our market power assessment for the standalone fixed voice (SFV) calls market.<sup>139</sup>
- 5.2 We have provisionally concluded that BT has SMP in fixed calls and that other CPs do not. This view is informed by:
- evidence of BT's high market share;
  - evidence that BT's customers are less engaged and more loyal compared to customers of other CPs; and
  - our assessment of BT's profits from this market.

## Market Overview

- 5.3 We begin by setting out an overview of the conditions within the market for SFV calls, particularly as regards declining call volumes.

### Ongoing decline in fixed voice calls

- 5.4 Figure 5.1 shows voice calls per line for both all residential lines and SFV lines.

**Figure 5.1: Call volumes per line per quarter in the UK**



Source: Ofcom/operators and s.135 information requests

<sup>139</sup> As set out in Section 3, the relevant fixed calls market refers to standalone fixed voice calls sold to residential customers in the UK (excluding Hull).

- 5.5 The average volume of fixed line voice calls per line is declining across all residential lines. Calls from all residential lines fell from approximately 3.8 thousand minutes per line in the year up to Q3 2010 to approximately 2.6 thousand minutes per line in the year up to Q4 2013 and down to 1.7 thousand minutes per line in the year up to Q3 2016. This represented declines of 55% between Q3 2010 and Q3 2016 and 33% since Q4 2013 (see Figure A8.5 of Annex 8).
- 5.6 SFV customers make more calls than fixed voice customers generally – 2.3 thousand minutes per line in the year up to Q3 2016, compared to the overall average figure of 1.7. While they are making fewer calls than in the past, the rate of decline is slower than for fixed lines generally – an 9.3% fall since Q4 2013 compared to the overall average decline of 33%.
- 5.7 However, as noted in Section 4 paragraphs 4.4-4.6 and Annex 8, the number of SFV lines has decreased significantly and consequently, total call volumes from SFV lines have been falling faster than total calls from all residential lines – for example (50%<sup>140</sup> vs. 31%<sup>141</sup> between Q2 2013 and Q2 2016).
- 5.8 As we note in Section 3, paragraph 3.92, we have observed an increase in calls originated on mobiles at the same time as this marked decline in the volume of voice calls originated by consumers on fixed lines. The 2016 NMR Consultation shows calls from fixed lines fell approximately 42% between 2009 and 2015, while calls from mobile lines increased 13% in the same period.<sup>142</sup>

## Our SMP assessment

- 5.9 Our approach to the assessment of SMP is set out in Annex 7 and is the same as we have followed for the assessment of SMP in SFV access. We note in this regard that many of the features of the SFV calls market are common with the SFV access market.
- 5.10 We assess SMP in SFV calls using the following criteria:
- Market shares;
  - Barriers to entry and expansion;
  - Pricing; and
  - Profitability.
- 5.11 We set out in Section 4 (paragraphs 4.72-4.73) that countervailing buyer power is not likely to constrain SMP due to the nature of retail customers. This is equally true for calls as for access, and so we do not consider this issue further in this section.

<sup>140</sup> Total call volumes from SFV lines fell from 3.2 bn minutes in Q2 2013 to 1.6 bn minutes in Q2 2016.

<sup>141</sup> Total call volumes from all residential lines fell from 15.92 bn minutes in Q2 2013 to 10.93 bn minutes in Q2 2016.

<sup>142</sup> See 2016 NMR Consultation, Figure 1.1, [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0016/95011/Narrowband-Market-Review.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0016/95011/Narrowband-Market-Review.pdf).



## Market shares

5.12 We have examined the market shares of the main suppliers of standalone voice services over the period 2013-2016<sup>143</sup> (see Figure 5.2), based on shares of call minutes (volume).

### **Figure 5.2: Market shares of SFV call volumes by CPs (in ranges)**

[REDACTED]

Source: S135 information request

\* Market shares for 2016 are averaged across January – September.

5.13 Figure 5.2 shows that BT has a very high market share [REDACTED]%. [REDACTED]. The next largest provider has a share of 5-15%. As with the market for SFV access, BT's market share has fallen to some extent over this period, [REDACTED].

5.14 [REDACTED].

5.15 As set out in Annex 8,<sup>144</sup> we have also considered revenue market shares by using shares of non-access SFV revenue as a proxy for operators' shares of SFV call revenue.<sup>145</sup>

5.16 [REDACTED]. [REDACTED].

## Provisional conclusion on market shares

5.17 BT has a market share of SFV calls [REDACTED]. While its volume market share has [REDACTED] to some extent in recent years, it [REDACTED] and is likely to remain so over the market review period.

5.18 We now consider whether barriers to entry or expansion prevent others from challenging this high market share.

## **Barriers to entry and expansion**

5.19 As we noted in Section 3, paragraph 3.13-3.20 we analyse SFV access and SFV calls as separate markets because there is scope for a difference in competitive conditions between them due to factors such as the potential to substitute to mobile calls. However, this does not mean that the competitive interaction among providers of SFV services necessarily differs between their provision of access and calls. As calls are typically bought alongside access, if another CP wanted to compete for the call revenues generated by BT's SFV customers, it would have to do so by getting them to switch their landline (i.e. access) away from BT. CPs therefore face the same barriers to entry or expansion in calls as they do in access. As we set out in section, those barriers are largely driven by high customer acquisition costs resulting from:

<sup>143</sup> Details of which CPs were included and excluded from this analysis is set out in Annex 8.

<sup>144</sup> See paragraphs A8.50-A8.52.

<sup>145</sup> Some CPs, including BT, offer "free" weekend calls within the line rental price. As a result, some line rental revenue is attributable to calls. We do not have a basis for separating access and inclusive calls within line rental prices, so for reasons of practicality we treat line rental as the price of access. However, as noted in Section 3 paragraph 3.24 this does not make a material difference to our analysis of market shares (particularly as a similar effect will apply to BT and other CPs), or to our overall SMP findings.

- 5.19.1 The relatively small size of the residential SFV access market compared to the total number of households in the UK means that, in order to run an efficient marketing campaign, a supplier would need to find a cost-effective way of identifying customers within the SFV access market (see paragraph 4.37 in Section 4). Further, for the reasons set out in Section 4 paragraphs 4.37-4.42 CPs are likely to find it difficult to reach and attract these customers.
- 5.19.2 As set out above, the number of calls per landline is declining over time. This will tend to create an additional disincentive to expansion/customer acquisition, as it means that, other things equal, customers will tend to make fewer calls, further reducing the potential revenues associated with new customers.
- 5.20 As noted in Section 4, we spoke to some CPs about their marketing efforts and the costs of acquiring residential SFV access customers. Overall, the views expressed by other CPs are consistent with our view on the existence of barriers to customer acquisition, which in turn, limit their ability and/or appetite to compete in the market. We set out further detail on CP views in paragraphs Section 4 4.74-4.79. We consider these views are also likely to apply to SFV calls as well as access.

#### Provisional conclusion on barriers to entry and expansion

- 5.21 Our analysis shows that potential competition from new entrants or expansion by existing CPs does not impose a strong constraint on BT. These considerations are consistent with our findings in relation to SFV access (see paragraphs Section 4 paragraphs 4.44-4.46).
- 5.22 In the absence of SMP remedies, we do not expect competition from other CPs to get significantly stronger over this market review period. If anything, it is more likely to be weaker as call volumes decrease as described above.

#### **Price Analysis**

- 5.23 The assessment in this section applies to all fixed voice services and is not limited to SFV calls alone since standalone voice customers currently pay the same call prices (and can purchase the same call plans) as all fixed voice customers.<sup>146</sup> As we have indicated in Section 3 paragraphs 3.82-3.85, we do not, however, consider the market for SFV calls to include calls by purchasers of multi-play access.
- 5.24 Consumers can purchase some types of calls within a call plan, allowing them to make calls to particular numbers (e.g. international calls) at no additional cost beyond the price of the plan (or, in some cases, for a discounted per minute price). Calls outside of a call plan incur a set-up fee per call and a price per minute.
- 5.25 In Annex 8, we set out further data on call prices (see paragraphs A8.80-A8.106).<sup>147</sup> This data covers prices, volumes and revenues for all fixed voice customers (as we

<sup>146</sup> There is an exception to this rule in the case of BT's Home Phone Saver product which offers a SFV specific line rental and call plan package.

<sup>147</sup> The data we analyse in this document differs to that used in the 2016 NMR Consultation. In the NMR, we noted that retail call prices declined somewhat between 2010 and 2015 (see Figure 3.13, available at: [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0016/95011/Narrowband-Market-Review.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0016/95011/Narrowband-Market-Review.pdf)). This is based on a revenue per minute analysis for certain (out of plan) calls applied to a basket of calls. Our analysis uses revenue per minute for out-of-bundle calls, similar to NMR.

cannot conduct analysis on SFV revenues and calls specifically). That analysis shows the following:

- 5.25.1 **Out-of-plan call prices and revenues per minute:**<sup>148</sup> In paragraphs A8.97-A8.99 we set out call prices for a number of CPs, which show that BT's prices are more or less in line with other providers and the market average. However, [redacted].<sup>149</sup>
- 5.25.2 **Call plan prices:** In paragraphs A8.84-A8.96 in Annex 8 we set out an analysis of selected call plan prices for individual CPs. BT's price increases for these call plans have generally been among the highest of the CPs for which we have data. However, in many cases its prices are still below those of other CPs shown in the charts. There is also no clear pattern about the price changes by different CPs – the size of price changes has varied across CPs, and some CPs have not increased these prices at all. Overall, call plan prices have increased well above inflation, with 11% year-on-year increases for Evenings and Weekends and over 7% for Anytime between 2012 and 2016 (see paragraph A8.104).
- 5.25.3 **Non-access revenue:** As CPs may change the balance of what is offered within and outside call plans, we also analyse overall non-access revenues per minute as a proxy for all call prices in paragraphs A8.106-A8.108. BT had [redacted] non-access revenue per minute between the financial years 2013/14 and 2014/15, and had [redacted] in 2015/16. [redacted].<sup>150</sup> [redacted].
- 5.25.4 **Decline in volumes:** we noted in paragraphs 5.4-5.8 above that call volumes have been declining significantly in recent years. Call prices may be argued to have increased in response to this trend. However, as set out in Annex 5 Figure A5.10 and paragraph A5.65, [redacted].
- 5.25.5 **Changes in costs:** We have considered whether changes in prices are justified by changes in wholesale call or retail costs. Regulated wholesale cost of calls is more complicated to examine compared to wholesale access charges.<sup>151</sup> However, the overall trend in regulated wholesale costs has been downwards. As set out in paragraph A5.67, if we were to allocate a much greater proportion of BT's other (retail) costs particularly heavily to

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However, our data also includes 'other calls', such as directory enquiries, premium rate calls, Freephone calls, and all other call types. In addition, we also utilise evidence on retail tariffs available to consumers. The effective prices paid by consumers (captured by revenue per minute) may have reduced over time even in the face of increased retail tariffs if consumers have moved more of their calls into call plans (which generally represent better value).

<sup>148</sup> Out-of-plan revenues potentially represent a substantial proportion of revenues earned from calls. [redacted] (see Figure A5.5 in Annex 5).

<sup>149</sup> In Annex 8 paragraph A8.97 we also note that the average price of out-of-plan UK geographic calls increased 29% in real terms between 2012 and 2016 (an annual average increase of 6.5%). This is quite similar to the increase in the average price of set-up fees. However, prices of calls to mobiles have been largely steady in real terms.

<sup>150</sup> Figure 5.4 in Annex 5 also suggests that BT's revenue per line for calls (both call packages and out-of-bundle calls) has been [redacted].

<sup>151</sup> Calls will generally involve a wholesale call origination (WCO) charge and some form of termination fee. For calls to other geographic numbers, this will be the Wholesale Call Termination (WCT) charge. WCO and WCT charges have seen very different trends in recent years, as shown in Figure A8.41. In addition, different types of calls will attract different termination costs which have been declining at different rates.

calls, [X]. Therefore, changes in retail prices do not appear to have been related to changes in [X] costs.

### Provisional conclusion on pricing

- 5.26 It is difficult to draw any firm conclusions from the pricing evidence. Whilst BT's prices for call plans are typically lower than its competitors, its revenues for [X] tend to be higher than its competitors. We note, however, that BT's prices are [X] and the price increases are not obviously linked to changes in [X] costs. Nevertheless, on balance, we have not sought to draw any conclusions as to market power on the basis of the pricing evidence alone.
- 5.27 While call prices are generally the same for SFV customers as for other fixed customers, this does not mean that CPs could not set different call prices between SFV and non-SFV customers in future, as discussed in Section 3 paragraph 3.82-3.85.<sup>152</sup>

### **Profitability**

- 5.28 As discussed in more detail in Annex 5, we estimate that between 2007/08 and 2015/16, BT's net margins from SFV services [X] from approximately £[X] to £[X] per line per year in real terms (in December 2016 prices). This equates to EBIT margins increasing from [X]% to 34%-42%. (See Annex 5, paragraph A5.59 and Figure A5.8).
- 5.29 We considered the extent to which BT's line rental and calls products drove its fixed voice profitability in paragraphs A5.63-A5.69 in Annex 5. As shown in Figure A5.10, we estimate that BT's gross margins per line from calls [X], from approximately £[X] per line per year in 2007/08 to £[X] per line per year in 2015/16 (in real terms, December 2016 prices). If we were to allocate BT's retail costs particularly heavily to either line rental or calls, [X].
- 5.30 As set out in Section 4, paragraph 4.71 and Annex 5, paragraph A5.71, our analysis suggests that SFV customers are also profitable for some other CPs. We do not have sufficient data to estimate the profitability of other CPs with respect to calls separately from access.

### **Other constraints on SFV calls**

- 5.31 We set out in Section 3 paragraph 3.97 that there are other services, particularly mobile, which, while not close enough substitutes to be regarded as part of the same market as SFV calls, could provide an increasing constraint for calls – if not in access – which we take into account in our assessment of market power.
- 5.32 In particular, we noted in paragraph 3.94 that mobile appeared to be a relatively close substitute on a call-by-call basis with respect to some call types by certain groups (but a more limited substitute for others). Mobile call prices had fallen in relative terms and call volumes had increased, and this appeared to be at least a partial driver of the fall in fixed voice volumes. In addition, in the 2016 NMR Consultation, we stated that mobile calls and other services outside the WCO market

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<sup>152</sup> There are examples of such discrimination today – BT's Home Phone Saver product is only available to SFV customers and includes a unique calls offering.

are a greater constraint than at the time of the last NMR. We also noted mobile in particular exerts a relatively stronger constraint for WCO than WFAEL.<sup>153</sup>

- 5.33 However, we note in Section 3 that balancing various factors we considered in the 2016 NMR that mobile calls are not a sufficient indirect constraint on fixed calls to be included in the relevant product market (at the wholesale level). Much of our assessment in the NMR consultation related to fixed calls generally, rather than SFV calls in particular. However, we consider that the considerations supporting our position in NMR also apply in the case of SFV customers, noting that SFV customers are less likely than fixed voice customers generally to have mobile phones, and that in the survey evidence discussed above they appear to be less price-responsive than fixed voice customers generally.
- 5.34 VoIP could also potentially provide an additional constraint on calls from fixed lines. At Section 3 we note it appears that a minority of SFV customers use VoIP and fewer use it frequently. Even consumers who use VoIP frequently mainly use VoIP calls for a limited range of call types (in particular international calls and calls to other VoIP users). In addition, in the 2016 NMR we proposed that, for similar reasons as described here, we do not consider switching to VoIP is a sufficiently strong constraint to prevent SMP in the WCO market in the review period.<sup>154</sup>
- 5.35 Therefore, whilst constraints from mobile and VoIP are relatively stronger for SFV calls than for SFV access, we do not consider that they are likely to provide an effective restraint on BT's market power during the market review period.

## Provisional conclusions on market power

- 5.36 We provisionally conclude that BT has SMP in residential SFV calls. This is based on the following evidence:
- 5.36.1 BT had a high market share of [ $\approx$ ] % or [ $\approx$ ] over the last four years for which data is available;
- 5.36.2 As for SFV access, other CPs face barriers in acquiring new customers and some of them are not interested in marketing to SFV customers. This is mainly due to high acquisition costs (e.g. due to low levels of consumer engagement and BT brand loyalty);
- 5.36.3 The profitability assessment shows that BT's gross margin per line for calls is increasing over time. Our analysis shows that BT's gross and net margins are also increasing for SFV services on a per line basis (i.e. access and calls combined).

## Consultation questions

*Question 5.1: Do you agree with our provisional conclusion that, during the period covered by this market review, BT will have SMP in the SFV calls market? Please provide reasons and evidence in support of your views.*

<sup>153</sup> 2016 NMR, paragraph 6.67.

<sup>154</sup> 2016 NMR, paragraph 6.57.

## Section 6

# Addressing consumer detriment

## Introduction

- 6.1 In Sections 4 and 5 we set out our provisional assessment that BT has SMP in the markets for SFV access and SFV calls. In this section:
- 6.1.1 We set out our view of the consumer detriment which results from BT's SMP;
  - 6.1.2 We explain why we do not consider that wholesale remedies have been effective in addressing this consumer detriment; and
  - 6.1.3 We describe ways in which consumer detriment in these markets might be addressed.

## Our assessment of consumer detriment

- 6.2 We have provisionally concluded that BT has SMP in the markets for SFV access and SFV calls. In our view, the lack of competition in those markets which is a result of BT's SMP, has resulted in two types of consumer detriment: direct effects and indirect effects.

### Direct effects

- 6.3 We have considered the extent to which BT's standalone voice prices are above the competitive level.
- 6.4 Our assessment of BT's profitability, set out in Section 8 and Annex 5, shows that BT is making profits in SFV markets which are [redacted] and the profit margins identified using competitive benchmarks. BT's prices are approximately £8-£10 per line per month above the level of its costs and £5-7 per line above a level indicated using competitive benchmarks.
- 6.5 Based on our estimate of around 2.9 million SFV lines in the UK (excluding BT Basic)<sup>155</sup> the overall current<sup>156</sup> consumer detriment is therefore of the order of £150 to £340 million per annum, depending on the choice of benchmark price (see Annex 5 for further details).
- 6.6 As set out in Annex 8, we also consider that in recent years there is evidence that BT has acted as a price leader in the market, in that when it has increased prices other providers have followed with similar price increases. The result is that SFV customers in the market generally pay prices significantly above costs due to BT's SMP.

<sup>155</sup> Annex 8, paragraph A8.15.

<sup>156</sup> Estimates of future consumer detriment would need to take into account that the base of SFV customers is declining over time and the potential for the detriment per line to change.

## Indirect effects

- 6.7 Competition can deliver a number of consumer benefits such as lower prices, more choice, better quality, and innovation. Competition in the provision of SFV services could, for example, deliver benefits in the form of product differentiation by reference to service features (e.g. reliability of the connection), customer and add-on services. Consumers could also benefit from competition in the provision of different call packages and inclusive call allowances. As a result of the lack of competition in the market, reflected in BT's SMP, consumers are deprived of the benefits that such competition would bring.

## Wholesale regulation

- 6.8 As set out in Section 2, before imposing regulation at the retail level, we are required to demonstrate that we are unable to perform, or to fully perform, our duties through the imposition of wholesale regulation.
- 6.9 The wholesale inputs required for the provision of SFV services, in particular WLR, have been subject to wholesale regulation, on a continuing basis, since Ofcom's last review of the retail fixed line markets in 2009. Wholesale regulation of these services has included an obligation to provide access, as well as different forms of pricing regulation. In our 2016 NMR Consultation we proposed retaining some form of wholesale regulation for these products.
- 6.10 However, as set out in Sections 4 and 5, BT continues to enjoy SMP in SFV markets, despite the presence of wholesale regulation. As also set out in Section 4, increases in retail line rental prices have occurred despite decreasing wholesale prices. Specifically, while the charges for key wholesale inputs to these services have fallen by up to 26% in real terms, retail line rental prices have risen by between 25% and 49% since 2010.
- 6.11 In addition, some of the concerns that we have identified are not addressable through measures at the wholesale level as they relate only to the conditions for competition at the retail level. This is particularly the case with some of the barriers to entry and expansion that we have identified in our SMP analysis, relating to the disengaged nature of the SFV customer base.<sup>157</sup>
- 6.12 In our view, it is therefore clear that wholesale regulation has not been, and will not be, sufficient to address the consumer detriment that we have identified in relation to SFV services. Accordingly, we do not consider that wholesale regulation would enable us to perform our duties, particularly our duty to promote competition, including by ensuring that users derive the maximum benefit in terms of choice, price and quality.

## Retail regulation

- 6.13 As a result of the SMP which we identified in section 4 and 5, BT has been able to raise retail prices to its standalone landline telephone customers despite falling costs. This has directly negatively impacted on current SFV customers who face higher prices than they otherwise would in a competitive market.

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<sup>157</sup> Section 4, paragraphs 4.38 – 4.42.

- 6.14 We are therefore of the view that it is appropriate to take measures to directly address the consumer detriment which has arisen through the imposition of a price cut. We also consider that, in addition to a price cut, it is appropriate to take action to try to increase competition for those consumers. This should result in better consumer outcomes, if it is successful. We are therefore proposing a combination of retail price controls and measures to change consumer behaviour to promote competition.
- 6.15 We set out our assessment of the options and the interrelationship between the remedies in the following Sections 7, 8 and 9. In summary our proposed approach (confirmed in Section 9) takes the following form.

### **Retail price control**

- 6.16 We are proposing to impose a price control on BT covering both line rental and calls as well as ancillary services for standalone landline telephone services.
- 6.17 This control – a price cut on the standard line rental of between £5-7 per month – will immediately reduce the gap between wholesale costs and retail prices we have seen emerge over the last few years. Thereafter BT will only be allowed to increase its charges for line rental and calls in line with inflation.
- 6.18 The price cut will apply to all BT customers using standalone landline telephone contracts (whether or not they buy fixed broadband from BT or other telephone companies outside of a bundle). It does not apply to landline services sold by BT as part of a bundle of services which include broadband or other non-voice services, as we consider competition in this market is delivering good outcomes for consumers.
- 6.19 The effect of the price cut will be to largely reverse the price increases since 2009. We recognise that the price cut may not reduce prices to the level BT might charge in a fully competitive market, however, we consider that it is appropriate to leave some room for competitors, who necessarily have higher customer acquisition costs, to re-enter the market and profitably compete for BT's customers. If we see no prospect of this arising, we may consider it necessary to go further in the level of the price control.

### **Promoting competition**

- 6.20 Competition has the potential to deliver benefits for consumers in terms of price and choice. However, in order for the benefits of competition to emerge, consumers must be sufficiently engaged to make well-informed decisions about switching to get a better deal. For this to happen, we believe that consumers need to have access to helpful, easy to understand information so that they can make more informed choices.
- 6.21 We are therefore proposing to require BT to work with us to trial – and, if appropriate, ultimately deliver – consumer information which will encourage its standalone landline customers to look for better value deals. We propose to trial and implement various ways of providing consumer information which will help customers understand what they are buying and what alternatives they have to get better value for money.
- 6.22 Our aim in imposing these measures is to allow other providers to compete more vigorously in this market and to win customers. If the engagement remedies we are



proposing are effective, we would expect consumers to benefit in terms of price and choice.

## Remaining Sections

- 6.23 In Section 7, we set out our view of the options for promoting competition, including: some details of how measures might be designed to work in the SFV markets, which of these measures are most likely to be effective in the market, and how we would propose to design a potential remedy involving those types of measures.
- 6.24 In Section 8, we set out the potential options for a price control remedy.
- 6.25 While clearly the two categories of remedy are not mutually exclusive, there are potential trade-offs and challenges in progressing with both of them at the same time. In Section 9 we consider these trade-offs, set out the potential range of options for an overall package of remedies, and present our argument for our preferred package of remedies noted above.

## Section 7

# Options to promote competition

## Introduction and summary

- 7.1 This section sets out our assessment of remedies to promote competition. In particular:
- 7.1.1 We discuss the potential role that remedies could play to promote competition, focussing on remedies to increase engagement. We summarise current survey evidence and our intention to carry out further research.
  - 7.1.2 We identify several options for engagement remedies which could promote competition. We discuss two broad categories of engagement remedies. Firstly, information remedies, that provide information to consumers to make it easier for them to engage in the market. Secondly, remedies that lead directly to a change in outcomes for a substantial number of consumers, unless they opt out of them.
  - 7.1.3 We set out the challenges to these engagement remedies being effective and/or appropriate and our initial assessment of each remedy.
  - 7.1.4 Given the uncertainty around effectiveness and optimal design, we discuss the need to trial and test remedies to gather more evidence before making any future decision on whether to impose specific remedies.
  - 7.1.5 In the light of this analysis, we identify that a set of information remedies may be appropriate for further research, development and trialling. We do not propose to take forward more intrusive remedies seeking to directly change outcomes. These carry risks of unintended consequences through potentially overriding consumer choice. They also raise design challenges in ensuring consumer privacy.
  - 7.1.6 We then discuss our initial view of how the trialling process would work, and why we require BT's cooperation in this process.
- 7.2 In Section 9 we consider engagement remedies and price controls together, and set out our proposals on the package of remedies to address the detriment discussed in Section 6. The analysis in Section 9 acknowledges the potential conflict between a price control and the encouragement of competition.

## The potential role of engagement remedies in promoting competition

- 7.3 In Sections 4 and 5, we described the barriers to entry and expansion faced by providers of standalone voice services. One of the key issues we have identified is barriers to the acquisition of new customers, which limit the ability of other communications providers (CPs) to compete effectively and expand in the market (see paragraphs 4.38-4.42).

- 7.4 CPs – particularly non BT CPs – face barriers in convincing SFV customers to switch away from their current supplier. A major factor driving this is the low level of consumer engagement in this market. Our assessment of SMP identified low willingness to switch and low actual switching rates. This is particularly the case for voice-only customers, but is also true for split purchasers. As set out in Annex 8:
- 7.4.1 Our survey evidence<sup>158</sup> indicates that only 3% of SFV customers report having switched in the last year and only 30% report ever switching. This contrasts with 12% of bundle customers who have switched their landline provider in the last 12 months.<sup>159</sup> Survey results also suggest that engagement is lower for BT's customers, as only 16% report ever switching, compared to 64% of non-BT customers. We note that some customers may engage without switching provider, such as by changing their call plan, and this may not be captured in our survey data.
- 7.4.2 In our switching tracker survey, only 9% of SFV customers are classified as “engaged”, as compared with 20% of bundle customers.
- 7.5 Some smaller players in the market offer substantially lower SFV prices than BT, but have struggled to gain market share. Historically, for example, Post Office had lower prices but this did not lead to a significant level of switching, or to BT reducing its headline prices (rather it has increased them, as has Post Office). Many split purchasers could (but do not) make significant savings by bundling their fixed voice and fixed broadband services into a single package with the same (or a different) provider.
- 7.6 Annex 6 sets out our views on barriers to consumer engagement. In summary, using the UK Regulators Network (UKRN)'s<sup>160</sup> framework we have identified several potential key barriers which may hinder consumer engagement for standalone voice customers.
- 7.6.1 **Perceptions of low potential gains** from switching or costs of the switching process may deter consumers from beginning the process of engaging in these markets.
- 7.6.2 Consumers may have concerns about the reliability of alternative providers: remaining with a **trusted provider** is by far the biggest reason given by these customers for not being interested in changing landline provider.<sup>161</sup>
- 7.6.3 Consumers in these markets receive **few triggers** to engage. In particular, there is little marketing of SFV services, and consumers are typically outside a minimum contract period (and so would not be prompted by the end of an initial term).
- 7.6.4 **Accessing information** on competing offers in the market may also be difficult for these consumers, given this lack of marketing. Further, our

<sup>158</sup> Ofcom switching tracker 2016 – see Annex 8, paragraph A8.149.

<sup>159</sup> This difference is statistically significant (at the 95% confidence level). Unless otherwise stated, all direct comparisons of survey evidence between customer groups in this section have differences that are statistically significant.

<sup>160</sup> The UK Regulators Network is a member organisation formed of 13 of the UK's sectoral regulators (<http://www.ukrn.org.uk/>).

<sup>161</sup> Ofcom switching tracker 2016 – see Annex 8, Figure A8.59.

research suggests many of these consumers do not have access to the internet.<sup>162</sup>

- 7.7 We discuss below a range of remedies which could address these barriers to consumer engagement. This would consequently act to promote competition by reducing acquisition costs and so barriers to entry and expansion. We are planning further consumer research to gather more detail on the nature of the lack of consumer engagement, and inform our further consideration of remedies ahead of our statement on this market review.
- 7.8 A relatively small minority of UK households purchase SFV services (around 3 million out of 26 million households).<sup>163</sup> Therefore, in order to run an efficient marketing campaign, a supplier would need to find a cost-effective way of identifying customers within the SFV market. A campaign without targeting would have high costs per customer acquired.
- 7.9 This could potentially be addressed by remedies that make changes to the customer acquisition process, directly reducing these costs. We also discuss these potential remedies below.
- 7.10 There are other factors on the supply side that would not be addressed through engagement remedies, however, and may impact on their effectiveness. The number of SFV lines is in a steady long-term decline (at a rate of around 15% per annum). This would likely include some customers who upgrade to bundled communication services (e.g. dual-play). In addition, some customers cease to have a phone line. As the market declines CPs may have a lower incentive to incur acquisition costs and compete for SFV customers.
- 7.11 Some CPs with strong brands ([&lt;], TalkTalk and Virgin) have told us that they are focused on multi-play offers and so do not devote significant resources to the standalone voice markets. On the other hand, some players with known brands, including Post Office, have told us that they are interested in growing their standalone voice customer bases.

#### Other actions could address barriers to engagement

- 7.12 We also note that there are a number of other actions being taken by Ofcom that could also contribute to addressing barriers to consumer engagement in these markets. A key area of focus in our Strategic Review of Digital Communications (DCR) is consumer empowerment, so that people can understand the array of choices available to them and are able to switch to the best value deal easily. To ensure this, we are taking a variety of actions, including publishing more information on service quality.
- 7.13 In April we will be publishing our first annual service quality report. The report will contain a range of comparative network and customer service quality measures that will aid consumer awareness of different levels of service quality. This would encourage them to choose a provider which best meets their needs and enhance the

<sup>162</sup> By definition, the 60% of SFV customers who are voice-only do not have internet access at home. See paragraph 4.7.3.

<sup>163</sup> Our estimates of UK households with SFV services is shown in Annex 8. For the number of UK households, see Ofcom, *CMR 2016*.

ability of firms to compete on the basis of their service quality. This may be relevant in relation to consumer preferences for a trusted provider.

## There are a range of potential remedies designed to address low levels of engagement

7.14 We have identified six broad areas that we think could potentially form the basis of a regulatory obligation on BT to improve engagement in this market. These are:

- Provision of information on **savings available** to consumers, to address factors that may prevent consumers from accessing and assessing the information they need to engage in the market.
- Information on the **switching process**, to address perceptions that may be preventing consumers from acting to get the best deal for them.
- Creating a **decision point** at which consumers would be prompted to make an active decision on their landline service.
- Increasing the ease of acting, to **reduce transaction costs** for consumers and increase the likelihood that they will act on information they receive.
- **Automatic switching** within BT tariffs that removes the need for consumers to habitually engage in the market, and ensures they are switched to the anticipated best BT tariff for their circumstances.
- Disclosure of **information on BT's inactive voice-only customers to (potential) competitors or third parties**, to reduce acquisition costs for those seeking to win these customers from BT, and so increase supplier engagement in the market.

7.15 We discuss each of these broad options and some detailed design considerations in turn below. For each we first describe the type of remedy and how it might address barriers to engagement. We then discuss some questions of detailed remedy design. Thereafter we provide our initial views on the potential benefits and the risks (such as failing to achieve the desired objective or unintended consequences). We discuss the potential relative costs of different remedies, but have not at this stage attempted to estimate in detail the costs involved in implementing any of these remedies. We conclude this section by summarising the types of remedy which we consider offer the most potential in terms of proportionate measures to promote competition.

### Information on savings available

#### Description of remedy

7.16 Under this remedy, we would require BT to provide information to its standalone voice customers on potential savings they could make. A simple approach would be to provide information on savings available by changing to a cheaper tariff within BT (and this could include information on BT Basic, including eligibility criteria). A more complex approach would be to provide information on savings available from switching to another provider. This could also include information on dual-play offers.

7.17 This information provided could include a summary of previous usage, to facilitate comparison. As discussed in Annex 6, we do not think an awareness and

understanding of usage is likely to be a hugely important factor for decisions made by many consumers in this market. However, where this information can be provided it may still provide incremental benefits.

- 7.18 Such communications could include references to accredited price comparison websites. We recognise that a proportion of voice-only customers do not use the internet, but price comparison websites may be of use to those who do (including split purchasers). Even for those who do not use the internet, it is possible that family and friends who do have internet access could assist them.
- 7.19 We envisage that this information could take the form of a letter or other communication from BT, or be incorporated into existing communications (such as being part of a consumer's regular bill), or both.

### Remedy design

- 7.20 Content, format and timing are all important to the effectiveness of information. There are a range of aspects that would need to be considered as part of detailed remedy design:
- Personalising the information, such as providing information on the specific savings that a consumer could make given their usual usage (i.e. volume, timing and destination of calls), or using a comparison based on a typical customer. A personalised comparison may be more challenging as it would require BT to make individual assessments for each consumer. If a consumer's usage pattern changes, then this comparison may no longer be relevant.
  - The way a potential saving is quantified (i.e. in absolute or percentage terms) and the time period over which this is presented (i.e. monthly or annual).
  - The way in which potential choices are framed – including whether they are presented as savings that could be made or losses that consumers are incurring through not switching.
  - Whether the basis of comparison is with alternative tariffs from BT or a comparison with the best available tariff in the market. Including whole-of-market comparisons would be a more significant intervention (and may require more effort from BT in assessing and describing potential savings, and ensuring that comparisons reflect currently available tariffs<sup>164</sup>), but is more likely to be effective, as many BT customers may already be on the most suitable tariff that is available to them from BT. Whole-of-market comparisons could also promote competition by giving other CPs an incentive to reduce prices, so as to be identified as the comparator tariff in BT customer communications.
  - Whether the letter is sent from BT or Ofcom (or jointly), and who within the organisation signs the letter. For example, in some cases a letter from an incumbent that includes information about its competitors could have the unintended effect of reinforcing consumers' perceptions of the incumbent as a trusted supplier and potentially dampening switching.

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<sup>164</sup> We envisage this would also require us to agree a methodology for whole-of-market comparisons, to ensure they are carried out on an appropriate basis.

- How information on usage, price comparison websites or BT Basic is explained and framed.

### Initial assessment

- 7.21 **Effectiveness:** The effectiveness of this remedy in promoting competition is likely to be dependent on the existence of material gains from switching provider or tariff. While our analysis suggests that gains from switching at present may be relatively modest for many voice-only customers (of the order £2/month in relation to non-promotional products), improved consumer engagement could potentially give other providers an incentive to offer more competitive tariffs. In the case of split purchasers, there may be potential for a targeted information campaign to highlight to them that they could be paying materially less for an equivalent set of services under a dual-play package.
- 7.22 However, even with the availability of attractive alternative offers, there is a considerable risk that an information remedy of this kind would have limited effectiveness, either by itself or in combination with other engagement remedies we consider below. A recent report by Professor Amelia Fletcher for Which? (“the Which? Report”) comments that:
- “...even where remedies are designed and implemented as well as they can be, the difficulty inherent in trying to change real consumer behaviour means they may still be only partially effective. It may simply be impossible to ensure that consumers fully take in, digest, and act upon the relevant information in a way that significantly improves their decision-making.”<sup>165</sup>
- 7.23 While noting some cases of successful information remedies, the Which? Report sets out a number of examples of information remedies which have been introduced in different markets, but have had a limited impact on consumer decision-making, in relation to: energy tariffs, care homes, unarranged overdraft charges, cash ISAs, credit card fees, and mutual funds.<sup>166</sup>
- 7.24 There is a risk that some types of SFV customers would be particularly difficult to engage through an information remedy. Some older or vulnerable voice-only customers may not be receptive to information about their phone service, or may not be confident in acting on such information. While split purchasers tend to be more connected than voice-only customers, the fact that the remaining split purchasers have not responded to date to widely-advertised dual-play offers suggests that they might not be responsive even to a more targeted information remedy.
- 7.25 **Costs:** Dependent on the nature of the changes to information provided, this is likely to be a relatively low cost remedy to implement, compared to other options discussed below, if it involves information on savings available from changing tariff with BT. BT already regularly communicates with its customer base. This remedy would most likely involve mandating changes to the content of communications sent out by BT. This means it would impose limited additional costs over and above those BT already incurs in communicating with its customers.

<sup>165</sup> *The Role of Demand-Side Remedies in Driving Effective Competition A Review for Which?* Amelia Fletcher, Centre for Competition Policy, University of East Anglia, 7th November 2016.

<sup>166</sup> *Ibid*, paragraph 2.39.

- 7.26 A remedy requiring BT to make personalised comparisons, or assessments of savings across the whole-of-market, would likely be significantly more complex and costly, as it would require BT to access information on customer usage, and/or the range of tariffs available in the market. This is likely to be further complicated if the comparison involved dual play as well as SFV tariffs, as it would also need to take into account additional factors such as availability at the customer's address and broadband speeds. This would also require the development of an appropriate approach to making these comparisons, to ensure they are made on an objective basis, are accurate, and up to date. We would need to carry out further assessment of these costs and complexities, as this approach may not be feasible and justified given the potential to be higher cost to implement.
- 7.27 **Risks of adverse consequences:** There is a risk that BT providing information on its competitors could unduly increase perceptions of BT as a trusted provider, and hence reduce switching. For example, there is some evidence that improved disclosure required by the OFT in the case of doorstep selling may have acted to increase consumer trust, perhaps unduly. This resulted in a lower proportion of consumers making price comparisons before purchasing.<sup>167</sup> However we consider ways of avoiding this risk – for example by identifying Ofcom, rather than BT, as the source of the communication.
- 7.28 Requiring BT to make whole-of-market comparisons may carry additional risk. For example, there may be a risk that the comparison BT makes is based on tariffs that are withdrawn from the market before the consumer receives the information on the comparison. We would need to take this risk into account in determining whether it would be feasible or justified for a remedy to cover whole of market comparisons.

## Information on the switching process

### Description of remedy

- 7.29 This remedy would seek to address potential barriers to engagement created by perceptions of high costs of switching. 15%\* of landline customers who do not bundle broadband say that “hassle” is a key reason for not being interested in changing provider.<sup>168</sup> Some of the views underlying this could be related to perceptions of the switching process. 22% of BT's voice-only customers say they perceive switching landline provider to be fairly or very difficult. Some consumers may not be confident that the process will be timely and straightforward, or that there may be a risk of loss of service and this may deter them from seeking or acting on information about offers from other providers.
- 7.30 Ofcom has already taken steps to make the switching process easier for customers of fixed telecoms services:
- 7.30.1 Switching voice and/or broadband services between providers within the Openreach or KCOM copper networks can be done through a gaining-provider led (GPL) process. This means that consumers can switch their broadband and/or phone services within these networks simply by agreeing

<sup>167</sup> Office of Fair Trading (2012), 'Evaluating the impact of the 2004 OFT market study into doorstep selling – Prepared for the Office of Fair Trading by GHK', OFT1413: [http://webarchive.nationalarchives.gov.uk/20140402142426/http://www.offt.gov.uk/shared\\_offt/reports/Evaluating-OFTs-work/oft1413.pdf](http://webarchive.nationalarchives.gov.uk/20140402142426/http://www.offt.gov.uk/shared_offt/reports/Evaluating-OFTs-work/oft1413.pdf)

<sup>168</sup> \* Caution: base under 100 (87) Ofcom switching tracker 2016 – see Annex 8, Figure A8.59.



terms with their new provider. The gaining provider then manages the switch. This means that consumers only need to contact the CP they want to switch to, unless they are switching between networks (e.g. to or from Virgin’s cable network).<sup>169</sup>

- 7.30.2 In addition, number portability arrangements enable customers (that are not moving home) to change their service provider whilst keeping their existing telephone number.<sup>170</sup>
- 7.31 Some consumers may not be aware of these features, or the steps they need to take. They may, for example, be concerned that switching would mean changing their phone number or contacting BT, when for many consumers this would not be the case.<sup>171</sup>
- 7.32 A remedy to address this barrier could require BT to provide information on the switching process to its customers, to address any inaccurate perceptions that they may hold.

### Remedy design

- 7.33 This remedy would particularly focus on explaining key features of the switching process and number portability.
- 7.34 We envisage this would be achieved through requiring BT to provide this information through its communications with customers. As with the communications on potential savings described above, there are a range of options around the information included, format and timing. There is some uncertainty around which options would be the most effective way of providing this information to consumers. For example, this may include:
- Determining the most effective pieces of information about the switching process to provide to consumers.
  - The way this information is phrased, and the level of detail included.
  - The impact of the timing of this information – including whether it is more effective if provided alongside other information (such as information on savings, or notification of price changes).

### Initial assessment

- 7.35 **Effectiveness:** We do not have detailed information on whether, and to what extent, standalone voice customers specifically see the switching process as being an obstacle to switching provider. In our 2016 Switching Tracker survey, 15%\* of standalone voice customers identified “hassle” as a key reason they were not

<sup>169</sup> In July 2016, Ofcom published a consultation on proposals to reform the cross-platform switching process, which would make this switching easier and more reliable for consumers (see here: <https://www.ofcom.org.uk/consultations-and-statements/category-1/making-switching-easier>). This would potentially incorporate, for example, the switching of a landline service from the Openreach network to Virgin’s cable network, and vice versa.

<sup>170</sup> Consumers that are moving home at the same time as they switch provider may be able to take their number with them if they are staying within the same exchange area.

<sup>171</sup> A current marketing campaign for Post Office notes that customers can retain their existing number and sets out a four-step switching process headlined “Joining us is easy”.

interested in switching their provider.<sup>172</sup> Some of the views underlying this could be related to perceptions of the switching process, though there may be other factors too. However, the question may be of little relevance to those customers who see limited, if any, gains to be had from switching. This remedy is more likely to be effective as a complement to the other remedies we discuss, to ensure that consumers are not deterred from switching where there are gains from doing so.

- 7.36 **Costs:** We anticipate that this remedy would have relatively low implementation costs, in line with the lower cost options discussed under information on savings. The information is likely to be generic across consumers in a given group, meaning there would not be a significant burden on BT in producing the information (as it would not need to be personalised to a given customer). If included as an addition to existing communications, it is likely to be particularly low cost, as it would not require a separate communication to be produced.
- 7.37 **Risks of adverse consequences:** The main potential adverse consequence associated with this remedy is the risk of inadvertently and unduly increasing consumer trust in BT as a provider of SFV services, as discussed in the context of the previous remedy. The provision of this information could reinforce consumers' perceptions of BT as a trusted supplier, willing to provide information on switching away from BT. Conversely, this could potentially dampen switching.

## Creating a new decision point

### Description of remedy

- 7.38 Many of BT's SFV customers have been with BT for an extended period of time (77% for more than 10 years, compared to 10%\* of other CP's customers<sup>173</sup>). These customers are highly likely to be outside a minimum contract period (and so would not be prompted by the end of their initial term to consider their options). Although moving home could act as a trigger for some, most of these customers are not likely to be frequently presented with a decision as to whether they should switch tariff or provider. This remedy would seek to address this barrier to engagement created by a lack of triggers to engage. This barrier may contribute to a lack of consumer engagement and switching, compared with a situation where a customer has to make an active decision to renew a contract or switch.
- 7.39 The European Commission's forced choice remedy in the Microsoft Internet Explorer (IE) case provides evidence that prompting a decision can deliver benefits in terms of increased switching. IE's market share in the EU fell by around 10 percentage points more than in the US over the same time period (2010-2014).<sup>174</sup>
- 7.40 We could introduce a remedy to require BT to actively provide a prompt for consumers to engage. This could provide a spur for consumers to access information, assess whether they are receiving the best deal in voice-only services and make an informed choice as to whether to continue with their current tariff with BT or act to switch tariff or supplier.

<sup>172</sup> \* Caution: Base under 100 (87) – see Annex 8, Figure A8.59.

<sup>173</sup> Ofcom, Switching Tracker, July to August 2016, see Annex 8, Figure A8.54. \*Caution: Base under 100 (59).

<sup>174</sup> See, for example, *The Role of Demand-Side Remedies in Driving Effective Competition A Review for Which?* Amelia Fletcher, Centre for Competition Policy, University of East Anglia, 7th November 2016.

7.41 We envisage that this would take place by requiring BT to send a letter or statement to their customers on a regular (likely annual) basis. This would set out their current arrangements and ask whether they want to remain with these arrangements or change them. If customers take no action (i.e. if in effect they ignore the communication), then they will continue to be served by BT as before. In effect, this would create similar conditions to the end of a minimum contract period. BT could be required to provide information on alternatives as part of this notification, and it could include elements of the information on savings and switching set out above.

### Remedy design

7.42 The frequency of the decision point and the timing of this are likely to be key considerations. Evidence suggests consumers may be more likely to act at the start of a new month or year.<sup>175</sup> In addition, we anticipate the sender of the communication may have an impact on effectiveness, for example whether it is sent from BT or Ofcom.

7.43 In a similar way to the remedies described above, there are a range of aspects where detail on the nature of the information provided, its format and its timing would need to be determined. We envisage this would include:

- The format of communications, including whether this notification is provided via a letter or some other means.
- What information is included alongside the notification, building on the considerations outlined above for information on savings or switching.

### Initial assessment

7.44 **Effectiveness / risk of adverse consequences:** A fundamental limitation of this category of remedy is that if customers are presented with a “decision point” and ignore it, then they will simply continue to be served by BT as before. If this threat of potential switching is low, then BT may not face strong incentives to provide competitive offers to retain customers. As a result, any remedy we would consider in this category would effectively amount to presenting information on savings and the switching process (i.e. the previous two remedies considered) in the form of a decision point. This creates three risks:

- that some consumers may pay no more attention than they would to any other communication;
- that information overload caused by providing lots of detail in one communication means consumers do not pay attention to the detail which is important to them; or
- that some consumers may be misled into thinking that they need to take action when that is not the case, potentially causing distress.

7.45 **Cost:** We anticipate that the relative cost of implementing this remedy would be moderate. It is likely to be costlier than making changes to existing communications

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<sup>175</sup> See, for example, Dai, H, Milkman, K.L. & Riis, J. (2014), ‘The Fresh Start Effect: Temporal Landmarks Motivate Aspirational Behaviour’ *Management Science*, available at: [https://faculty.wharton.upenn.edu/wp-content/uploads/2014/06/Dai\\_Fresh\\_Start\\_2014\\_Mgmt\\_Sci.pdf](https://faculty.wharton.upenn.edu/wp-content/uploads/2014/06/Dai_Fresh_Start_2014_Mgmt_Sci.pdf)

that would have been sent in absence of remedies. It would require the creation and sending of an additional communication, with associated costs of production and sending. For example, the postage for an additional one million letters could cost in the region of £250k-350k.<sup>176</sup>

## Increasing the ease of responding

### Description of remedy

- 7.46 This remedy would look to address the barrier to engagement caused by perceptions of difficulties switching and behavioural biases (such as status quo bias), which may make consumers less likely to act on information. If there are ways to make it easier to act, then this may support an increase in switching where it provides benefits to consumers.
- 7.47 This category of remedy would require BT to provide a mechanism to allow customers to easily respond to information they receive. This could be developed as an addition to the provision of information on savings or additional decision point outlined above. For example, this could include the provision of ‘tear-off’ slips which consumers could sign and return in a pre-paid envelope if they wanted to respond to the information on savings remedy. We envisage this response could take two forms:
- 7.47.1 The first would allow consumers to respond to offered changes in tariff within BT, and request BT make this change to their tariff. In the case of BT Basic, this may take the form of a request for an application form, which would subsequently need to be completed by the consumer.
- 7.47.2 The second would allow consumers to respond to information on savings from switching provider by requesting more information from the alternative provider.<sup>177</sup>
- 7.48 A first step in taking forward this category of remedy would be to carry out further research – particularly qualitative market research to specifically explore barriers to changing tariff or switching provider which SFV customers may currently face.

### Remedy design

- 7.49 The effectiveness of this remedy is likely to depend on the nature of the action required for a consumer to respond, the options provided for consumers to choose from and the framing of this choice.
- 7.50 A response to a potential change of tariff within BT is likely to be straightforward to implement, in that it would only require BT to arrange for consumers to send responses to itself.
- 7.51 Where the response involves requesting more information on a possible switch to another CP, this would be more complicated. It would require a degree of

<sup>176</sup> Based on Royal Mail business mail calculator, sending 1,000,000 letters second class.

<sup>177</sup> We note some parallels with the “reply card” system that was in place until July 2002. To switch to carrier pre-selection (CPS) when the reply card system was in place customers had to sign and return a confirmation slip to BT. This was alongside the separate process of making arrangements with their prospective CPS provider (such as signing and returning a contract). Industry experience of the reply card found that, in practice, it proved to be an obstacle to switching resulting in low switching levels. After use of the reply card was stopped, CPS orders increased dramatically.

coordination to enable the customer's response to reach the relevant CP, though we envisage this could be achieved by, for example, including an envelope addressed to the relevant other CP identified in the information or comparison provided.

### Initial assessment

- 7.52 **Effectiveness:** A remedy which reduces or removes barriers to responding will, by its nature, only be effective if consumers are willing to change tariff or switch provider in the absence of these barriers. In the present case, it therefore depends on other remedies being effective in increasing consumer engagement (such as enabling consumers to access and assess information on potential savings).
- 7.53 The FCA's work on cash savings looked at a return switching form pre-filled for a switch to the best internal rate, along with a prepaid envelope. This allowed customers to request to change their account with their current provider. In trials, they found this to be successful, increasing switching by nine percentage points.<sup>178</sup> Experience from other cases indicates that the results of making switching easier can vary widely from case to case. This category of remedy may act as a complement to other engagement remedies, by making it easier to respond at the time consumers receive information on savings and switching, helping to overcome status quo bias.
- 7.54 **Costs and risks of adverse consequences:** We would expect these measures would have moderate costs of implementation, such as providing customers with tear-off slips and pre-paid envelopes to select a new BT tariff or request more information from an alternative CP. The cost of postage for reply envelopes could be in the region of £30,000-70,000.<sup>179</sup>
- 7.55 A measure targeted at switching tariff with BT could have the unintended consequence of resulting in consumers inadvertently finding themselves tied into a minimum contract period when they change to a new tariff. This may need to be managed through the remedy design, such as by ensuring any minimum term is clearly communicated to customers.
- 7.56 A broader process allowing consumers to request further information about a potential switch from the prospective gaining CP could incur some additional costs if implemented, as it would require coordination to enable the customer's response to reach the relevant CP.

### **Default tariff**

#### Description of remedy

- 7.57 An alternative approach to address low levels of switching would be to introduce a remedy which directly protects consumers and does not require them to actively participate in the switching process. This could mandate that, as a default, BT move its consumers to its best available tariff given their recent usage. The aim of this remedy would be to address barriers to engagement by reducing the level of engagement needed from consumers. This would ensure that consumers were protected from the detriment of being on the wrong tariff for their usage.

<sup>178</sup> FCA (2016), 'Attention, Search and Switching: Evidence on Mandated Disclosure from the Savings Market' <https://www.fca.org.uk/publication/occasional-papers/occasional-paper-19.pdf>

<sup>179</sup> Based on a 10-20% response rate to 1,000,000 letters, at Royal Mail Business Reply Plus second class rate of £0.335 per reply sent.

- 7.58 We envisage this remedy could take the form of a provision requiring BT to ensure that each of its SFV customers were moved to the tariff that represented the best value for money for them, given their historical usage. For example, BT currently offers a Home Phone Saver product that would likely be better value for many of BT's voice-only customers. A customer who purchases only standard line rental and unlimited anytime calls from BT could save £5.50/month by switching to Home Phone Saver.
- 7.59 For BT's split-service customers, this category of remedy could take the form of replacing their standalone voice product with an equivalent dual play product bundled with their broadband purchase. For example, a customer purchasing a 17Mb broadband-only product for up to £34/month and separate line rental at £18.99/month would save up to £19/month by switching to an equivalent dual play product. Of course this would only impact on a very small percentage of the market.

### Remedy design

- 7.60 This remedy would require a range of detailed rules to be specified in advance, to ensure consumers were being switched to an appropriate deal. We envisage this would include specifying the criteria for determining historical usage in order to calculate the best tariff for each consumer. For instance, specifying that they should only be moved to a tariff that would have been better for them over a particular length of time (such as each of the previous four quarters). Opt-out arrangements would also need to be specified, including the notice period required before the change would take effect. This would allow consumers to choose not to be switched if they considered that the proposed new tariff was not right for their needs.
- 7.61 The effectiveness of this remedy may depend on the design, format and timing of the notification explaining the default switch to consumers and providing them with the opportunity to opt out. For instance, this could include different ways of explaining the savings that could be made if the consumer allowed the switch to go ahead.

### Initial assessment

- 7.62 **Effectiveness:** This remedy has the advantage of potentially ensuring that consumers are moved to a better tariff from BT if one exists for them, without a need to engage in the market. It provides direct protection for those customers who are not engaged and may be less likely to respond to improved information on savings and switching.
- 7.63 This remedy may be most effective if applied to split-service customers. These customers could be automatically switched from separate, i.e. unbundled, voice and broadband services from BT, to an equivalent dual play bundle from BT if that provided them with savings. We understand several other providers in effect do this already. As they would not experience any change in the service they received, it would be straightforward to design in a way that maximises potential effectiveness in reducing detriment.
- 7.64 Overall, while there is some potential for this remedy to improve consumer outcomes in relation to their BT tariff, this remedy would not promote competition, as it would only lead to switching between BT tariffs, rather than switching to rivals.
- 7.65 **Costs:** We expect that the principal costs of implementing this remedy would be as follows: (a) the operational cost to BT of calculating the optimum tariff for each of its SFV customers, and of switching them to this tariff (i.e. updating its billing systems);

(b) the cost to BT of communicating this change to its customers; and (c) the cost to BT of providing follow-up support to customers who wanted information about the switch, or had failed to opt-out but wanted to revert to their earlier arrangements. We would expect the implementation costs to be somewhat higher than for the information remedies we have discussed above.

7.66 **Risk of unintended consequences:** Automatic switching within BT tariffs may carry several risks of unintended consequences, such as:

- BT altering the range of tariffs it offers, which may affect or remove the cheapest offers in the market. Specifically, BT may choose to change or withdraw the Home Phone Saver tariff, which would eliminate a significant source of current potential savings for voice-only customers.
- Some consumers could change their usage subsequent to the switch, such that the tariff to which they have been moved is no longer the best one for them. If usage is changing over time, this could be an issue unless the automatic switching exercise is repeated periodically.<sup>180</sup>
- BT may not have sufficient information to make this assessment on behalf of consumers. For example, they would not know if the consumer was eligible for BT Basic so this tariff could not be included in this process (although information about BT Basic, including its eligibility criteria, could be provided to BT customers).
- The best available tariff may require consumers to sign up to a minimum contract period, and it may not be appropriate for consumers to be committed to this by default.
- Consumers who feel they have been protected by this remedy might have even less incentive to engage in the market – in particular by considering offers from other providers than BT.
- Some consumers – including some vulnerable consumers – may fail to opt-out if they do not notice the opportunity to do this, and so end up with a different tariff against their preferences without intending to do so.

7.67 Further, it is likely to be challenging to ensure that all consumers are better off if they allow the switch to go ahead. For example, if a consumer's usage pattern was likely to change they may have been better remaining on their previous tariff. Specifically, Home Phone Saver has a higher rate for calls to mobiles, and so a consumer increasing their call volumes to mobiles after being switched could be worse off.

7.68 This risk is closely linked to the importance of usage in determining the best tariff. The more important usage is, the more valuable this remedy is likely to be. For voice-only customers, the key determinant in choosing between call plans is the time of day at which consumers typically make calls (e.g. whether they tend to make calls during

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<sup>180</sup> However, to the extent that usage of landlines is generally decreasing over time, customers could still be better off with a one-off automatic switch than with the status quo. For example, a customer could be switched from an Anytime call plan to an Evenings and Weekends call plan in Year 1. By Year 3 their usage might have declined to the point where a Weekends call plan was most suitable for them, rather than the call plan they are on, but they would still be better off than if they had stayed on the Anytime call plan.

the day on weekdays). It is likely that many consumers may be able to make this assessment relatively easily, which may limit the value of a usage-based automatic change in tariff. In addition, call plans tend to be standardised across providers (most CPs offer three: weekends, evenings and weekends, and anytime).

## **Disclosure of information on BT's inactive voice-only customers**

### Description of remedy

- 7.69 Acquisition costs could be reduced by making it easier for competing firms or third party intermediaries (such as price comparison websites) to identify and contact consumers in this market. This could be achieved by requiring BT to gather information on their standalone voice customers who have not recently switched and create a database of this information, which could then be provided to (potential) competitors or third parties.<sup>181</sup> This would identify these customers, provide contact details and potentially their current tariff and usage pattern. Customers would be able to opt out of inclusion in this process at any time.<sup>182</sup>
- 7.70 This information could be used to make it easier for competing suppliers (or third party intermediaries) to reach these customers, and hence reduce acquisition costs. It would also enable them to provide bespoke offers that reflect an individual customer's circumstances, current tariff and usage patterns.

### Remedy design

- 7.71 It would be important to ensure the database is kept up to date so that it is useful for competing CPs and third parties. The inclusion of detailed usage information would allow competitors to provide personalised offers to consumers. However, this increased complexity may make the database more complex to develop and keep up to date.
- 7.72 It may be necessary to place restrictions on the communications initiated under this remedy (such as their frequency), in order to ensure they do not inadvertently reduce consumer engagement.
- 7.73 The information collected would contain personal information for some of the most vulnerable consumers, and so would be highly sensitive. It would be necessary to ensure sufficiently strong data protection, and restrictions around access to this data. The database could be open to all actual or potential suppliers of standalone voice services, as the telecoms market operates under a general authorisation regime (in contrast to an individual licensing regime as in energy, for example). This may mean the database could be open to a potentially large number of organisations without ex ante approval of this access. This may mean there is a requirement for a screening process before a CP is allowed access, and ongoing monitoring of access. Alternatively, Ofcom could select, through some form of vetting process, a subset of

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<sup>181</sup> Following the CMA's energy market investigation, Ofgem are currently working to implement a similar database for customers in the energy market on standard tariffs. See here:

<https://www.ofgem.gov.uk/consumers/household-gas-and-electricity-guide/how-switch-energy-supplier-and-shop-better-deal/ofgem-energy-customer-database-service>

<sup>182</sup> Consumers who have signed up to the telephone preference service (TPS) should not be contacted by phone for marketing purposes without explicit consent. This may require a separate process to allow these consumers to consent (if they so wished) to inclusion in the database, for the purposes of voice calls.



CPs to have access to the database but this would itself raise issues around constraining competition.

### Initial assessment

- 7.74 **Effectiveness:** The disclosure of information on BT's inactive voice-only customers to competitors would reduce acquisition costs and so could make competing CPs more likely to seek to win these customers from BT. However, its effectiveness would depend firstly on BT customers not choosing to opt out of inclusion in the database in the first instance, and then responding to marketing communications from BT's competitors or third parties. If some of these customers are TPS registered, then CPs should not contact them by telephone without explicit consent. The value of this remedy is also dependent on the importance of usage information in determining appropriate tariff, which we think may be relatively unimportant for many customers in these markets.
- 7.75 **Cost:** Addressing the design issues outlined above may be challenging and costly. For example, ensuring the data was held in a secure format, yet accessible to third parties in a way that enables them to use it effectively. Screening CPs before allowing access would add another level of complexity to this remedy. Implementing this remedy is also likely to be significantly costlier than the other remedies focused on changes to consumer communication. We estimate one-off costs of the order £[>].
- 7.76 **Risk of adverse consequences:** There is a material risk that consumers who would prefer not to be on the database were nevertheless included by default, having failed to opt-out. Consumers on the database may receive more marketing communications than they want to receive about alternative SFV services. Some vulnerable consumers could find this distressing. There is also a risk of confusion for consumers who are already TPS registered; for instance, they may be uncertain which arrangement takes precedence.
- 7.77 Sharing a database of this nature – particularly one including a large proportion of older and potentially vulnerable consumers – with third parties is likely to raise serious concerns about data security. If the information was misused, there is a risk of significant consumer harm (such as from nuisance calls or scams). If we seek to limit access to the database Ofcom would need to develop access criteria for CPs.

## Scope for engagement remedies to address our SMP concerns

### The more intrusive remedies have significant downsides

- 7.78 Broadly speaking, we can categorise the remedies we have considered above into:
- 7.78.1 Remedies which make it easier for consumers to engage in the market: information on savings, information on the switching process; introduction of a decision point; remedies to facilitate response to this information.
- 7.78.2 Remedies which are likely to lead directly to a change in outcomes for a substantial number of consumers, unless they opt out of them: automatic switching within BT's tariffs, or the creation of a customer database.
- 7.79 While the latter group of remedies may have a more direct effect, they entail a significant risk of adverse consequences. In particular, there is a risk of over-riding consumer choice. This may mean some customers will ignore or fail to notice that

they have an opportunity to opt out of these remedies, and as a result may end up with a change in their landline provision which they did not expect, and/or which may be not suit them if their circumstances are changing. Of these two remedies, this risk may be lowest (though still potentially material) for automatic switching within BT's tariffs, as this remedy does not entail a change of provider (or sharing of customer data with third parties). As this remedy is limited to helping customers get the best available deal from BT, rather than the best deal on the market, and as such does not promote competition and is likely to have a limited effect in addressing our SMP concerns.

- 7.80 Linked to this, some of these remedies require a third party to take responsibility for the outcome for consumers. It may be complex to ensure that the outcome is unambiguously the best one for consumers, and may not be appropriate for the third party to take on this role (e.g., BT selecting which of their tariffs consumers should automatically be switched to), in place of consumer choice.
- 7.81 In addition, as discussed above these remedies present significant design challenges if undesired consequences are to be avoided. We have concerns around consumer privacy in relation to the potential sharing of their information. Also, these remedies could potentially entail repeated intervention (such as repeated automatic switching within BT tariffs) in the light of subsequent market changes.
- 7.82 In the present case, we think the risks associated with these remedies are particularly acute because there are potentially a large number of vulnerable citizens among the consumers concerned – for example around 43% of BT's standalone fixed voice customers are aged 75 or older. At the same time, a standalone fixed voice service typically represents a relatively small proportion of household spend, so the potential savings for an individual moving to a better deal may be relatively limited, albeit that the detriment is significant across the market as a whole.
- 7.83 In summary, whilst these remedies may have the potential to promote competition and reduce detriment, we think the risks of unintended consequences would outweigh these potential benefits. We therefore provisionally conclude that we should not take forward either of the following remedies: automatic switching within BT tariffs, or creation of a customer database and disclosure of this information to CPs or third parties.

### **Making it easier for consumers to engage has potential**

- 7.84 Turning to our first category of remedies – those that provide information that could potentially make it easier for consumers to engage in the market – ultimately these rely on a response by consumers to have the desired outcome of promoting competition and addressing our SMP concerns. On the one hand, this may reduce the risk of adverse consequences as, at worst, consumers can simply ignore them and continue as before. On the other hand, to be effective they rely on consumers not doing this, but rather becoming more engaged in the market. They also rely on at least some suppliers responding to this increased level of customer engagement by actively competing for their business. Finally, fully addressing our competition concerns would require that consumer and supplier engagement must be sustained over time. Trialling these remedies would allow us to gather evidence on their potential impact in promoting competition.
- 7.85 We consider there is a reasonable prospect that an effective increase in consumer engagement would encourage some suppliers to become more engaged in the market. However, there are reasons to believe that achieving and sustaining a

substantial increase in engagement may be challenging. In particular, the fact that in many cases SFV spending – and the potential savings from competition – is likely to be a relatively small proportion of household budgets, may limit the incentive for consumers to become more engaged. In addition, the relatively small (and declining) size of the market and the lack of upselling opportunities may limit supplier engagement even if remedies succeeded in increasing consumer engagement. There are some further risks to the effectiveness of these remedies in increasing consumer engagement:

7.85.1 **Price cap:** If we introduce a cap on BT's prices, below current levels, it would mean that other CPs would in most cases have to offer lower prices than they do at present, if they are to attract customers away from BT. We discuss the trade-off between a price cap and measures to promote competition in sections 8 and 9.

7.85.2 **Timing:** The effectiveness of many of the engagement remedies we discuss will depend on the attractiveness of alternative offers (relative to BT's prices) which are available on the market at the time that the remedy is tested and/or implemented. Ongoing consumer engagement will require CPs to effectively market and promote their offers. There is a risk that if CPs do not have competitive offers in the market at the right time, consumers will be unresponsive to any engagement remedies based on such offers.

7.86 While there is some uncertainty as to the potential effectiveness of these remedies, we consider that there is sufficient merit in this first group of remedies such that, should we conclude promotion of competition is warranted, they are suitable for further development and trialling, namely:

- information on savings;
- information on the switching process;
- introduction of a decision point; and
- remedies to facilitate response to this information.

7.87 We see these information remedies as complementary to one another and we would seek to develop them as a package. This trialling would allow us to gather evidence on the effectiveness and optimal design of these remedies.

## Trialling engagement remedies

### We would trial engagement remedies before implementing

7.88 The remedies discussed above have the potential to reduce acquisition costs and lower barriers to entry and expansion in the SFV markets. This would act to promote competition and address the detriment identified in Section 6. We identify the remedies that merit further consideration below.

7.89 Evidence suggests BT's customers are particularly unengaged, and many have never switched their fixed voice provider. If effective, remedies to promote competition would address BT's SMP by reducing barriers to entry and expansion faced by BT's competitors.

- 7.90 We anticipate carrying out further consumer research on the extent and nature of barriers to engagement, to inform our final decision on which remedies to take forward and their detailed design.
- 7.91 Recent regulatory practice in this area also emphasises the importance of systematically testing, trialling, evaluating and refining engagement remedies. For example, the FCA regularly trials remedies before implementation. The CMA's recommendations in banking and energy also emphasise the importance of trials to gather evidence on the effectiveness of engagement remedies before implementation. The Behavioural Insights Team has also carried out a range of trials across sectors.
- 7.92 In the discussion above, we noted some of the design choices and market features that could determine the effectiveness of the remedies we are considering. Theory, literature and experience from other markets can provide some insights into what measure might or might not be effective, though it is not possible to know which will be most effective in practice in this market. Small changes – for example to the specific information provided or the way in which it is communicated – can make big differences to consumer responses.
- 7.93 Given this uncertainty around the effectiveness and optimal design of these remedies, in our view it would be disproportionate to impose any of these remedies at this stage, without first gathering further evidence. We would propose to require BT to cooperate in testing and implementing engagement remedies. This would allow us to gather evidence on overall effectiveness and test some of the detailed design considerations outlined above. We would propose SMP conditions requiring this cooperation.
- 7.94 In order to design these remedies to be as effective as possible, we would expect to conduct consumer research and a programme of trialling of the remedies that we consider have greatest potential. This would allow us to reach a final view on (a) the specific design features that would maximise the effectiveness of these remedies and (b) whether we can identify a package of remedies which is appropriate and proportionate to implement under SMP conditions.

### Approach to trialling process

- 7.95 Trialling engagement remedies would enable us to identify the most effective engagement remedies, and the optimal design of these remedies.
- 7.96 We envisage five stages to the process:
- 7.96.1 **Diagnosing the issue** to be addressed, potentially including research to identify the specific factor(s) restricting engagement. For example, which are the most critical barriers to engagement. This would also include considering whether the issue is common across all standalone voice customers, or just a subset (such as voice-only or split-purchase customers).
- 7.96.2 **Identifying the remedies** to be trialled, specifying their detailed design, carrying out research and tests (such as focus groups or lab experiments) to refine these options and determining which specific aspects would be varied in trials to provide evidence on optimal design.

- 7.96.3 **Designing and running the trial**, which could be a randomised control trial (RCT) if appropriate, or another method of testing such as quasi-experimental analysis or lab-based testing.
- 7.96.4 **Assessing the results** of these trials, and then implementing the permutations shown to be most effective (if any).
- 7.96.5 **Monitoring and evaluating the implemented measures**, with further testing of refinements and adjustments to remedies where appropriate.
- 7.97 We propose that trialling should be subject to a set of principles to ensure it is effective and avoids unintended consequences. We propose the following principles:
- The remedies trialled should be proportionate to the problem they are seeking to address.
  - The frequency and number of trials should also reflect the detriment identified in the market, accounting for any detriment addressed through other remedies – for example, the application of a price control if one is introduced.
  - The trials should have clearly defined success criteria at the outset, which the results can be measured against.
  - The trials should be transparent, with details published on the process and analysis of the results to allow independent verification.
  - The trials should be ethical – for example they should not deny information to consumers that they would have received in the absence of a trial.
- 7.98 We consider that the overall programme for these trials should be led by Ofcom. This will allow us to take a market-wide view of the trials and their impacts, and ensure that both the process of trialling and any changes subsequently implemented are in the interests of consumers and address the detriment identified in this market review.
- 7.99 We expect that the cost of the initial phase of diagnosing the issue and identifying remedies would fall on Ofcom. This would include further research to inform these initial stages, which we envisage could be carried out at moderate cost. Running any trials themselves would entail some cost which we would require BT to bear, though we anticipate in the case of the remedies we propose to take forward this would be modest (in general less than £100,000 per trial).<sup>183</sup>

#### **Example hypothetical trial process – information on savings**

We set out below a hypothetical example of a trial process, including roles and responsibilities and the type of issues that could be subject to trial:

<sup>183</sup> To give an indication, when implementing the results of RCTs in its review of cash savings, the FCA estimated the overall burden per firm of making several changes the information provided to their entire customer base to be around £100k. We estimate the postage cost of additional communications to be around 30p per letter (so a trial of 10,000 customers would cost around £3,000 in postage).

**Step 1)** Ofcom carries out research into barriers to consumer engagement that indicate that access to information on savings is a key factor limiting engagement among voice-only customers.

**Step 2)** Ofcom determines that this could be remedied through the provision of information on savings as part of BT's bills. Ofcom also carries out initial testing through focus groups or lab tests to narrow down options for trialling. This indicates that consumers respond better to information on annual rather than monthly savings. Ofcom specifies that the trial would test the provision of information on potential annual savings, and would test whether this information should be presented in absolute or percentage terms, and whether it should be provided as a generic or personalised statement.

**Step 3)** Ofcom determines that these four options should be tested through an RCT, with a random sample of 20,000 of BT's voice-only customers. The sample would be split into a control group and 4 treatment groups with the permutations specified above (that is: generic, absolute terms; personalised, absolute terms; generic, percentage terms; personalised, percentage terms).

**Step 4)** The trial is run, with BT making the specified changes to the next bill for these customers, and then monitoring their behaviour in the following three months. This would include collecting information on whether customers in the control and treatment groups switched provider or changed tariff. Ofcom evaluates the results of the trial, and determines whether any of the treatments generated statistically significant effects, and if so which generated the largest effect. Ofcom then directs implementation of this remedy across BT's voice-only customer base.

**Step 5)** BT is required to continue to gather information on the impact of the implemented remedy, by monitoring switching rates, and reporting on this to Ofcom. Ofcom would evaluate this information and determine if the remedy was effective as indicated by the trial. If necessary, Ofcom would propose changes to the remedy, and kick-off a new round of trials to examine these.

- 7.100 In summary, should we decide to act to promote competition, we would propose BT be required to provide information to Ofcom to inform the design of any trial, as well as details on the results of a trial. This is because BT holds information that we could not easily obtain ourselves, and has the customer relationship that would allow them to effectively measure the impact (such as recording the number of customers from each group who switch tariff or supplier in a given time frame).
- 7.101 We would also propose that BT would be required to carry out the trial in line with the parameters set out by Ofcom. This is because BT is best placed to carry out these trials efficiently as it has the existing systems and processes in place to communicate with its customer base. For Ofcom to carry out the trial would require a degree of replication of these systems, and so significant additional overall cost. In addition, much of the remedies may involve changes to existing BT communications, which by definition would need to be made by BT.
- 7.102 We anticipate that these trials would be of a relatively large scale. This is because changes in behaviour may be relatively small yet still have a meaningful impact on consumer detriment. A large sample is therefore needed to ensure appropriately narrow confidence intervals and provide robust evidence on the effectiveness of potential remedies. The sample size will also depend on the number of permutations

being tested. As a guide for scale, we anticipate a trial may involve around 10,000 BT customers.

- 7.103 We recognise that trialling engagement remedies will mean it will take time before those remedies identified as effective can be fully implemented across BT's standalone voice customer base. We anticipate that this process of development, trialling and implementation could take up to two years before any engagement remedies are fully implemented.<sup>184</sup> Due to this time needed for development and trialling before full implementation, these engagement remedies will not be able to immediately address the detriment we have identified.
- 7.104 If a particular remedy is shown to be effective in the trialling phase, we would direct BT to implement the remedy in respect of all SFV customers.
- 7.105 We consider the appropriateness of setting regulation to impose these remedies in Section 9 alongside our consideration of our options for price controls.

## Consultation questions

*Question 7.1: Do you agree with the need to trial and test engagement remedies before implementation? Please explain your reasons for this.*

*Question 7.2: Do you agree that remedies focussed on improving consumer communications to increase engagement listed below offer a reasonable prospect of success in encouraging competition?*

- *information on savings;*
- *information on the switching process;*
- *introduction of a decision point; and*
- *remedies to facilitate response to this information.*

*Please explain your reasons.*

*Question 7.3: Do you agree with our conclusions that the other remedial options we have considered, namely the establishment of a customer database for marketing purposes and automatic switching within BT's tariffs, raise significant implementation risks and therefore do not warrant further consideration? If you do not agree or consider there are other options we should have considered, please provide your reasons.*

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<sup>184</sup> On the basis of the process outlined in paragraph 7.96 above, we envisage it would take 6-12 months to diagnose the issue, identify remedies and carry out any initial testing of these (such as focus groups or lab tests). The RCT would then be in the field for at least three months, and analysis of results and direction to implement successful remedy would take a further three months. Finally, allowing time for the changes to be implemented could take up to a further six months.

## Section 8

# Options for a price control remedy

## Introduction

- 8.1 We set out in Section 6, the direct consumer harm that we believe is occurring due to pricing of standalone fixed voice (SFV) services above the competitive level and that a possible remedy to deal with this harm was the imposition of a price control obligation on SFV services provided by BT. In this section we explain:
- i) How we have determined the options for the appropriate level of a price control; and
  - ii) If a price control is imposed how we would plan to implement a price control in terms of duration, which products are price controlled and over what period we would reduce prices.

## Framework for assessing the appropriate level of prices

- 8.2 In developing proposals for the appropriate level of prices for an SFV control, we have considered the following factors:
- **Protecting consumers from prices above costs:** as set out in Section 6, our analysis suggests that BT's prices of SFV services are above what we would expect to see in a competitive market. Given past price increases and BT's current level of profitability, customers of SFV services are paying considerably more than they should be.
  - **Promoting competition in the provision of SFV services:** in Section 7 we discuss remedies to support increased consumer engagement and encouraging competitive entry and expansion. These remedies will not be effective in promoting competition if we reduce the price of SFV services below the level at which it is profitable for other CPs to acquire SFV customers. When dealing with SFV customers, these acquisition costs may be quite substantial, although such costs should be reduced if engagement remedies prove to be effective.
- 8.3 We therefore face a trade-off between controlling prices in a way that protects consumers and ensuring that we do not reduce them by so much that we weaken the scope for growth in competition (taking into account the impact of any engagement remedies discussed in Section 7). We can strike this trade-off in various ways with a range of options on a price control.

## Options for setting prices

- 8.4 When setting prices via a price control, we first need to consider whether the purpose of the price control is to prevent SFV customers being made worse off than currently (i.e. by stopping prices rising above their current levels) while any engagement remedies take effect, or whether we want to actively reduce the prices paid by SFV customers.



### A safeguard cap

- 8.5 When we use a safeguard cap, we set a price control that prevents prices increasing above their current levels (in either nominal or real terms, allowing for increases up to the rate of inflation). We generally use a safeguard cap when we believe that competition is growing and we expect that as competition develops competitive pressures will cause prices to decrease without undue delay. The safeguard cap ensures that consumers are made no worse off by further price increases in the time it takes for competition to develop.
- 8.6 If competition does not develop sufficiently quickly, a safeguard cap may not be appropriate because it would leave consumers paying high prices for longer than necessary. We would therefore only wish to use a safeguard cap if we believed that effective competition would develop within a reasonable time after the start of the price control.

### A price reduction

- 8.7 In developing our price reduction options we have sought to assess two price points:
- The price reduction we could impose on BT if we were not concerned about allowing competition to develop because we believed it was not viable (i.e. a cost based charge derived from BT's costs). We refer to this option as the "**maximum price reduction**".
  - The price reduction we could impose on BT in order to protect consumers from high prices whilst still allowing effective competition to develop for SFV customers. We refer to this option as the "**price reduction consistent with promoting competition**".
- 8.8 We set out our conclusion on the prospects for competition to develop and which of the price control options we propose to use in Section 9.

## **Options for the size of a reduction in the price of SFV services**

### **BT's cost of providing retail services**

- 8.9 We have collected information from BT on its costs of providing retail services. In assessing the level of BT's costs, we did not consider it appropriate to produce detailed cost modelling. Cost models are most appropriate where there are clearly identifiable relationships between services and the costs to provide those services. Some costs associated with the provision of retail services are easily identifiable (e.g. the price of wholesale line rental), however, where we have a retail provider providing multiple products, allocating retailing costs between products is not straightforward. We have therefore taken a relatively high level approach to allocating retail costs (as described below and in paragraphs A5.40 to A5.42 rather than attempting to model costs explicitly.
- 8.10 We do not believe there is clear evidence that service costs per line will change significantly over the price control period. [X]. [X]. We have therefore not

undertaken any cost forecasting when determining BT's level of future profitability.<sup>185</sup> We discuss how we might allow prices to change over the price control period below.

- 8.11 In addition to determining an appropriate cost level, we also need to consider how to determine an appropriate level of profitability for BT retail services. Our starting point is to use a measure of BT's weighted average cost of capital (WACC) as an appropriate level of profitability and compare this to BT's ROCE for SFV services. This is our preferred approach when setting charge controls on wholesale services. As we set out in Annex 5, using a ROCE approach has some drawbacks when dealing with retail services. We would expect retail operators to have low capital employed which is partly due to a high level of intangible assets.
- 8.12 We may not wish to include some of these intangible assets, such as brand value, because they may (at least in part) reflect BT's market power. However, we would want to capture the value of other intangible assets, such as the value of staff training. As discussed in Annex 5, we would only want to include intangible assets to the extent that they would form part of an operator's asset base if it operated in a competitive environment.
- 8.13 We have also considered using BT's return on sales (ROS)<sup>186</sup> as a measure of BT's profitability. As discussed in detail in Annex 5, we consider ROS as preferable in this case. Although ROS is not as well based in economic theory as ROCE, we are able to estimate it more accurately and it does provide us with an acceptable proxy for profitability. It is also a measure that is widely used by regulatory bodies controlling retail prices and is well understood by industry.
- 8.14 Although we are able to measure BT's ROS, we do not have an established method for calculating a cost-based level of ROS. We have looked at benchmarks used across other industries and believe that a ROS of between 5% and 10% is broadly consistent with a cost-based measure of profitability in a fully competitive market (see Section A5.86).
- 8.15 In order to calculate BT's level of profitability, we requested data from BT Consumer on costs and revenues for its fixed voice consumers. BT was able to provide us with the direct wholesale cost of providing voice services, but it was not able to split the majority of retail costs between different services. Where BT was not able to identify to which products retail costs should be allocated, we allocated them between fixed voice and fixed broadband services based on the number of lines in each financial year, i.e. we assumed the cost was the same for each fixed voice and for each fixed broadband line. We consider this to be a conservative assumption because we did not allocate any of these costs to BT Mobile, BT Sport or BT TV.
- 8.16 We also considered whether we should calculate costs and revenues for SFV customers separately from other voice customers. Our analysis (as shown in paragraphs A5.43 to A5.52) suggests that the net cost and revenue difference between SFV customers and other voice customers is not material for our

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<sup>185</sup> As discussed in Annex 5, we are aware that there may be price and cost changes in the 2016/17 and 2017/18 financial years (e.g. the cost of nuisance call blocking) and we will look to capture these changes once further data is available. However, we do not believe that any of these changes would be sufficiently large to change our view on BT's profitability.

<sup>186</sup> Also referred to as the EBIT (earnings before interest and tax) margin.

purposes.<sup>187</sup> We have therefore calculated the profitability per line BT achieves on voice across all consumers and assumed this is the same for SFV customers.

- 8.17 BT currently earns revenue of approximately £[redacted] per month (ex VAT) from SFV subscribers on average. Our estimates of BT's costs suggest it achieved profitability (ROS) for SFV services in 2015/16 of c.34-42%, which equates to profit of about £8-10 per line per month (ex VAT). Our analysis suggests that a ROS of no more than 10% is consistent with a cost based estimate of profitability for a provider of retail voice services, which equates to profit of between £[redacted] and £[redacted] per month. We could therefore reduce prices for SFV services by around £[redacted] per month (ex VAT) in order to reduce BT's profitability on these consumers to a cost based level, which equates to a decrease in prices that consumers experience of between £8-10 per month (inc VAT).
- 8.18 However, as discussed below, an adjustment of this size would be highly likely to make it uneconomic for other CPs to compete in offering SFV services and acquiring customers. Other CPs incur substantial acquisition costs when acquiring customers, which BT does not incur when serving its existing SFV subscriber base. These costs make other CPs less profitable when compared to BT. Even if the engagement remedies we discuss in Section 7 are effective, some acquisition costs will remain meaning it is unlikely that other CPs would be able to profitably supply SFV customers if prices were set on the basis of BT's costs. We would therefore only use an £8-10 reduction in prices if we were not also imposing engagement remedies. We discuss below the level of price reduction that is still consistent with competition emerging.

### **A competitive benchmark for SFV retail prices**

- 8.19 In order to understand how much we could reduce prices by and still expect competition to emerge, we have looked a number of different measures in order to estimate a competitive benchmark. Analysis of these options is set out in more detail in paragraphs A5.70 to A5.86.

#### **BT's historic levels of profitability for SFV voice services:**

- 8.20 In 2009 we removed retail regulation on the basis that the retail market was competitive. BT's level of retail profitability at this time was at a level at which we believed regulation was no longer necessary, given the market circumstances. At that time BT was struggling to maintain its market share and, despite the removal of retail price controls in 2006 did not appear to have the commercial freedom to raise retail prices. Accordingly, the level of profitability that BT achieved on retail services at that time provides us with a starting point for the level of profitability that we believe is consistent with a market that is sufficiently competitive not to require regulation.
- 8.21 In 2009, we assessed BT's profitability using ROS and have used the same approach for this assessment. Our assessment of ROS in 2009 suggests a margin for BT of c.20% is consistent with emerging competition.<sup>188</sup> If a similar margin was applied today, BT's monthly line rental would need to be reduced by approximately £[redacted] (ex. VAT).

<sup>187</sup> We estimate that there is £[redacted] more revenue for SFV customers and £[redacted] more cost. However, there is a high degree of uncertainty associated with these estimates.

<sup>188</sup> See Figure 5.4, [https://www.ofcom.org.uk/data/assets/pdf\\_file/0023/51836/statement.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0023/51836/statement.pdf)

Current levels of profitability in the dual play market:

- 8.22 Although there is limited competition in the SFV market there is more active competition in other retail services. For example, dual-play bundles include voice services but also broadband services. By assessing the level of profitability in dual-play services with active competition, we can obtain a benchmark for the level of profitability required to encourage competitive entry.
- 8.23 Using a similar approach as we used to calculate the profitability of SFV customers, we have assessed current levels of profitability in dual play for BT (outlined in paragraphs A5.79 to A5.81. We have calculated ROS margins of c. [x%] for BT's combined net margin for fixed voice and broadband service.<sup>189</sup>

Profitability of other communication providers

- 8.24 Other CPs are likely to have a different cost base to BT and may not benefit from the same economies of scale. As with BT, we have sought to calculate the level of profitability achieved by other CPs offering retail voice products.<sup>190</sup> Our analysis of other CPs' data suggests they are achieving ROS margins of c. [x%] for retail voice services. This may not be surprising because, as we discuss in Section 4, we have evidence to suggest BT acts as a price leader with other CPs following its price increases. However, while these ROS margins appear to be similar to those for BT, other CPs had lower revenues and lower profits in absolute terms. BT's absolute profit in £ per customer was approximately [x%] higher than the next most profitable CP.
- 8.25 This level of profitability for other CPs is still high, suggesting other CPs could still potentially be profitable if we reduced SFV prices closer to BT's costs. However, we are concerned about the robustness of our estimates for other CPs' profitability. We were not able to obtain data for all other CPs and those CPs that were able to provide us with data were only able to provide them at an aggregate level (i.e. for all fixed voice customers including those that purchase broadband). We have therefore treated the results of our analysis of the profitability of other CPs with caution.

Profitability of a marginal subscriber

- 8.26 In the context of promoting competition, basing our assessment of profitability on benchmarks from other markets and on BT and other CPs' historic profitability has the drawback of being based on the average costs and profitability of subscribers. In deciding on whether to try to acquire an additional subscriber, a rational CP will consider whether the discounted revenue it can earn from serving the subscriber is greater than the discounted marginal cost of serving the subscriber. Excluding the cost of acquiring the subscriber, the marginal cost is likely to be considerably lower than the average cost of serving the subscriber that we are measuring with our benchmarks. The cost of acquisition is therefore a key input in determining whether a marginal subscriber will be profitable.
- 8.27 Unlike the benchmarks we have calculated, cost information on a marginal subscriber is not readily available from accounting data. We have built a simple discounted cash flow model in order to try and assess the profitability of the marginal

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<sup>189</sup> This includes an allocation for BT Sport where this is provided free with BT broadband.

<sup>190</sup> Given the available data, we were not able to calculate the other CPs' profitability of offering SFV products.

subscriber faced by a notional CP. This model is described in detail in paragraphs A5.72 to A5.78. If this model calculates that a marginal subscriber is still profitable (i.e. the discounted revenues are greater than discounted costs) when a price reduction is introduced, then this would suggest that it is still possible for competition to develop.

- 8.28 We used this model to consider how profitable it will be to acquire marginal consumers under different scenarios depending on how successful our demand-side remedies are at reducing acquisition costs. In each of these cases we assume that our notional CP sets prices at a 10% discount to BT's prices. Our modelling suggests that even if we only achieve a modest (25%) reduction in acquisition costs it would still be profitable for CPs to acquire new standalone voice subscribers after a reduction in line rental prices of up to £7 (inc VAT) per month, which equates to a 37% discount on BT's prices.

### BT's Home Phone Saver

- 8.29 As discussed in Section 4, BT uses its Home Phone Saver tariff as a retention tool where it may lose its customers to competitors. As such, this provides a market indication of the price cut BT is willing to offer commercially where it perceives the threat of competition. The Home Phone Saver tariff is at least £5.50 lower than standard BT prices for a customer taking Anytime calls (and significantly more if various opt-in features are included – see Annex 8 for details).<sup>191</sup>

### **Conclusions on the options for the size of the price reduction**

- 8.30 If we consider that a reduction in prices is appropriate in order to protect consumers from prices that are above the competitive level, based on our assessment we believe that the maximum price reduction that we could introduce would mean a reduction in line rental of approximately £8-10 inc VAT per month. This size of reduction would be consistent with reducing prices to our estimate of BT's costs. However, such a reduction would be likely to seriously reduce the chance of competition emerging. Our competitive benchmarks and DCF analysis suggest a range of between £5 and £7 inc VAT a month would still allow profitability at a level that would be consistent with competition developing. The discount offered by BT on its Home Phone Saver product is consistent with this range.

## **Design of the price control**

### **Duration of price control**

- 8.31 We have considered what period of price control would allow certainty for consumers and CPs. The periodic re-setting of price controls allows the regulator to ensure that allocative efficiency objectives are met by setting the new control based on an up-to-date view of costs and revenues. In this case, we propose to use a three-year price control period that aligns with the market review period. This length of price control would give consumers and CPs certainty over BT's charges over the medium term.

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<sup>191</sup> Home Phone Saver Plus incorporates a number of additional inclusive services not automatically included with the standard line rental. These are relevant to the benefit of Home Phone Saver to customers if they are valued or would have otherwise been purchased with the standard tariff.

## Which customers are going to be affected by the price control?

- 8.32 As discussed in Section 3, we have identified two categories of purchasers of SFV services:
- Voice-only customers who do not purchase fixed broadband from any supplier; and
  - Split-purchase customers who purchase both fixed telephony and broadband but outside a bundle.
- 8.33 Both sets of consumers purchase the same SFV products and therefore, as we noted in Section 3, they both face the same detriment from the prices of SFV services being above the competitive level. Our provisional conclusion in Section 3 is that both of these sets of consumers are included in the same SFV markets. These provide reasons to include both sets of consumers in any price control.
- 8.34 Nevertheless, we have also considered whether there is a reason to exclude split purchasers from any price control. One possible reason is the potential for engagement remedies to be more effective in promoting competition for split purchasers than for voice-only consumers. Compared to voice-only customers, split purchasers have the added benefit of using the internet to compare and switch between products and CPs. In addition, there are many CPs offering competitive dual-play packages which split purchasers could adopt. However, even if, assisted by these circumstances, engagement remedies proved to be effective, in the absence of a price control, consumers who remain split purchasers are likely to continue to suffer detriment from BT's prices for SFV services being above cost in the significant period of time before the implementation of such remedies. Therefore, we propose that both sets of consumers purchasing SFV services would be included in a price control.
- 8.35 All other fixed voice services sit outside our market definition, such as those included in dual-play or other multi-play bundles, and will therefore not have a price control applied to them.
- 8.36 We have considered the risk that BT could look to recover lost revenue on SFV services by increasing prices in other markets (e.g. bundle prices for dual-play subscribers). However, we have not identified a clear causal mechanism to connect a reduction in prices in BT's SFV services with higher prices in other markets in which BT operates.<sup>192</sup> In particular, we believe that there is sufficient competition in these other markets to place a constraint on BT and stop it raising its prices in response to a price control for SFV services.

## How quickly should we reduce prices?

- 8.37 In considering how we would go about price controlling SFV services we have considered two options:

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<sup>192</sup> This is in contrast to some other situations, such as the causal mechanism that in principle connects reductions in mobile termination charges to higher prices offered by mobile operators to acquire mobile subscribers. This mechanism – often called the “waterbed effect” – is that a reduction in termination charges reduces the profitability to a mobile operator to acquire a new subscriber, because less profit is earned on incoming calls to that subscriber. In this case, however, it is not clear that the profitability of dual play or other services are reduced by a price cut for the services in the SFV markets.

- 8.37.1 **One-off reduction:** reduce prices using a one-off adjustment and hold them constant in real terms thereafter.
- 8.37.2 **Reduce prices using a glide path:** glide paths involve setting a control so that there is a gradual convergence of prices from the current level to the target level by the end of the control period.
- 8.38 When setting price controls, particularly where the control replaces existing controls, we have a strong preference for glide paths, rather than one-off adjustments. However, we do not always use glide paths and in some circumstances we have considered it more appropriate to use one-off adjustments.<sup>193</sup> For instance, we have considered making one-off adjustments where there is a risk to competition from distorted pricing signals, or where prices are significantly above or below cost for reasons other than efficiency or volume growth.
- 8.39 When moving between control periods a glide path approach provides greater incentives for cost efficiency improvement as it allows the firm to retain the benefits of cost reductions made under the previous price control. By contrast, one-off adjustments to charges reduce the effective regulatory lag, and hence the incentives to reduce costs.
- 8.40 Using a glide path also has the benefit of avoiding discontinuities in charges over time and leads to a more stable and predictable background against which investment and other decisions may be taken by both suppliers and consumers.
- 8.41 The drawback of using a glide path is that it allows prices to be above the target level for an extended period of time. In this case, that will mean SFV customers paying more than the target level for the duration of the glide path.
- 8.42 In this case, there is no existing price control and we therefore do not have the usual concerns regarding removing the incentive to reduce costs. Additionally, our analysis shown in Annex 5 suggests that the majority of the increase in BT's profitability over time has been caused by increases in the prices of line rental and calls rather than by cost reduction measures.
- 8.43 We estimate that using a glide path rather than a one-off adjustment would lead to BT's SFV customers paying around £60-80m more over the three-year price control period. If our engagement remedies led to competition emerging quickly then the impact of using a glide path would be reduced as competitive pressure pushed down prices. However, as discussed in Section 7, we expect that the process of developing, trialling and implementing engagement remedies could take up to two years, which would limit the time before the end of the price control period for them to have a material effect on competition.
- 8.44 Due to the potential for consumer harm during the price control period, we are proposing to impose a one-off reduction in prices. We recognise that some transition period is appropriate to allow BT sufficient time to implement price changes. We are therefore proposing that the one-off reduction to line rental prices occurs one month after the start of the price control period.

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<sup>193</sup> For instance, we made one-off adjustments to starting charges for Ethernet and TI services in the 2016 Leased Lines Charge Control (see Business Connectivity Market Review – Volume II, Section 7.4) [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0015/72312/bcmr-final-statement-volume-two.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0015/72312/bcmr-final-statement-volume-two.pdf)

## How should we price control SFV products?

- 8.45 As discussed in Section 4, when assessing pricing and profitability for SFV retail services, we have looked at line rental and call costs. When assessing options for which services to price control we have considered a number of trade-offs:
- 8.45.1 **Simplicity:** it should be clear to consumers what they can expect from a price control on retail services. Our price control should provide certainty to SFV customers in relation to what they will pay over the period of the price control.
- 8.45.2 **Flexibility:** over time, the products that consumers purchase change. For instance, we may expect the number of calls that subscribers make to change, or subscribers may start to purchase additional add-on services. We would want to price control services in such a way that BT can respond to market developments.
- 8.45.3 **Effectiveness:** our price control should prevent consumers being overcharged for SFV services. BT should not be able to rebalance its pricing structure in such a way that consumers are overcharged.

### A maximum cap or an average basket cap

- 8.46 In determining proposals for controlling prices we have considered:
- **Line rental charges only:** a cap on the maximum charge for line rental and pricing freedom for call charges and ancillary services; or
  - **A basket of line rental charges, call charges and ancillary services**<sup>194</sup>: a cap on the average revenue earned by BT across standalone line rental, calls services and ancillary services.
- 8.47 Line rental charges make up the majority of the cost for SFV customers.<sup>195</sup> Only price controlling line rental provides a simpler price control because we would be able to set a maximum cap on charges. A maximum price cap control provides certainty to consumers over their line rental prices and transparency in the compliance process.
- 8.48 However, there is a risk that if we do not include the price of calls and ancillary services in our price control, then BT would respond to a reduction in line rental charges by increasing the price of calls, call packages or ancillaries to SFV customers.
- 8.49 We believe that a basket control is the appropriate way to ensure our price control is effective. However, we believe there is benefit for consumers having certainty over what the new price control will mean for them. A one-off reduction to line rental also means that all SFV customers benefit by the same amount per line. We are therefore proposing to apply the first year one-off reduction to line rental charges only. We propose that all other call and ancillary products should be included in a basket for the first year.

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<sup>194</sup> Ancillary services are optional services that are provided alongside line rental. A full list of ancillary services can be found at the end of this section.

<sup>195</sup> From 2007/08 to 2015/16, line rental costs made up between 50% and 60% of the total cost of SFV customers' bills.



- 8.50 In the second and third year of the price control we propose that all services should be included in a single basket. However, for the reasons set out above, we would be concerned if the one-off reduction to line rental was undone by significant increase in line rental prices as prices were rebalanced. We are therefore proposing to place a sub-cap on line rental services to prevent unduly large increases in the line rental prices.
- 8.51 The basket control limits the maximum weighted average increase in prices in any given year. When determining the weighting of each service in the basket, we propose to use a prior year weighting approach. This approach sets basket weights equal to the proportions of basket revenue accruing to the relevant services in the year prior to the one in which the price change occurs. By using prior year weights, we allow BT to plan its price changes in a given year with confidence that it can assess whether it will meet the overall basket control.

### Indexation of the price control baskets

- 8.52 In addition to reducing SFV prices in year 1 of the price control, we will need to decide how prices should be allowed to change over time. Over time, costs may increase due to general inflation, or they may decrease as operators find efficiency savings in the way they provide services. We have not forecasted costs and revenues over the price control period and so do not have new cost estimates to adjust to in each year of the price control. However, as discussed in Annex 5, we do not expect a significant deterioration in BT's profitability during the price control period. Therefore, we believe broadly flat prices across the basket over the price control period would be appropriate.
- 8.53 In determining the level of indexation we have considered:
- **A flat nominal cap:** average basket prices remain the same over the price control period; or
  - **A flat real cap:** average basket prices are allowed to increase each year by the consumer price index (CPI).
- 8.54 We recognise that there is a risk to operators from general economy-wide inflation and therefore we believe it is appropriate to allow BT to respond to this inflation by increasing its prices where we have determined a specific level of profitability. If we did not allow BT to increase prices in line with inflation, there is a risk that prices, and the associated level of profitability, could fall below the level on which we based our assessment.
- 8.55 If we decided to propose the use of a safeguard cap, then we believe a flat nominal price cap is more appropriate. We would not have the same concern regarding profitability falling below a particular level given that our expectation would be that prices would fall as competition emerged. We are therefore not targeting a particular level of profitability for BT or other CPs and if we allowed prices to increase with inflation, we would unnecessarily allow additional consumer detriment while competition is developing.
- 8.56 The CPI is a widely recognised measure of inflation and forms the headline figure for multiple government agencies. It is also the measure that the Bank of England uses as its target for economy-wide inflation and is recognised as an official statistic by the

UKSA.<sup>196</sup> We therefore believe it appropriate to allow the average price of the basket of SFV services to increase by the CPI each year.

- 8.57 We are proposing to place a sub-cap on line rental in the price control basket in order to stop line rental prices increasing significantly over time. However, this does not mean that we wish to remove all flexibility for BT to increase line rental prices. Indeed, there may be good reasons for us to give extra flexibility for BT to increase line rental prices if we believed that changes in the market meant lower levels of profitability for BT than we considered when setting the controls. For instance, over time call volumes have been decreasing and we expect them to decrease further in the future. In Section 3, we recognise that the pricing constraint on SFV calls may be greater than for SFV access. BT may wish to decrease call prices in the future in response to this competitive pressure. If we do not allow sufficient flexibility on the line rental price in the price control basket, BT would not be able to reduce call prices without undershooting the price control target.
- 8.58 In order to take account of this, we have considered either aligning the line rental sub-cap with the price control basket and allowing it to increase by the CPI over time, or allowing it to increase by more than CPI.
- 8.59 We have considered the extent to which BT may wish to reduce call prices during the price control period. As discussed in Section A5.63 to A5.69, we have examined the proportion of total SFV revenue that are made up of SFV call revenue and how SFV revenue has changed over time. We believe allowing BT the ability to increase prices in the line rental sub-basket by up to CPI+2.5% would be sufficient pricing flexibility to allow for any change in market circumstances. We estimate that this would allow BT to reduce call prices by approximately 7% per year in nominal terms and still set price at the price control cap.
- 8.60 If BT chose to increase prices in the line rental sub-basket by the full permitted amount of CPI+2.5%, it would need to reduce call prices in real terms to comply with the cap on the overall basket of CPI. A sub-cap of CPI+2.5% on line rental would not therefore allow BT to recover additional revenue and should ensure that price rises for consumers do not exceed CPI when other services are taken into account.
- 8.61 For the first year of the price control, we propose to assess whether BT has set prices that comply with the control by comparing them to prices in place on the 2 April 2017, rather than the prices in place for the period immediately preceding the start of the price control. We propose to do this in order to avoid giving BT the opportunity to game the price control by upwardly adjusting its prices in the period between the publication of this consultation and the start of any price control.

#### Which version of line rental should we price control?

- 8.62 As discussed in Section 3, we have included all SFV access products in the market definition excluding BT Basic. These products are Standard Line Rental, Standard Line Rental Saver, Home Phone Saver and Line Rental Plus.<sup>197</sup> We propose to include the Standard Line Rental and Standard Line Rental Saver in the price control.

<sup>196</sup> The United Kingdom Statistics Authority is the body class with assigning statistics their classifications.

<sup>197</sup> These line rental products are discussed in more detail in section A5.37.

- 8.63 Although we have included Home Phone Saver and Line Rental Saver in our market definition, both products have quite different pricing structure and level of profitability to Standard Line Rental standalone voice products. As discussed above, the discounts reflected in Home Phone Saver are already at a level similar to or larger than those available to customers on the standard tariff if we reduce standard line rental by £5-£7.<sup>198</sup> We therefore believe that Home Phone Saver is priced in a way that is broadly consistent with the prices in the price control option designed to be consistent with competition developing. The Line Rental Plus package is also sold at a discount that is similar to the reduction in line rental that we are proposing. We would therefore propose not to include Home Phone Saver or Line Rental Plus in the price control for the price reduction consistent with promoting competition option.
- 8.64 However, under our maximum price reduction option (i.e. a reduction in the price of standard line rental of £8-10), Home Phone Saver would require a reduction in prices to be consistent with the price of standard SFV services. We would therefore propose to include Home Phone Saver in the price control. However, due to the discount offered by BT on the Home Phone Saver product, reducing its price by £8-10 may force BT to sell it at or below cost. A price reduction that reduces the level of profitability on Home Phone Saver to the benchmark level of profitability on standard line rental (i.e. a ROS margin of around 10%) would lead to a one-off reduction of £[>] (inc VAT) in the price of the Home Phone Saver product.<sup>199</sup>
- 8.65 The Standard Line Rental Saver product provides a 10% discount on the Standard Line Rental price for those consumers willing to pay their line rental for a year in advance. We believe that this product should benefit from a one-off reduction in line rental prices. We therefore propose to set the Standard Line Rental Saver product price at a 10% discount to the price we set for Standard Line Rental in the first year of the price control. For those customers who have paid for Line Rental Saver for the period of up to 12 months in advance of the start of the price control, we propose that they receive a discount on the remainder of their contract equal to the number of complete months left on their contract multiplied by the monthly reduction in the Standard Line Rental Saver price.
- 8.66 We believe that in subsequent years, Standard Line Rental will constrain the price of Standard Line Rental Saver. We therefore do not believe it is necessary to continue including Standard Line Rental Saver in years 2 and 3 of the price control and propose to exclude it.

#### Which ancillary products should we include in the price control?

- 8.67 BT currently offers a number of different ancillaries alongside line rental and as part of its call packages. Some of these ancillary services simply enhance the caller experience, such as a voice mail service and the equivalent of this service can be obtained through alternative competitive means. Other services are, like the Line Rental Saver, sold as a discount on a core service and will by necessity be controlled by a constraint on the core service. We, therefore, do not consider that we need to price control these “services”.

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<sup>198</sup> When ancillary services are also taken into account, Home Phone Saver 2019 offers a £5.50 to £13.05 per month reduction on similar package of standard SFV products (see paragraph A.114-A.116 Figure A8.38).

<sup>199</sup> See Annex 5.

8.68 However, there are a number of ancillary services that form an essential part of customers' SFV services. For example, we consider those ancillaries that have a consumer protection function (such as anonymous call reject and choose to refuse) form an essential part of fixed voice services. With this in mind, we would be concerned of a risk that BT could inflate the prices of this type of services to recover revenues lost from any one off adjustment and price cap within a basket. We therefore propose to include these essential ancillary service in the price control basket.

8.69 Below we set out a full list of BT ancillary services that we consider to be essential. We have identified the following services as those we propose include in any price control basket because they form an essential part of consumers' SFV services.

Line Rental, which includes:

Service	Description
<b>Standard Line Rental or Line Rental</b>	Price paid per month for line
<b>BT Smart Talk</b>	Smartphone app which allows calls on mobile at BT call plan rates.
<b>BT Call Protect</b>	Sends user defined calls to a junk voicemail.
<b>Permanent withhold number</b>	Number not available or displayed when calling.
<b>Bar Three Way Calling</b>	Prevents anyone using Three Way Calling from customer's phone.
<b>Block Ring Back</b>	Prevents callers booking a Ring Back to the customer's line.
<b>1471</b>	Provides the last number that called.
<b>1470</b>	Display number on a per call basis

Ancillary services we consider to be essential, include:

Service	Description
<b>Unlimited Anytime Calls (not including Line Rental)</b>	Calls made at any time of day.
<b>Calls to BT Mobile Consumer numbers</b>	Calls to all BT Mobile consumers at any time of day.
<b>Calls to all other UK Mobile numbers</b>	Calls to all other UK Mobile numbers, including non-BT Mobile Consumer numbers at any time of day.
<b>Calls to UK National and local numbers</b>	
<b>Calls to 0845 &amp; 0870 Numbers</b>	Calls to numbers with these prefixes at any time of day
<b>Calls to Service Numbers 090, 118 and other 084 &amp; 087</b>	Calls to numbers with these prefixes at any time of day
<b>Calls to International numbers</b>	Calls to numbers
<b>Friends &amp; Family International</b>	
<b>International Freedom</b>	
<b>Calls to 070/076/055/056 number ranges</b>	Calls to numbers with these prefixes at any time of day.
<b>Choose to Refuse</b>	Block up to ten telephone numbers.
<b>Anonymous Call Reject</b>	Stop calls from people who have withheld their number.

<b>BT Privacy at Home</b>	Registers customer for the Telephone Preference Service to stop unwanted sales calls.
<b>BT Privacy with Caller Display</b>	As above together with showing number of person calling (requires compatible phone)
<b>Call Barring</b>	Allows customer to stop certain types of calls being made from the phone line.
<b>Call Diversion</b>	Divert incoming calls to another phone number.
<b>Call Waiting</b>	While on a call a beep sounds when another call is incoming.

## Monitoring compliance with the price control

- 8.70 In order to carry out our duties it is important that financial information is available on the services and markets that we regulate. The availability of this information helps us understand the volumes, revenues, costs and returns of services and markets, which allows us to monitor the impact and effectiveness of, and (for certain remedies) compliance with, the remedies imposed as part of a market review. We propose that BT is required to supply information in order for us to monitor its compliance with the control. BT would be required to provide this information annually to Ofcom, three months after the end of the price control year.<sup>200</sup>
- 8.71 In the 2014 Regulatory Financial Reporting Statement we said that “BT must produce non-confidential compliance schedules for each regulated market. These non-confidential compliance statements must be published on BT’s website in the same location as the Published Regulatory Financial Statements and at the same time as the confidential compliance statements are provided to Ofcom”.<sup>201</sup> Publication of compliance statements helps provide assurance about BT’s compliance with price controls. We therefore propose to require BT to publish non-confidential compliance schedules for the retail voice only price controlled services on its website alongside the public version of the RFS.

## Consultation questions

*Question 8.1: Do you agree with our approach to determining the options for the level of price controls for Standalone Fixed Voice services? If not, please give your reasons.*

*Question 8.2: Do you agree with our proposed basket structure if implementing a price control for Standalone Fixed Voice services? In particular, do you agree with the need for a separate sub-cap on the Line Rental within the basket? If not, please give your reasons.*

*Question 8.3: Do you agree that it would be appropriate to allow the prices in a price control basket to rise by up to consumer price index (CPI)? If not, please give your reasons.*

*Question 8.4: Do you agree that we should exclude Home Phone Saver and Line Rental Plus from the price control? If not, please give your reasons.*

<sup>200</sup> This requirement is set out in Condition 2.7 of Annex 9.

<sup>201</sup> See 2014 Regulatory Financial Reporting Statement (Section 4.49).

[https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0025/78460/financial-reporting-statement-may14.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0025/78460/financial-reporting-statement-may14.pdf)

*Question 8.5: Do you agree that it is appropriate for the Line Rental sub-cap to have greater price flexibility than the overall price cap to allow BT to rebalance pricing between the line rental and call prices? If not, please give your reasons.*

*Question 8.6: Do you agree with the services we are proposing to include in a price control remedy basket for Standalone Fixed Voice services? If not, please set out your alternative proposals and please give your reasons.*

## Section 9

# Our proposals

## Introduction and summary

- 9.1 In this section, we set out our package of proposed remedies to address consumer detriment arising from BT's SMP in SFV access and calls. As discussed in Section 6, we consider that we cannot rely on wholesale remedies to address competition concerns associated with BT's SMP, and that we need to respond directly with regulation of BT's retail activity. We also set out our consideration of the relevant legal tests that we need to satisfy in imposing regulation.
- 9.2 We are proposing a package of remedies consisting of measures to promote competition by encouraging greater engagement in the market, and a price control on BT to address the consumer detriment we have identified.
- 9.3 Specifically, we propose to set a three-year retail price control on BT's standalone fixed voice services of the following form:
- 9.3.1 An initial one-off price reduction of the line rental by between £5 and £7 per month and controls on line rental in years 2 and 3 of between CPI-0 and CPI+2.5%;
- 9.3.2 A CPI-0 basket control on all other core<sup>202</sup> existent standalone fixed voice services available to residential customers' charges in each year
- (the basket will also include the line rental in years 2 and 3 though subject to a sub-cap to avoid significant rebalancing between call charges and the line rental, which might harm consumers who make fewer calls).
- 9.4 We propose that the price control will apply to all BT customers who purchase the relevant standalone voice services. This includes all the customer segments of voice-only, split-supplier and split-service customers (i.e. whether or not they purchase fixed broadband from BT or third parties outside a bundle). It will not apply to voice services sold by BT as part of a bundle of services which include broadband.
- 9.5 In order to encourage greater engagement in the market, we also propose to impose an obligation on BT to:
- 9.5.1 cooperate with Ofcom in the testing or trialling of different measures to provide information to its customers; and
- 9.5.2 if justified in the light of that evidence, to implement measures in the manner and form as Ofcom may direct.
- 9.6 The level of the one-off adjustment in the price control has been chosen so as to be consistent with promoting competition to BT in this market. In particular, we have set a price which we consider reduces, to a significant extent, direct consumer detriment

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<sup>202</sup> We propose to exclude BT's Home Phone Saver from the price control as this is already significantly discounted. BT Basic does not form part of our relevant market definition and is therefore also excluded from the price control.

in the form of high prices, while also allowing BT's competitors to win new customers from BT and make an adequate return from serving those customers, taking into account the potential reduction in acquisition arising from measures to encourage greater customer engagement.

## Introduction to assessment of options

- 9.7 As set out in Section 6, we consider that SFV customers suffer detriment arising from BT's SMP, and we distinguish between (a) direct detriment due to prevailing market prices being above the competitive level; and (b) indirect detriment arising from a lack of competition in the market. We have presented estimates that the price-related detriment is at least £150 million and up to £340 million per year, while we have not quantified the indirect detriment.
- 9.8 A suitably designed cost-based price control could largely address the direct price detriment we have identified. However, a cost-based price control would not promote competition.
- 9.9 As we remain of the view that in the medium-term competition offers the potential to deliver benefits for consumers in terms of price, choice and available services, we therefore need to consider whether there is scope for measures to promote competition to be effective in this market. If so, we also need to consider the interaction between such measures and a price control. The right balance of reliance on competition promotion remedies and a price control depends, in part, on our expectation of the effectiveness and timeliness of measures to promote competition.

## Remedies Options

- 9.10 We have considered the following combination of remedies to address the concerns identified in this document:
- Option 1: Measures to promote competition alone (i.e. no price control).
  - Option 2: Measures to promote competition, plus a safeguard cap on BT's prices at current levels.
  - Option 3: Maximum price reduction on BT line rental (£10), followed by a price freeze (with no measures to promote competition).
  - Option 4 (Preferred Option): Measures to promote competition, plus a price reduction on BT line rental consistent with promoting competition (£5 to £7), followed by a price freeze in real terms.

### Option 1: measures to promote competition alone

- 9.11 Under this option, we would impose an obligation on BT which would allow us to impose measures to promote competition, but we would not impose a price control.
- 9.12 In Section 7, we concluded that the most appropriate potential remedies to promote competition are those which make it easier for consumers to engage in the market, namely:
- 9.12.1 Communications to BT customers aimed at providing them with useful and suitably tailored information about alternative services available in the market which might be more suitable and better value for them;



- 9.12.2 Communications to BT customers making them aware of the process for switching SFV provider, and particularly reassuring them about aspects of the process,<sup>203</sup> such as the ability to switch between providers without contacting BT, the ability to retain their existing phone number (if not moving home), and that they will not need new equipment or face a significant interruption to their service;
- 9.12.3 Introduction of a decision point, by requiring BT to provide a prompt for consumers to consider switching their SFV provider or the tariff they use from their existing one;
- 9.12.4 Remedies to increase the ease of responding to a potential change in tariff or switch, such as the provision of tear-off slips which consumers could sign and return in a pre-paid envelope to either BT or another provider if they wanted to change BT tariff or engage with another supplier.
- 9.13 The advantage of this option is that it would ensure that BT's competitors have the greatest possible incentive to compete for SFV customers, both in terms of prevailing prices and hence returns associated with winning customers, and also in terms of signalling to BT's competitors that we did not intend to intervene in the market by cutting prices.
- 9.14 If measures to promote competition were successful, we would expect these to lead to a reduction in prices over time to competitive levels (this would be one of the key success criteria). In the extreme case – where acquisition costs are materially lowered and providers start to compete aggressively to win and retain customers – this could in principle lead to lower prices than we are considering in the context of price controls.
- 9.15 However, such a package of remedies would do nothing to protect consumers from price increases in the short term and we recognise that success in promoting competition may be challenging due to:
- 9.15.1 the age of SFV customers, lower-than-average rate of online adoption, and relatively limited share of household budget accounted for by SFV services;
- 9.15.2 the fact that brand loyalty to BT is strong;
- 9.15.3 some CPs have already stopped competing in the market, while declining customer numbers and limited opportunities to upsell mean this segment is unlikely to be a priority for most CPs; and
- 9.15.4 the limited evidence in other markets of the effectiveness of such remedies
- 9.16 Even in the best-case scenario, it would likely take some time for us to trial, evaluate and implement a package of measures to promote competition, and for greater competition to develop in the standalone fixed voice markets.
- 9.17 For example, if measures to promote competition took two years to start to have an effect, then we estimate that the consumer detriment would be about £200 million to £425 million at current prices<sup>204</sup> (and we note that the delay before the market

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<sup>203</sup> If switching within the Openreach copper network.

<sup>204</sup> See Section 6 where we discuss consumer detriment.

became effectively competitive could be materially longer). This estimate takes into account that the base of standalone voice customers is declining over time. In addition, providers are continuing to raise prices, so in the absence of any price cap it is likely that consumer detriment per line would increase in the coming years.

- 9.18 Finally, as discussed Section 7, we also consider that there are material risks that such a package of remedies would not ultimately be effective in promoting effective competition.

### **Option 2: measures to promote competition, and a safeguard cap**

- 9.19 Option 2 differs from Option 1 in the inclusion of a safeguard cap, which would remove the risk of detriment increasing further in the coming years. A safeguard cap would be based on prices as at a fixed date. However, this would not address the existing high level of detriment in the market, which measures to promote competition may not address in a timely fashion, if they do so at all. So, for the reasons set out under Option 1, we do not consider this option is appropriate.

### **Option 3: maximum price reduction on BT line rental, followed by a price freeze**

- 9.20 A £8-10 price cut on BT's line rental, followed by a price freeze, would remove all current price related consumer detriment we have identified arising from high prices in the provision of SFV services.
- 9.21 We expect that if we imposed such a price cut, other CPs would face pressure to reduce their prices to new and/or existing SFV customers since BT is a price leader and customers could switch to BT at the price-controlled level (or potentially to another provider).<sup>205</sup>
- 9.22 However, we expect that in this case these other CPs would not have an adequate incentive to compete for new customers, as prevailing prices (based on the price control on BT) would not allow them a sufficient return to cover new customer acquisition costs. This might also mean some providers might even withdraw from existing supply. For this reason, if we imposed a price control at this level we would not impose an obligation on BT in relation to measures to promote competition, as we would not expect any such measures to have a reasonable chance of success.
- 9.23 However, given the benefits we consider competition offers, we do not consider this to be a desirable outcome if there is a reasonable prospect of improving competition in this market.

### **Option 4 (Preferred Option): measures to promote competition, and a price reduction on BT line rental consistent with promoting competition, followed by a price freeze**

- 9.24 While there are challenges to introducing successful measures to promote competition in this market, there is also a case for exploring whether such measures can be successful, in particular given the presence of competitors who are interested in acquiring – or actively seeking to acquire – more SFV customers.

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<sup>205</sup> Whilst current rates of switching are low, the evidence suggests that rates of switching are materially higher for SFV customers of other CPs than for BT's customers (see Annex 8).

- 9.25 If we are to explore the scope for such measures to succeed, in our view this needs to be balanced against the need to protect consumers from detriment. A price cut of £5 to £7 in the monthly line rental would substantially reduce consumer detriment in this market.<sup>206</sup> The choice of price cut within this range would depend on our judgement about the most appropriate balance between promoting competition and protecting consumers, as well as any refinement in our analysis of competitive benchmarks and profitability (discussed in Section 8 and Annex 5) following responses to this document.
- 9.26 We have derived the size of this range for the price cut on the basis that it is consistent with promoting competition. However, we recognise that there is still a risk that other CPs would be deterred from engaging in the market, by the reduction in margins and potentially the prospect of future price regulation.
- 9.27 We also note the potential interaction with our proposed change in regulation of a key wholesale input in the 2016 NMR Consultation, to change from a charge control for WLR to a fair and reasonable charges obligation (providing BT with greater flexibility in setting WLR charges).<sup>207</sup> We are proposing this change to wholesale regulation on the basis of our assessment that BT's market power in wholesale lines is likely to be lower than it was when we last reviewed the market, as a result of growing alternatives to traditional fixed voice services, particularly increased competition from infrastructure based competitors. Nevertheless, this proposed change is clearly a material consideration for existing and potential suppliers of retail SFV services.
- 9.28 While, as we have argued, BT has SMP in the standalone fixed voice markets there are some willing competitors with the potential to become stronger rivals to BT.
- 9.29 As discussed in Section 6, we consider that there are benefits to competition in service provision that go beyond simply the service price. Telephony services are not a simple commodity product and absent competition there is a risk of a slow decline in diversity of service options and even quality.
- 9.30 On balance we do not at this stage favour giving up on the prospect of promoting competition and we consider that we should trial and test the measures discussed above to improve customer engagement alongside price controls including a significant price cut of £5-7 per month to mitigate consumer detriment. In the event that we consider in future that our initiatives do not lead to a material improvement in competition, and we conclude that they were not likely to do so, then we would expect to reconsider this position.

## Proposed retail regulation

### Promoting competition

- 9.31 The detailed justification for our proposal to set information remedies to encourage competition is set in Section 7. In summary, the proposals are:

<sup>206</sup> Beyond the reduction arising from the declining base of standalone voice customers.

<sup>207</sup> This proposed change in regulation of WLR is less relevant to the other options. For Options 1 and 2, the price of WLR is unlikely to be a major constraint on growth in competition. For Option 3, promotion of competition is not important.

- An obligation on BT to act in accordance with Ofcom’s directions requiring it to produce, provide or distribute information, or make specific communications to, its customers (“Communications Requirements”);
- Our directions may include the content, format and frequency of the information to be provided;
- They may also specify the identity of the sender, the group of customers that will receive the communications or require the provision of information about BT’s prices and the prices of other communications provider. Ofcom’s directions may also require BT to provide response cards, tear off slips and addressed envelopes to its customers; and
- An obligation on BT to cooperate in the development and design of Communications Requirements and to provide information to Ofcom.

## Price control

9.32 The detailed justification for the structure of the price control is set out in Section 8. Given our preference for Option 4, our proposed price control will take the form of:

- a basket control on all core SFV services, based on BT prices as at 2 April 2017, allowing BT to increase price by up to CPI in each year of the control;
- a one-off adjustment to the line rental of between £5-£7 per month, subject to our final assessment, taking into account responses to this consultation, of the balance between promoting competition and protecting consumers. The adjusted line rental price will remain in place for the remainder of year one;
- a sub-cap on the line rental in years two and three of the control of between CPI and CPI+2.5%, subject to our final assessment, taking into account responses to this consultation, on the appropriateness of allowing BT some freedom to rebalance prices as between the line rental and calls in the face of continuing declines in retail calls;
- a requirement on BT to reduce the price of its line rental advance payment product – Line Rental Saver – by a proportionate amount to the reduction in the line rental and refund existing purchasers of this product for any period of the pre-payment that overlaps with the price control period;
- an annual compliance report to confirm adherence to the price control; and
- BT will have to adhere to a fixed date for the commencement of the price control but have at least one month after the statement date to implement the new controls.

## Regulatory reporting

9.33 As set out in Section 2, section 91(6) provides that, when imposing regulatory controls on tariffs, Ofcom shall also set the necessary and appropriate obligations relating to the use of accounting systems. We are considering whether such obligations are required for this market and if we consider they are we will consult separately.

## Legal tests

- 9.34 Section 91 authorises the imposition of SMP conditions in relation to the provision of retail services. For the reasons set out below we are satisfied that the conditions we are proposing to impose on BT meet the various tests set out in the Act.
- 9.35 In making our proposals, we have considered, in particular, our duties under section 3 of the Act. We consider that by addressing the direct and indirect consumer detriment that we have identified, our proposed regulations will further the interests of citizens in relation to communications markets and further the interests of consumers in relevant markets, including by promoting competition. We have also had particular regard to our duty under section 3(4)(i) and the needs of the elderly who form a large part of the relevant retail markets.
- 9.36 In making our assessment, we have also taken into account the Community requirements set out in Section 4 of the Act and Article 8 of the Framework Directive. We consider that our proposals will promote competition in relation to the provision of electronic communications services by ensuring that users derive maximum benefit in terms of choice, price and quality.
- 9.37 In addition, we have considered whether our proposals satisfy the test set out in section 47 of the Act, namely that SMP obligations must be:
- 9.37.1 objectively justifiable in relation to the networks, services, facilities to which they relate;
  - 9.37.2 not such as to discriminate unduly against particular persons or against a particular description of persons;
  - 9.37.3 proportionate to what the conditions are intended to achieve; and
  - 9.37.4 transparent in relation to what is intended to be achieved.

## Communication Requirement

- 9.38 Condition 1 is specifically aimed at promoting competition by reducing the acquisition costs to communications providers through greater engagement of consumers in this market. We consider this remedy is:
- objectively justifiable in light of the market failure we have identified and our provisional conclusion that there is still potential for competition in the SFV market that can deliver good outcomes for consumers. Our proposed measure is also appropriate in light of our provisional conclusion that wholesale remedies are not sufficient to address the identified harm;
  - not unduly discriminatory, in that it will only apply to BT, which we have identified as the only CP having SMP in the relevant markets;
  - transparent in that it is clear what it is seeking to achieve – the promotion of competition through greater consumer engagement – and in setting out what BT is or may be required to do in future; and
  - proportionate, in that we have identified a market failure and the condition is targeted specifically to the area for which regulation is required. Our proposed condition is the least onerous means of achieving the objective we have

identified in that it allows for the trialling of the least onerous engagement remedies.<sup>208</sup>

### Price control for exchange line services

9.39 Condition 2 has been proposed in order to reduce the consumer detriment we have identified in this market through regulation of the maximum price the dominant provider can provide to SFV customers. We consider this remedy is:

- objectively justifiable, in light of the direct consumer detriment we have identified and the inadequacy of wholesale regulation in addressing that harm identified in section 6;
- not unduly discriminatory, in that it will only apply to BT, which we have identified as the only CP having SMP in the relevant markets. Our proposed remedy will also affect all BT customers that purchase SFV in the relevant markets;
- transparent in that it is clear what it is intended to achieve and in setting out the controls that we are proposing to implement on BT's prices; and
- proportionate, in that it seeks to strike the right balance between promoting competition and protecting consumers from harm and is the least onerous means of achieving that balance.

9.40 Lastly, we have considered, as required by section 91(2), whether wholesale regulation alone would have allowed us to perform our duties under section 4 of the Act. For the reasons set out in this section, we are satisfied that wholesale remedies have not been, and are not likely to be, sufficient in achieving those aims. Accordingly, we consider the legal tests set out in the Act are satisfied.

### Consultation questions

*Question 9.1: Do you agree with our proposed set of remedies for the Standalone Fixed Voice services markets, that is a price control, with a one-off adjustment set with reference to the costs of BT competitors in this market, and an obligation on BT to work with us to explore and ultimately implement information options to promote competition? If not please set out your reasons.*

*Question 9.2: Do you agree that BT should have at least one month after the date of the statement to implement the new price structure? If not, please set out your reasons.*

*Question 9.3: Do you have any additional comments on our analysis or conclusions in this consultation?*

<sup>208</sup> We note that any direction made by Ofcom in relation to BT's compliance with the proposed condition will be subject to separate consultation.

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**ANNEX 6**

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# The review of the market for standalone landline telephone services - Annexes

Provisional conclusions

**Consultation**

**Publication date:** 28 February 2017

**Closing Date for Responses:** 9 May 2017



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## Annex 1

# Responding to this consultation

## How to respond

- A1.1 Ofcom would like to receive views and comments on the issues raised in this document **by 5pm on 9 May 2017**.
- A1.2 We strongly prefer to receive responses via the online form at <https://www.ofcom.org.uk/consultations-and-statements/category-1/review-of-landline-telephone-services>. We also provide a cover sheet (<https://www.ofcom.org.uk/consultations-and-statements/consultation-response-coversheet>) for responses sent by email or post; please fill this in, as it helps us to maintain your confidentiality, and speeds up our work. You do not need to do this if you respond using the online form.
- A1.3 If your response is a large file, or has supporting charts, tables or other data, please email it to [retailvoicemarketreview@ofcom.org.uk](mailto:retailvoicemarketreview@ofcom.org.uk), as an attachment in Microsoft Word format, together with the cover sheet (<https://www.ofcom.org.uk/consultations-and-statements/consultation-response-coversheet>).
- A1.4 Responses may alternatively be posted to the address below, marked with the title of the consultation.
- Catherine Warhurst  
Ofcom  
Riverside House  
2A Southwark Bridge Road  
London SE1 9HA
- A1.5 If you would like to submit your response in an alternative format (e.g. a video or audio file), please contact Catherine Warhurst on 020 7981 3382, or email [catherine.warhurst@ofcom.org.uk](mailto:catherine.warhurst@ofcom.org.uk).
- A1.6 We do not need a paper copy of your response as well as an electronic version. We will acknowledge receipt if your response is submitted via the online web form, but not otherwise.
- A1.7 You do not have to answer all the questions in the consultation if you do not have a view; a short response on just one point is fine. We also welcome joint responses.
- A1.8 It would be helpful if your response could include direct answers to the questions asked in the consultation document. The questions are listed at Annex 3. It would also help if you could explain why you hold your views, and what you think the effect of Ofcom's proposals would be.
- A1.9 If you want to discuss the issues and questions raised in this consultation, please contact Catherine Warhurst on 020 7981 3382, or by email to [catherine.warhurst@ofcom.org.uk](mailto:catherine.warhurst@ofcom.org.uk).

## Confidentiality

- A1.10 Consultations are more effective if we publish the responses before the consultation period closes. In particular, this can help people and organisations with limited resources or familiarity with the issues to respond in a more informed way. So, in the interests of transparency and good regulatory practice, and because we believe it is important that everyone who is interested in an issue can see other respondents' views, we usually publish all responses on our website, [www.ofcom.org.uk](http://www.ofcom.org.uk), as soon as we receive them.
- A1.11 If you think your response should be kept confidential, please specify which part(s) this applies to, and explain why. Please send any confidential sections as a separate annex. If you want your name, address, other contact details or job title to remain confidential, please provide them only in the cover sheet, so that we don't have to edit your response.
- A1.12 If someone asks us to keep part or all of a response confidential, we will treat this request seriously and try to respect it. But sometimes we will need to publish all responses, including those that are marked as confidential, in order to meet legal obligations.
- A1.13 Please also note that copyright and all other intellectual property in responses will be assumed to be licensed to Ofcom to use. Ofcom's intellectual property rights are explained further at <https://www.ofcom.org.uk/about-ofcom/website/terms-of-use>.

## Next steps

- A1.14 Following this consultation period, Ofcom plans to publish a statement at the turn of the year.
- A1.15 If you wish, you can register to receive mail updates alerting you to new Ofcom publications; for more details, please see <https://www.ofcom.org.uk/about-ofcom/latest/email-updates>

## Ofcom's consultation processes

- A1.16 Ofcom aims to make responding to a consultation as easy as possible. For more information, please see our consultation principles in Annex 2.
- A1.17 If you have any comments or suggestions on how we manage our consultations, please email us at [consult@ofcom.org.uk](mailto:consult@ofcom.org.uk). We particularly welcome ideas on how Ofcom could more effectively seek the views of groups or individuals, such as small businesses and residential consumers, who are less likely to give their opinions through a formal consultation.
- A1.18 If you would like to discuss these issues, or Ofcom's consultation processes more generally, please contact Steve Gettings, Ofcom's consultation champion:

Steve Gettings  
 Ofcom  
 Riverside House  
 2a Southwark Bridge Road  
 London SE1 9HA  
 Email: [corporationsecretary@ofcom.org.uk](mailto:corporationsecretary@ofcom.org.uk)

## Annex 2

# Ofcom's consultation principles

## Ofcom has principles that it follows for every public written consultation:

### Before the consultation

- A2.1 Wherever possible, we will hold informal talks with people and organisations before announcing a big consultation, to find out whether we are thinking along the right lines. If we do not have enough time to do this, we will hold an open meeting to explain our proposals, shortly after announcing the consultation.

### During the consultation

- A2.2 We will be clear about what we are consulting, why, on what questions and for how long.
- A2.3 We will make the consultation document as short and simple as possible, with a short summary.
- A2.4 We will try to make it as easy as possible for people to give us a written response.
- A2.5 If the consultation is complicated, we may provide a short Plain English / Cymraeg Clir guide, to help smaller organisations or individuals who would not otherwise be able to spare the time to share their views.
- A2.6 We will consult for up to ten weeks, depending on the potential impact of our proposals.
- A2.7 A person within Ofcom will be in charge of making sure we follow our own guidelines and aim to reach the largest possible number of people and organisations who may be interested in the outcome of our decisions. Ofcom's Consultation Champion is the main person to contact if you have views on the way we run our consultations.
- A2.8 If we are not able to follow any of these principles, we will explain why.

### After the consultation

- A2.9 We think it is important that everyone who is interested in an issue can see other people's views, so we usually publish all the responses on our website as soon as we receive them. After the consultation we will make our decisions and publish a statement explaining what we are going to do, and why, showing how respondents' views helped to shape these decisions.

## Cover sheet for response to an Ofcom consultation

### BASIC DETAILS

Consultation title:

To (Ofcom contact):

Name of respondent:

Representing (self or organisation/s):

Address (if not received by email):

### CONFIDENTIALITY

Please tick below what part of your response you consider is confidential, giving your reasons why

Nothing

Name/contact details/job title

Whole response

Organisation

Part of the response

If there is no separate annex, which parts?

If you want part of your response, your name or your organisation not to be published, can Ofcom still publish a reference to the contents of your response (including, for any confidential parts, a general summary that does not disclose the specific information or enable you to be identified)?

### DECLARATION

I confirm that the correspondence supplied with this cover sheet is a formal consultation response that Ofcom can publish. However, in supplying this response, I understand that Ofcom may need to publish all responses, including those which are marked as confidential, in order to meet legal obligations. If I have sent my response by email, Ofcom can disregard any standard e-mail text about not disclosing email contents and attachments.

Ofcom seeks to publish responses on receipt. If your response is non-confidential (in whole or in part), and you would prefer us to publish your response only once the consultation has ended, please tick here.

Name

Signed (if hard copy)

## Annex 3

## Consultation questions

*Question 3.1: Do you agree with our provisional conclusion that there is a separate market for Standalone Fixed Voice residential access which includes both voice-only and split purchase consumers? Please provide reasons and evidence in support of your views.*

*Question 3.2: Do you agree with our provisional conclusion that there is a separate market for Standalone Fixed Voice residential calls? Please provide reasons and evidence in support of your views.*

*Question 4.1: Do you agree with our provisional conclusion that, during the period covered by this market review, BT will have Significant Market Power in the Standalone Fixed Voice access market? Please provide reasons and evidence in support of your views.*

*Question 5.1: Do you agree with our provisional conclusion that, during the period covered by this market review, BT will have Significant Market Power in the Standalone Fixed Voice calls market? Please provide reasons and evidence in support of your views.*

*Question 7.1: Do you agree with the need to trial and test engagement remedies before implementation? Please explain your reasons for this.*

*Question 7.2: Do you agree that remedies focussed on improving consumer communications to increase engagement listed below offer a reasonable prospect of success in encouraging competition?*

- *information on savings;*
- *information on the switching process;*
- *introduction of a decision point; and*
- *remedies to facilitate response to this information.*

*Please explain your reasons.*

*Question 7.3: Do you agree with our conclusions that the other remedial options we have considered, namely the establishment of a customer database for marketing purposes and automatic switching within BT's tariffs, raise significant implementation risks and therefore do not warrant further consideration? If you do not agree or consider there are other options we should have considered, please provide your reasons.*

*Question 8.1: Do you agree with our approach to determining the options for the level of price controls for Standalone Fixed Voice services? If not, please give your reasons.*

*Question 8.2: Do you agree with our proposed basket structure if implementing a price control for Standalone Fixed Voice services? In particular, do you agree with the need for a separate sub-cap on the Line Rental within the basket? If not, please give your reasons.*

*Question 8.3: Do you agree that it would be appropriate to allow the prices in a price control basket to rise by up to consumer price index (CPI)? If not, please give your reasons.*

*Question 8.4: Do you agree that we should exclude Home Phone Saver and Line Rental Plus from the price control? If not, please give your reasons.*

*Question 8.5: Do you agree that it is appropriate for the Line Rental sub-cap to have greater price flexibility than the overall price cap to allow BT to rebalance pricing between the line rental and call prices? If not, please give your reasons.*

*Question 8.6: Do you agree with the services we are proposing to include in a price control remedy basket for Standalone Fixed Voice services? If not, please set out your alternative proposals and please give your reasons.*

*Question 9.1: Do you agree with our proposed set of remedies for the Standalone Fixed Voice services markets, that is a price control, with a one-off adjustment set with reference to the costs of BT competitors in this market, and an obligation on BT to work with us to explore and ultimately implement information options to promote competition? If not please set out your reasons.*

*Question 9.2: Do you agree that BT should have at least one month after the date of the statement to implement the new price structure? If not, please set out your reasons.*

*Question 9.3: Do you have any additional comments on our analysis or conclusions in this consultation?*

## Annex 4

# Equality Impact Assessment

## Introduction

- A4.1 Ofcom is required by statute to assess the potential impact of all our functions, policies, projects and practices on equality.<sup>1</sup> An equality impact assessment (EIA) also assists us in making sure that we are meeting our principal duty of furthering the interests of citizens and consumers regardless of their background or identity.
- A4.2 We have not considered it necessary to carry out separate EIAs in relation to race or sex equality, or equality schemes under the Northern Ireland and Disability Equality Schemes. This is because we anticipate that our regulatory intervention will not have a differential impact on people of different sexes or ethnicities, consumers with protected characteristics in Northern Ireland<sup>2</sup> or disabled consumers compared to consumers in general.

## Equality Impact Assessment

- A4.3 We have considered whether the proposed remedies would have an adverse impact on promoting equality. In particular, we have considered whether the remedies would have a different or adverse effect on UK consumers and citizens with respect to the following equality groups: age, disability, sex, gender reassignment, pregnancy and maternity, race, religion or belief and sexual orientation, and, in Northern Ireland, political opinion and persons with dependants.
- A4.4 We are consulting on proposals to impose a set of regulatory obligations on BT that will promote competition, by for example, encouraging consumers to look for better value deals, and protect consumers from harmful conduct, such as the charging of prices above the competitive level.
- A4.5 We consider that our proposals will not have a detrimental impact on any defined equality group. Rather, we consider that our proposals will further the aim of advancing equality of opportunity between different groups in society by furthering the interest of all consumers in the standalone voice markets, many of which are in older age groups.<sup>3</sup>
- A4.6 Further, we do not propose to carry out separate EIAs in relation to race, gender equality or equality schemes under the Northern Ireland and Disability Equality Schemes. This is because we anticipate that our proposed regulatory intervention would not have a differential impact on people of different genders or ethnicities, consumers with protected characteristics in Northern Ireland or on disabled consumers compared to consumers in general.

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<sup>1</sup> We explain why we undertake an Equality Impact Assessment (EIA) and how we have done it in Section 2. Ofcom has a general duty under the 2010 Equality Act to advance equality of opportunity in relation to age, disability, sex, gender reassignment, pregnancy and maternity, race, religion or belief and sexual orientation.

<sup>2</sup> In addition to the characteristics outlined in the 2010 Equality Act, in Northern Ireland consumers who have dependents or hold a particular political opinion are also protected.

<sup>3</sup> As illustrated in Figure 2.2 in Section 2.



## Annex 5

# Profitability of standalone fixed voice services

- A5.1 In this Annex we examine different measures of profitability for SFV (standalone fixed voice) services.
- A5.2 In the first part of this annex we consider how we should measure profitability given the nature of SFV services and how we wish to use profitability to determine the level at which to set a price control on SFV services. In particular, we set out why we consider that when assessing the profitability of SFV services, we should use a return on sales (ROS) approach rather than a return on capital employed (ROCE) approach.
- A5.3 In the second part of this section we present the returns that BT is currently earning on SFV services and our assessment of potential levels of profitability that are consistent with competition developing for SFV customers.

## Approach to measuring profitability at the retail level

- A5.4 In order to calculate the profitability of SFV services, we must first understand the cost of providing those services including an appropriate rate of return. Typically, when we set charge controls on wholesale telecommunication services, we use a measure of ROCE to determine the reasonable rate of return. As we discuss below and in Section 8, we have considered a number of options for how to set the level of a price control beyond just being set at BT's level of costs. Specifically, we have considered the level of profitability of other CPs' SFV services who may compete with BT for SFV customers. We would therefore wish to use a measure for the reasonable rate of return that enables us to compare across these options.
- A5.5 Calculating the ROCE requires us to calculate a Weighted Average Cost of Capital (WACC) and then apply this to a Regulatory Asset Base (RAB). Some regulators and competition authorities have recognised that under certain circumstances, such as when the service to be charge controlled is "asset-light" on an accounting basis<sup>4</sup>, a ROCE approach might not be a reliable measure of determining returns. In some cases, an alternative approach, such as ROS, has been used when determining the appropriate rate of return.
- A5.6 An asset-light service or business has relatively low accounting capital employed for the assets used compared to the economic value of the assets. This can occur when the provision of a service only requires a small base of tangible assets, but has a large base of intangible assets associated with its provision.

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<sup>4</sup> The asset base would exclude intangible assets. Once these intangibles are included, the service in question may not be asset light.

## The ROCE and ROS approaches for setting an allowed return

### Theoretical underpinning for profitability assessment

- A5.7 The Internal Rate of Return (IRR) and Net Present Value (NPV)<sup>5</sup> of cash flow streams are the conceptually robust approaches for measuring rate of return as they allow us to measure the economic cost of an investment against the revenue that the investment earns.
- A5.8 The economic costs can be considered in two parts:
- i) the efficiently incurred operating costs of a firm; and
  - ii) the required return on the capital invested in the business – the investor's expected return on capital for investing in a risky asset over time.
- A5.9 When prices are set equal to economic costs the IRR of an investment would be expected to be equal to the discount rate at which the NPV of the investment would be zero (we would expect this to be equivalent to the WACC<sup>6</sup> of the investment). However, IRR and NPV calculations are challenging to calculate in reality due to the practicability of assessing the cashflows over the lifetime of the investment which may last many years.
- A5.10 Some form of a ROCE approach tends to be adopted by economic regulators as a practical proxy for the IRR approach. By using a ROCE approach, regulators can rely on accounting cost data rather than trying to estimate cashflows over the life of the investment. In practice, we use Earnings before Interest and Tax (EBIT) to approximate the yearly return and an estimate of the accounting value of the assets to approximate the capital employed. The key strength of the ROCE approach over a ROS approach is that it takes account of the capital required to operate the business on which investors will expect a positive return. This means that we are able to compare the ROCE to an estimate of WACC. In a competitive market, we would not generally expect the ROCE to be significantly and persistently above the WACC.<sup>7</sup>
- A5.11 A ROS<sup>8</sup> approach is an alternative measure of profitability that is widely used by companies, investors, analysts and other stakeholders as a measure for comparing performance across companies and company performance over time. A ROS approach equates the rate of return to some measure of profit divided by total sales.
- A5.12 Economic regulators and competition bodies, including Ofcom, have adopted a ROS approach to assessing profitability and setting price controls where there are concerns with the practical difficulties of applying a ROCE approach. However, from a regulator's perspective as ROS does not explicitly allow for a return on the capital employed, it is less clear how to derive an appropriate benchmark level of ROS that would indicate profitability in excess of a reasonable return.

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<sup>5</sup> A practical application of this approach is through a discounted cash flow analysis.

<sup>6</sup> Weighted average cost of capital.

<sup>7</sup> In some markets, we may set prices that mean the ROCE is above the WACC. For instance, we may make adjustments to asset values if we believe the accounting value of the asset is different from the economic value.

<sup>8</sup> Also referred to as EBIT (earnings before interest and tax) margin.

## Regulatory precedent

- A5.13 Due to its strong economic underpinning most economic regulators in the UK use some form of ROCE approach. However, in a number of cases regulators have recognised that a ROCE approach may be unreliable where the business is considered as “asset-light”. Most utility businesses are reliant on a physical network of assets such as wires, pipes, airports, power stations or tracks. In some cases, businesses may be described as “asset-light” as they have a small physical asset base compared to the revenues the business generates.
- A5.14 Examples of the use by UK regulatory bodies of a ROS approach to assess asset light businesses include:
- Ofwat’s decision to include an allowance for returns based on a retail net profit margin in its 2015-20 retail price controls for household water<sup>9</sup>.
  - The decision of the Northern Ireland Authority for Utility Regulation (NIAUR) to adopt a ROS approach in its 2014 Power NI energy supply price control<sup>10</sup>.
  - Ofcom’s own 2012 decision on the regulatory framework for the postal sector<sup>11</sup> where we concluded that an EBIT margin approach to assessing the financial sustainability of the universal postal service network was more appropriate than a ROCE approach.

## The challenges in using the ROCE approach for standalone fixed voice services

- A5.15 The use of a ROCE approach requires valuing the RAB and calculating a WACC as the benchmark for the return. In order for us to use this approach for all of our measures of profitability, we would need to be able to calculate the ROCE and RAB for BT and other CPs. We consider the following to be challenges for applying a ROCE approach to the SFV services:
- Observable accounting capital employed may understate the true economic value of the assets invested in by the company due to material unrecognised intangible assets, resulting in an undervalued RAB.
  - Developing a RAB that incorporates a robust valuation of the intangible assets is challenging and it may be disproportionate to develop a RAB if that asset base can only be calculated with a strong element of subjectivity.
  - Disaggregating the value of the assets and allocating this appropriately to the different services provided by BT Consumer such that a robust valuation is determined for the services we are considering regulating.
  - We would need to be able to calculate an appropriate WACC for a number of different operators.

<sup>9</sup> ‘Setting price controls for 2015-20 – final methodology and expectations for companies’ business plans’, Ofwat, 2013.

<sup>10</sup> ‘The 2014 Power NI supply price control – Decision paper’, UR, 19 December 2013.

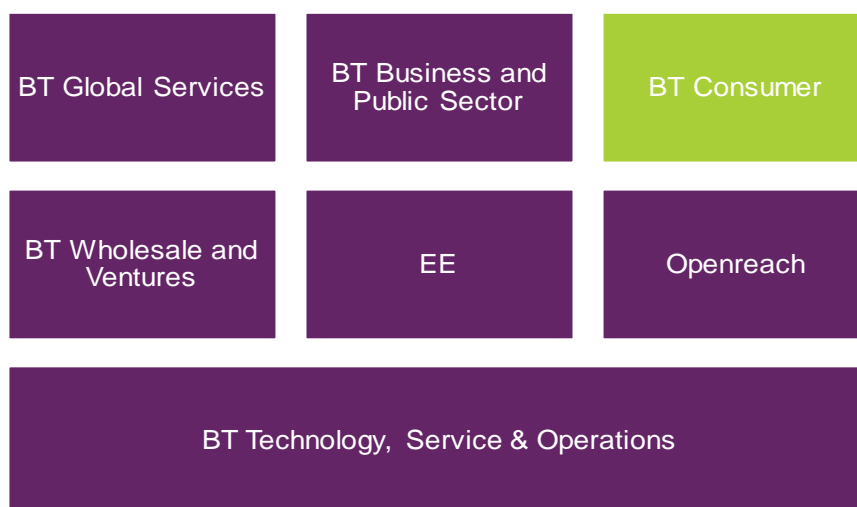
<sup>11</sup> ‘Securing the Universal Postal Service, Decision on the new regulatory framework’, Ofcom, 27 March 2012: <https://www.ofcom.org.uk/consultations-and-statements/category-2/review-of-regulatory-conditions>.

### Valuing a robust RAB

- A5.16 Accounting capital employed based on physical assets may understate the true economic value of the assets invested in by the company due to material unrecognised intangible assets, resulting in an undervalued RAB. In a company such as BT Group, the type of intangible assets in which investment has been made but has not been recognised in the statutory accounts could include:
- the staff training on developing improved customer service delivery; and
  - the marketing investment in developing the brand value of the business.
- A5.17 For accounting purposes these outlays do not satisfy recognition as an ‘asset’ on a balance sheet but, like those of a traditionally capital-intensive business, a key driver of future profits will be the level and effectiveness of the spending undertaken in them.
- A5.18 A range of techniques could be used to form a value for these ‘intangible’ assets but there is judgement inherent in each approach that would need to be carefully considered when judging the efficacy of each. Additional complexity occurs because we may not wish to include all of these intangibles in our estimate of BT Consumer’s RAB. For instance, it could be argued that part of the source of BT Consumer’s market power in the SFV markets is linked to its brand value. We would therefore not wish to capture this brand value in the RAB. We would only wish to capture intangibles in that RAB that an operator in a competitive market would hold.
- A5.19 We do not have a reliable basis on which to calculate the value of BT Consumer’s intangibles. We have asked BT Consumer whether they have undertaken any recent valuations of BT Consumer’s intangible assets. They have explained that, as far as they have been able to establish BT Consumer does not undertake such valuations or reviews.

### Disaggregating the value of the assets and allocation to the relevant services

- A5.20 Using a ROCE approach for the SFV services would require an accurate estimate of the economic value of the capital employed required on a standalone basis. As we set out in Figure A5.1 below, BT Group contains a number of different businesses within its group structure, including BT Consumer which provides the services we are considering regulating, a subset amongst a number of other products.

**Figure A5.1: BT Group's lines of businesses**

- A5.21 BT has provided a value for the BT Consumer capital employed (absent of an estimate of intangible assets) but, within the business unit, BT does not maintain a balance sheet for SFV services, and a significant proportion of the capital employed is likely to be shared across the many services offered by the division.
- A5.22 Developing an objective and economically meaningful methodology for constructing an asset base for the services we are proposing to regulate from a BT Consumer asset base that has a valuation for both the accounting assets and the intangible assets would be challenging and may not provide a reliable basis for assessing profitability.

#### Calculating an appropriate WACC

- A5.23 A ROCE approach would also require establishing an appropriate WACC for the SFV services. The BT Group PLC WACC would represent the return required by investors to invest in the Group as a whole, while we would want to determine a WACC for services within the BT Consumer business unit.
- A5.24 Additionally, we would need to be able to calculate an appropriate WACC for other CPs in order to determine the appropriate level of return that is consistent with promoting competition.

#### Consideration of whether SFV services are asset-light

- A5.25 BT Consumer is the BT Group business unit that provides SFV services. SFV services are only one set of the services sold by BT Consumer which provides five main sets of services – landline, broadband, TV, mobile and sports channels.
- A5.26 SFV services constitute c.[redacted]%, c. £[redacted]m of BT Consumer's revenues. Using our formal information gathering powers we have sought to gather data on the value of assets used by BT Consumer specific to providing SFV services. BT was not able to provide us with this data, but it was able to provide us with data on the value of assets used to provide all BT Consumer services. We consider that SFV services at the retail level would be no more capital-intensive (and perhaps considerably less so) than other services sold by BT Consumer. Therefore, we treat the data provided

to us by BT as an upper bound for the value of assets used to provide SFV services.

- A5.27 Using the BT Consumer business unit as indicative of the capital-intensiveness of SFV services, we have performed a comparison against business units that might be considered as either asset-light or capital-intensive. Figure A5.2 below sets out selected measures of capital-intensity for BT Consumer and other comparators.

**Figure A5.2: Indicators of capital-intensity for BT Consumer and selected comparators**

Company/ Business Unit	Capital Expenditure /Revenue 15-16	Operating Expenditure exc. depreciation/ Revenue 15-16	Depreciation/ Operating Expenditure 15-16	Sector
Balfour Beatty	1%	104%	0.0%	Construction & Engineering
Capita	2.5%	89%	0.0%	Support Services
Royal Mail	3%	92%	3%	Industrial Transportation
BT Consumer	4%	77%	6%	Telecoms
Pennon	21%	80%	18%	Utilities
National Grid	23%	63%	15%	Utilities
Openreach	28%	48%	35%	Telecoms
United Utilities	37%	46%	31%	Utilities

- A5.28 The indicators above for BT Consumer are nearer to the range for those that may be categorised as asset-light such as Royal Mail. Therefore, on these indicators, in contrast to energy networks or wholesale telecommunication networks where regulated companies are required to invest heavily in physical assets that make up that network, the services sold to SFV customers have more in common with asset-light businesses and services.

### The ROS approach

- A5.29 Given the above analysis, we do not believe that a ROCE approach provides a reliable way for us to measure profitability. An Earnings Before Interest and Tax (EBIT) margin (as a percentage of revenues) as a measure of ROS is a widely used measure of profitability and is used by companies, investors, analysts and other stakeholders as a measure for comparing performance across companies and profitability performance over time.
- A5.30 While there is some judgment involved in setting an appropriate ROS benchmark and it does not have the same conceptual basis as ROCE, we believe that it is a practicable and proportional approach to determining an appropriate level of return. It also enables us to more easily compare profitability between BT and other CPs, which is important when we are considering the level of price and profitability that is consistent with competitive entry developing.

### The challenges in using the ROS approach for the services we are considering

- A5.31 The setting of the EBIT margin benchmark requires selection of appropriate comparators that reflect not just the BT Consumer business unit but that of the SFV services. Deciding on the characteristics that reflect the services for which we want to derive an appropriate return and determining the companies or services that most appropriately exhibit those characteristics requires a level of regulatory judgement. Unlike the ROCE approach, where we can compare the return to the WACC to indicate excessive profitability, when using ROS we do not have a specific level that equates to normal profit.
- A5.32 Even though using a ROS approach has some challenges, we believe it provides us with the best method for comparing BT's profitability to the profitability of the competitive benchmarks that we set out in the next section.

### **Assessing the profitability of SFV services**

- A5.33 In this section, we start by estimating how BT's profitability for SFV services has developed over time, using EBIT margins as our measure of BT's return on sales. We then compare this to other measures of profitability that may provide benchmarks for the level of profitability that we would expect to see for SFV services if there was a greater degree of competition.

### **BT's profitability for SFV services**

- A5.34 As discussed below, BT does not hold revenue or cost data on its SFV customers, instead it provided data for all of its fixed voice customers, regardless of whether they also bought fixed broadband. However, for the reasons we explain below in paragraphs A5.43 to A5.52, we consider that the data provided is a good proxy for its SFV customers.

### Data and methodology for estimating revenues and costs

- A5.35 To estimate BT's profitability from selling SFV services, we requested data from BT Consumer under our formal s.135 powers.<sup>12</sup> BT provided data on revenues, costs, profits and the number of lines for its fixed voice services and for its fixed broadband services for the financial years 2007/08 to 2015/16.
- A5.36 BT provided the data separately for fixed voice and fixed broadband services from its P&L statements. However, BT was not able to differentiate between different customer groups (e.g. SFV, dual-play) or different voice and broadband products.
- A5.37 The fixed voice data includes all customers that purchase line rental from BT, and the revenues are those from line rental and calls.<sup>13</sup> The data combines customers

<sup>12</sup> Responses dated 24 June 2016 to questions 2 and 3 of the 10th BT s.135 under the NMR, and 9 December 2016 to questions 5 and 6 of the 2<sup>nd</sup> BT s.135.

<sup>13</sup> BT also provided other fixed voice revenue data, relating to services such as connections, network features, paper billing and late payment charges. These revenues were an insignificant proportion of BT's fixed voice revenues, on average approximately [redacted] from 2007/08 to 2015/16.

on all of BT's fixed voice products: BT Basic, BT Home Phone Saver and BT's standard product.<sup>14</sup>

- A5.38 Similarly, the fixed broadband data includes all customers that purchase fixed broadband from BT, and the broadband revenues exclude line rental and calls.<sup>15</sup> The data combines customers on all of BT's fixed broadband products, including products with different download speeds and allowances.
- A5.39 BT provided gross margins separately for fixed voice and fixed broadband services, which were calculated by subtracting direct (wholesale) costs from the reported revenues. However, BT did not allocate all of its retail costs between its fixed voice and fixed broadband services, so we now discuss our approach to estimating these costs. Once we had estimated retail costs, we subtracted them from the reported gross margins to estimate net margins. To calculate EBIT margins, we divided our estimated net margins by the reported revenues (excluding VAT).

### Allocation of retail costs

- A5.40 BT provided direct (wholesale) cost data for fixed voice and fixed broadband separately. However, the vast majority of the retail costs were not allocated to fixed voice and fixed broadband services. This is because these costs were incurred across the whole of BT Consumer (covering fixed voice, fixed broadband, mobile, TV and sport services) and BT did not have information available about how all of these costs could be allocated.
- A5.41 Where BT identified a retail cost item that was exclusively related to fixed voice or fixed broadband, we spread the cost fully across the relevant service. To be conservative when estimating BT's SFV profitability, where BT did not provide information about how individual cost items could be allocated, we allocated these retail costs exclusively to fixed voice and fixed broadband services, i.e. we made no allocation to BT Mobile, BT Sport or BT TV.
- A5.42 For these costs, we allocated them to fixed voice and fixed broadband services based on the number of lines in each financial year, i.e. we assumed that the cost was the same for each fixed voice and for each fixed broadband line. Due to the fact that BT had [x<] fixed voice lines than fixed broadband lines over the period 2007/08 to 2015/16, we allocated [x<] of the retail costs to fixed voice. For 2015/16, approximately [x<]% of these costs were allocated to BT's fixed voice services. One implication of this approach is that a customer taking both fixed voice and fixed broadband from BT would have twice the retail costs of a customer taking only fixed voice or only fixed broadband from BT.

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<sup>14</sup> BT's fixed voice products are: BT Basic, Home Phone Saver and its standard product. Customers on BT's standard product can pay their line rental annually in advance and receive a 10% discount for doing so (BT call this Line Rental Saver). They can also pay their line rental by means other than direct debit (BT call this Line Rental Plus). To the extent that customers choose to pay in different ways for their line rental, this is reflected in the data provided by BT.

<sup>15</sup> The fixed broadband data excludes BT Sport. BT split out other fixed broadband revenue data for 2013/14 to 2015/16, relating to services such as connections, value added services, postage and packaging and fair usage charges. These revenues were an insignificant proportion of BT's fixed broadband revenues, on average [x<]% from 2013/14 to 2015/16.



## Adjustments for SFV customers

- A5.43 As discussed in our market definition analysis (Section 3), we are concerned with all of BT's SFV customers except those on BT Basic. The data provided by BT includes all of its fixed voice customers, i.e. SFV customers and customers that also bought fixed broadband, and also customers on all of BT's fixed voice products.<sup>16</sup>
- A5.44 We have considered whether we need to adjust the data BT provided in order to analyse BT's SFV customers. For the 2015/16 financial year, we made the following adjustments to the average fixed voice data provided by BT to estimate how the revenues and costs for BT's SFV customers (excluding BT Basic) might differ. We made adjustments to:
- Remove BT Basic customers;
  - Account for the fact that BT's SFV customers made slightly higher volumes of calls than BT's other fixed voice customers; and
  - Account for the fact that BT's SFV revenues will be lower (on a per-line basis) than the average revenues in the data reported, because some of its SFV customers are on Home Phone Saver, a discounted product which is not available to customers also buying fixed broadband from BT.
- A5.45 We start by removing BT Basic customers. In 2015/16, a small proportion (approximately [x]%) of BT's fixed voice lines were BT Basic lines.<sup>17</sup> Using this information along with data from BT on BT Basic customers' average monthly spend on line rental and calls, we estimate that the impact of removing BT Basic customers from the data BT provided would be a minor increase in average revenues by £[x] per line per month (excluding VAT).
- A5.46 We next account for different call volumes. The data we received from BT suggests that, excluding BT Basic customers, its SFV customers made slightly [x] volumes of calls (in minutes) than its average fixed voice customers in 2015/16. Using information on BT's call revenues and volumes, we estimate the impact of BT's SFV customers making [x] calls would be to [x] average revenues by £[x] per line per month (excluding VAT).
- A5.47 Finally, we estimate the impact of some of BT's SFV customers being on Home Phone Saver, using information on the maximum savings customers can make by switching to the product and data from BT on the number of customers on the product.<sup>18</sup> We estimate that, other things being equal, this would cause BT's SFV revenues to be slightly lower, at most £[x] per line per month (excluding VAT), than the average fixed voice revenues in the data BT provided.
- A5.48 We now consider how the costs for BT's SFV customers might differ from the average fixed voice costs reported by BT. The majority of the wholesale costs for BT's fixed voice customers are WLR, which will be the same for all fixed voice customers. However, there will be differences in wholesale call costs due to

<sup>16</sup> See paragraph A5.37 for a description of BT's fixed voice products.

<sup>17</sup> This includes SFV customers on BT Basic and BT Basic customers that also take fixed broadband from BT, because all of these customers are included in the fixed voice data BT provided.

<sup>18</sup> From Table A8.38 in Annex 8, the maximum possible saving for a customer moving to BT's Home Phone Saver product is £13.05 (£10.88 excluding VAT) per month.

different customer groups making different volumes of calls. Using a similar approach to that for call revenues above, we estimate that the impact of SFV customers having higher call volumes in 2015/16 would be to increase the monthly wholesale cost of calls for these customers by £[X] per line per month (excluding VAT).

- A5.49 We do not have any evidence to show that BT's retail costs for SFV customers will differ materially from those for average fixed voice customers. As set out in paragraphs A5.40 to A5.42 above, we have made some assumptions in order to allocate BT's retail costs to its fixed voice and fixed broadband services, but do not consider that we have sufficient data to model how these retail costs might differ across BT's different fixed voice customers. That said, we are not aware of any reasons which could cause retail costs for SFV customers to be materially different to those for other fixed voice customers.
- A5.50 Based on our analysis for the 2015/16 financial year, we consider that the revenues and costs for BT's SFV customers are immaterially different from BT's average fixed voice customers. While we estimate that the profit from each SFV customer is slightly [X] than for an average fixed voice customer, we estimate the impact to be under £[X] per line per month. In Figure A5.3 below, we set out the various adjustments we have considered along with their estimated impact.

**Figure A5.3: Adjustments for SFV customers and estimated impact (per line per month, ex. VAT)**

	Revenue adjustments	Cost adjustments
Removing BT Basic customers	£ [X]	
Accounting for SFV customers having higher call volumes	£ [X]	£ [X]
Accounting for SFV customers on Home Phone Saver	£ [X]	
<b>Total</b>	<b>£ [X]</b>	<b>£ [X]</b>

- A5.51 Data from BT indicates that the proportion of its SFV customers that are on either BT Basic or Home Phone Saver has been [X] over time. This means that the effect of including these discounted tariffs would be [X] pronounced in earlier years.
- A5.52 Therefore, we have performed our profitability analysis on a per-line basis, based on the average fixed voice data BT provided. For the reasons set out above, we consider that adjusting the analysis to capture BT's SFV customers would show very similar, albeit slightly [X], levels of profitability.

### Time series of BT's fixed voice profitability

- A5.53 As discussed above, we consider that, on a per-line basis, the profitability for BT's SFV customers and BT's average fixed voice customers is likely to be very similar. We therefore discuss BT's revenues, costs and profits on a per-line basis, and then multiply this by the number of BT's SFV lines (excluding BT Basic) to estimate total profits for this customer group.

A5.54 The number of BT's SFV customers, excluding BT Basic, has fallen by between 35% and 55% between 2012/13 to 2015/16.<sup>19</sup> This has contributed to BT's overall revenues and costs for its SFV customers [redacted] over the period in absolute terms.

### Revenues

A5.55 As shown in Figure A5.4 below, BT's revenues per SFV line [redacted] slightly in real terms from 2007/08 to 2015/16, although there were [redacted] in the most recent three years. While revenues from [redacted] and [redacted] [redacted], this was outweighed by [redacted] revenues from [redacted].

#### **Figure A5.4: BT's SFV revenues (£ per line per month, ex. VAT, CPI adjusted for December 2016 prices)**

[redacted]

*Source: Response dated 24 June 2016 to questions 2 and 3 of the 10th BT s.135 under the NMR and 9 December 2016 to questions 5 and 6 of the 2nd BT s.135.*

A5.56 We can then multiply these SFV per-line revenue estimates by the number of BT's SFV lines. We estimate that BT's revenues for these customers [redacted] over the period, by approximately [redacted]%. Total revenues from line rental, call plans, out-of-plan calls and other revenues all [redacted] over the period shown in Figure A5.5 below.

#### **Figure A5.5: BT's SFV revenues (£m ex. VAT, CPI adjusted for December 2016 prices)**

[redacted]

*Source: s.135 responses from BT.*

### Costs

A5.57 BT's costs over the same period [redacted] from approximately £[redacted] to £[redacted] per line per month. Retail costs [redacted] on a per-line basis, due to [redacted] volumes of lines and per-line wholesale costs fell. Figure A5.6 below shows the wholesale costs which BT reported as well our estimates for BT's retail costs, all on a per-line basis, using the methodology described above in paragraphs A5.40 to A5.42.

#### **Figure A5.6: BT's SFV costs (£ per line per month, CPI adjusted for December 2016 prices)**

[redacted]

*Source: Response dated 24 June 2016 to questions 2 and 3 of the 10th BT s.135 under the NMR and 9 December 2016 to questions 5 and 6 of the 2nd BT s.135.*

A5.58 Once we account for the fact that the number of BT's SFV lines [redacted] from 2012/13 to 2015/16, we estimate that BT's total costs [redacted] over the period, and by a [redacted] amount than the [redacted] in revenues shown in Figure A5.5 above. Our estimates are shown below in Figure A5.7.

#### **Figure A5.7: BT's SFV costs (£m, CPI adjusted for December 2016 prices)**

[redacted]

*Source: s.135 responses from BT.*

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<sup>19</sup> See Figure A8.3 in Annex 8.

## Profits

A5.59 The [X] in per-line costs was [X] than the [X] in the per-line revenues, resulting in higher profits per line (and therefore EBIT margins) over the period, increasing from [X]% to 34-42%. This equates to net margins increasing from under £[X] to £8-10 per line per month over the period. Figure A5.8 below shows our estimates of BT's profits and wholesale and retail costs, with the height of the stacked graph being the revenue (ex. VAT).

### **Figure A5.8: BT's SFV profits (£ per line per month, CPI adjusted for December 2016 prices)**

[X]

*Source: Response dated 24 June 2016 to questions 2 and 3 of the 10th BT s.135 under the NMR and 9 December 2016 to questions 5 and 6 of the 2nd BT s.135.*

A5.60 Once we multiply our estimate of BT's profitability per SFV line by the number of BT's SFV lines, we estimate that BT's net margins from SFV services [X] over the period.<sup>20</sup> Figure A5.9 below shows our estimates for BT's profits on a per-line basis (left axis) and in £m (right axis).

### **Figure A5.9: BT's SFV profits (CPI adjusted for December 2016 prices)**

[X]

*Source: s.135 responses from BT.*

A5.61 Our analysis to date has covered the 2007/08 to 2015/16 financial years. We do not yet have sufficient data to run our analysis for the 2016/17 financial year but we are aware of several changes that have taken place since the 2015/16 financial year. BT also provided some information to us about future cost increases for its fixed voice customers. In summary, these changes are:

- BT's line rental price increased from £17.99 to £18.99 per month (inc. VAT) in July 2016, i.e. in the 2016/17 financial year, so this impact was not captured in our 2015/16 analysis;
- BT has announced that from April 2017, the prices for several call plans and some other call prices will be increasing.<sup>21</sup> BT's Evening and Weekend calls and its Anytime calls plans will be increasing by £0.30/month and £0.49/month (including VAT), respectively. In addition, call set-up fees, calls to landlines, calls to mobiles, international calls, BT's Friends & Family International calls package and BT's International Freedom calls package are all increasing in price; and
- In December 2016, BT provided information which suggests that for the 2017/18 financial year, it will incur additional costs relating to fixing faults faster, UK call centres and BT Call Protect (nuisance call blocking). BT argued that this will increase costs by £[X] per fixed voice line per month.

A5.62 We do not know exactly how these changes would impact our assessment of BT's profitability, particularly the increases in the prices of calls. However, even in the

<sup>20</sup> If we were to exclude customers on Home Phone Saver, we estimate that the EBIT margin for 2015/16 would be approximately [X]% higher.

<sup>21</sup> <https://www.productsandservices.bt.com/products/phone-packages/>

absence of these price increases, the increased costs that BT described are insufficiently large to materially change our view of BT's profitability from SFV services.

### Profitability of line rental and calls

- A5.63 Our analysis so far has looked at a combination of line rental and calls. We now attempt to understand the extent to which BT's line rental and calls services drive its SFV profitability.
- A5.64 BT provided revenue data for line rental and calls separately, however, the wholesale (direct) costs were not split between line costs (WLR) and call costs. Using Openreach's price list, which shows the evolution of WLR charges over time, we removed WLR charges from the total wholesale costs that BT provided to leave the wholesale costs associated with calls.<sup>22</sup> Subtracting these wholesale line and call costs from the reported revenues provides estimates of the gross margins for these services.
- A5.65 The gross margins we have estimated on a per-line basis are shown in Figure A5.10 below. Over the period shown, combined gross margins per SFV line increased, [§]. The cumulative gross margins earned over the period from [§] were larger than those from [§].

#### Figure A5.10: Estimated gross margins for line rental and calls (£ per line per month, CPI adjusted for December 2016 prices)

[§]

Source: Response dated 24 June 2016 to questions 2 and 3 of the 10th BT s.135 under the NMR and 9 December 2016 to questions 5 and 6 of the 2nd BT s.135.

- A5.66 In Figure A5.11 below we then show our estimated gross margins in £m across BT's SFV customers. Due to the falling number of BT's SFV customers, we estimate that the gross margins for line rental and calls combined [§] over the period, largely driven by [§] gross margins for [§]. Our estimated gross margins for [§] also [§] over the period but by a smaller amount.

#### Figure A5.11: Estimated gross margins for line rental and calls (£m, CPI adjusted for December 2016 prices)

[§]

Source: s.135 responses from BT.

- A5.67 We have not identified a clear basis to allocate BT's retail costs between line rental and calls. If we allocated a materially greater proportion of retail costs to either line rental or calls, [§] on a per-line basis over the period shown.
- A5.68 As shown in Figures A5.4 and A5.5, BT's SFV call revenues have been [§], per-line and in total (£m). Call revenue contributes about [§]% less to total revenue than line rental. Therefore, a given percentage increase in monthly line rental prices is sufficient to offset a larger percentage reduction in call prices. It could be argued that BT has increased the price of line rental over time to offset the falling revenues from fixed voice calls. Should call revenues continue to fall at the same rate, we

<sup>22</sup> Source: [Openreach price list](#).

consider that, to maintain the same level of profitability, BT would need to increase line rental prices by up to 2.5% per year in nominal terms.

A5.69 As we discuss in Section 3, BT may have a greater pricing constraint on SFV calls than SFV access. In the future, BT may respond to this pricing constraint, and potential further loss of call volumes, by decreasing call prices. However, we would not expect BT to decrease call prices such that the reduction in revenue from reducing prices was greater than the loss in revenue from falling call volumes. Therefore, if BT were to increase its line rental to offset a decrease in call prices, we would not expect this increase to need to be more than the 2.5% calculated above.

### **Competitive benchmarks for the profitability of SFV services**

A5.70 Above, we have estimated that BT's profitability on SFV services has been increasing over time on a per-line basis. We now compare our estimates of BT's profitability to other measures of profitability that may provide benchmarks for the level of profitability that we would expect to see for SFV services. We have considered:

- The profitability of other CPs from selling fixed voice services;
- BT's profitability of dual play, i.e. across fixed voice and fixed broadband services combined;
- BT's profitability from selling fixed voice services when we deregulated the retail line rental and calls markets in 2009; and
- Other industries.

### Other CPs' profitability from selling fixed voice services

A5.71 As with BT Consumer, we also requested revenues, costs and profit data from other CPs under our formal s.135 powers.<sup>23</sup> Some of the CPs were able to provide data relating specifically to their SFV customers, but some CPs provided data for all of their fixed voice customers, as BT did.<sup>24</sup> The data suggests that some other CPs are making reasonably high profits from their fixed voice customers, though none are as profitable as BT. Data from [X], [X] and [X] indicates that these CPs earn a profit of £[X] to £[X] per year, or [X]% to [X]% EBIT margins, from each fixed voice customer. While these EBIT margins are similar to those for BT, this is a result of other CPs having lower revenues and lower profits than BT.

A5.72 One feature of CPs' data on profitability is that it indicates the average profitability of their existing fixed voice customers, but is not directed at how profitable it might be for them to acquire new SFV customers. For these reasons, we produced a discounted cash flow model to estimate the marginal profitability of acquiring new SFV customers, under several scenarios, i.e. only considering the incremental revenues and costs that a CP would incur.

<sup>23</sup> The s.135 notices were sent to the Phone Co-op, Post Office, Sky, SSE, TalkTalk and Virgin Media in November 2016.

<sup>24</sup> As is the case for BT, we do not have any information to suggest that SFV revenues and average fixed voice revenues are materially different for other CPs.

- A5.73 Our model is structured to account for the initial acquisition costs involved in persuading a customer to switch, and then considers the incremental revenues and costs associated with serving that marginal customer in each given year. The incremental revenues are those from line rental, calls and other ancillary services, and the costs are wholesale costs and retail costs, including customer retention costs. The model discounts future revenues and costs over the assumed customer lifetime (in years), and determines whether the NPV (net present value) is positive in each of three scenarios:
- The first scenario models the current market conditions, with current market prices and high acquisition costs;
  - The second scenario assumes that, as a result of highly successful engagement remedies, acquisition costs fall, and that CPs have to spend more on customer retention; and
  - The third scenario assumes partially successful engagement remedies, with smaller reductions in acquisition costs and a smaller increase in customer retention costs.
- A5.74 Our model has several global assumptions. Firstly, we assume that CPs would need to price their line rental at a discount of at least 10% compared to BT in order to attract customers away from BT.<sup>25</sup> For our incremental costs, we use the wholesale costs from the data BT reported to us, which includes line costs (WLR) as well as the wholesale cost of calls. Future revenues and costs are discounted at a rate of 10% in all three scenarios.
- A5.75 Figure A5.12 below sets out the assumptions used in our three scenarios along with the estimated NPV of a CP acquiring a marginal customer. There is inevitably a degree of uncertainty around the assumptions we have used in our modelling, e.g. it is not possible to perfectly understand how long future SFV customers might remain with a CP after switching to them.

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<sup>25</sup> We assume that other prices for calls and ancillary services would be equal to those of BT.

**Figure A5.12: List of assumptions for discounted cash flow model**

Variable	Current market conditions	Highly successful engagement remedies	Partly successful engagement remedies
Incremental revenue (£ per customer per year)	25% discount on line rental compared to BT	10% discount on line rental compared to BT after £5 adjustment to BT	10% discount on line rental compared to BT after £7 adjustment to BT
Customer lifetime (years)	8	8	8
Acquisition costs (per customer)	£360	£180	£270
Incremental wholesale costs (£ per customer per year)	£[redacted]	Same as under current market conditions	Same as under current market conditions
Incremental retail costs (£ per customer per year)	£[redacted]	Same as under current market conditions	Same as under current market conditions
Incremental customer retention costs (£ per customer per year)	£0	40% of ongoing retail costs	20% of ongoing retail costs
<b>NPV of marginal customer</b>	Significant and positive	Larger than under current market conditions	Small but positive

A5.76 Our modelling suggests that currently, even though the acquisition costs of SFV customers may be substantial, they appear to be highly profitable to acquire under current market conditions. If acquisition costs were lower than this, or if customer lifetimes were longer, then these customers would appear even more profitable on an incremental basis.

A5.77 In our second scenario, even in the event that a £5 reduction was made to BT's line rental, we still consider that CPs would find marginal customers profitable, if they were to charge 10% less than BT for line rental. This is due to the likely impact of falling acquisition costs if there were highly successful engagement remedies.

A5.78 In our third scenario, where a larger adjustment was made to BT's line rental, we estimate that customers would still be marginally profitable. While revenues would be lower and acquisition costs higher than in our second scenario, lower customer retention costs mean that the NPV is small, but still positive.

#### BT's profits from dual-play: fixed voice and fixed broadband services combined

A5.79 Another useful analysis is to compare BT's profits for SFV services to those earned by BT from dual-play services, including both a fixed voice and a fixed broadband service from BT. Doing so means that we need to account for the costs of BT Sport,



as we did in the VULA margin squeeze.<sup>26</sup> Our approach to estimate BT's dual-play profitability, on a per-customer basis, was to:

- Start with our per-line estimates of BT's fixed voice revenues and profits;
- Estimate per-line revenues and profits for BT's fixed broadband services and add these to the fixed voice estimates; and
- Subtract the costs of BT Sport from the combined fixed voice and fixed broadband profits (on a per-line basis), then divide these combined profits by the combined fixed voice and fixed broadband revenues (on a per-line basis) to estimate EBIT margins.

A5.80 To estimate BT's fixed broadband profits, we used the same methodology as with BT's fixed voice services. BT provided total fixed broadband revenues which we divided by the number of fixed broadband lines to calculate per-line revenues. To estimate net margins, we started with the reported gross margins and then subtracted our estimates of retail costs.<sup>27</sup>

A5.81 Once the fixed voice and fixed broadband revenues and profits are combined, and we subtracted the costs of BT Sport, we estimate that BT made a dual-play EBIT margin of approximately [x] % to [x] %.

#### BT's profits when we deregulated the retail line rental and calls markets

A5.82 In our 2009 Fixed Narrowband Retail Services Markets statement, we showed that BT's revenues from fixed voice services (line rental and calls) had been falling consistently from 2003/04 to 2008/09.<sup>28</sup> However, as BT's costs had been falling by more than its revenues, its gross margins grew from 16% in 2007/08 to 21% 2008/09. The analysis did not include estimates for BT's retail costs, which would result in lower net margins if included.

A5.83 Our recent analysis based on the latest data from BT Consumer suggests net margins of approximately [x] % and [x] % for 2007/08 and 2008/09, respectively.

#### Other industries

A5.84 As discussed in paragraphs A5.25 to A5.28, we consider that the selling of SFV services could be considered as relatively asset-light. We now look at recent regulatory decisions made for returns of asset-light activities in other industries.

A5.85 EBIT margins have been set as part of the regulatory decisions made by Ofwat, the Northern Ireland Utility Regulator (NIAUR), the Office of Rail Regulation (ORR), and Ofcom. As shown in Figure A5.13 below, other regulators have set returns between 1% and 7% of turnover for asset-light businesses. We set out that an EBIT margin range between 5% to 10% represented a reasonable commercial rate of return for Royal Mail's Reported Business.

<sup>26</sup> Ofcom, *Fixed Access Market Reviews: Approach to the VULA margin*, [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0015/72420/vula\\_margin\\_final\\_statement.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0015/72420/vula_margin_final_statement.pdf)

<sup>27</sup> See paragraphs A5.40 to A5.42 for an explanation of how we allocated retail costs between BT's fixed voice and fixed broadband services.

<sup>28</sup> See Figure 5.4, [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0023/51836/statement.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0023/51836/statement.pdf)

**Figure A5.13: Recent regulatory decisions on returns for asset-light markets**

Regulator	Profit Margin	Decision	Coverage
Ofwat	1%	Price Control 2015-20	Household retail
Ofwat	2.5%	Price Control 2015-20	Non-household retail
NIAUR	2.2%	Price Control 2015-2016	Retail electricity
ORR	7.3%	2014	Network Rail High Speed
Ofcom	5-10%	2012 Decision	Royal Mail's 'Reported Business'

**BT's profitability (EBIT margins) with various adjustments to line rental**

A5.86 In Figure A5.14 below we have estimated how BT's profitability from SFV services would be affected based on different line rental prices from BT. We have shown a range of adjustments that could be made to BT's line rental that would result in similar EBIT margins to those we have discussed above.

**Figure A5.14: BT's estimated EBIT margins for SFV services**

Line rental (£/month inc. VAT)	Estimated EBIT margins in 2016/17 financial year	Comment
£18.99	BT: ~ 34-42% Other CPs: ~ [3<]%	BT's current price
£13.99 (£5 adjustment)	BT: ~ [3<] % Other CPs: ~ [3<] %	Lower estimate consistent with promoting competition
£11.99 (£7 adjustment)	BT: ~ [3<] % Other CPs: ~ [3<] %	Upper estimate consistent with promoting competition
£10.99 (£8 adjustment)	BT: ~ [3<] % Other CPs: ~ [3<] %	Similar to BT's estimated EBIT margin for fixed voice and fixed broadband combined
£8.99 (£10 adjustment)	BT: ~ [3<] % Other CPs: ~ [3<] %	

## Annex 6

# Consumer engagement

## Introduction

A6.1 This Annex sets out a framework for assessing barriers to engagement, and considers the markets for SFV services in terms of that framework. We cross-refer to this annex when discussing SMP in access and calls, and remedies to promote competition.

## Consumer engagement in the markets for SFV services is low

A6.2 Annex 8 sets out the evidence we currently have on low consumer engagement in the SFV markets. Survey results suggest a very low level of switching by SFV customers. Only 3% report having switched in the last year and only 30% report ever switching. This contrasts with 12% of bundle customers who have switched their landline provider in the last 12 months.<sup>29</sup> Survey results suggest that engagement is lower for BT SFV customers, as only 16% report ever switching, compared to 64% of non-BT customers. We note that some customers may engage without switching provider, such as by changing their call plan, and this may not be captured in our survey data.

A6.3 The main reason for not considering changing provider amongst SFV customers is that they prefer to stay with a trusted provider (62%\*).<sup>30</sup> Other reasons stated by SFV customers were hassle (15%\*), no cost benefit (7%\*) and provider satisfaction (9%\*). However, we do not have detailed evidence of customers' knowledge of their SFV services or others available on the market, their perception of the switching process, or their perception of other providers of SFV services. For this reason, we intend to conduct market research into these issues. We will use the framework set out below as a guide to areas for questioning / topics in this research.

## We use the UKRN framework to assess barriers to engagement

A6.4 We have assessed consumers' ability to engage effectively and drive competition using the UK Regulators Network (UKRN)<sup>31</sup> framework.<sup>32</sup> This framework was developed by the UK's economic regulators (including Ofcom) as part of a report organising previous work by these regulators on consumer engagement. It provides a common basis for considering the barriers to this. When considering a change of provider, consumers typically move through three stages:

- **Engage:** An engaged consumer is aware that they have a choice of product, service and provider and is willing to consider the alternatives available.

<sup>29</sup> This difference is statistically significant (at the 95% confidence level). Unless otherwise stated, the differences in all comparisons of survey evidence between customer groups in this annex are statistically significant.

<sup>30</sup> \* Caution: base under 100 (87)

<sup>31</sup> The UK Regulators Network is a member organisation formed of 13 of the UK's sectoral regulators (<http://www.ukrn.org.uk/>)

<sup>32</sup> UKRN (2014) 'Consumer engagement and switching', 17 December 2014

<http://www.ukrn.org.uk/wp-content/uploads/2016/07/20141217ConsumerEngSwitch.pdf>

- **Assess:** To make informed decisions, a consumer must be able to assess which product, service or provider best satisfies their needs. For this they need access to trusted and comprehensive information, an understanding of their own likely consumption pattern, and the ability to make comparisons.
- **Act:** To exercise their choice, a consumer must be able to purchase the product or service which they have assessed as best satisfying their needs.

A6.5 The UKRN report identifies a number of issues in general terms which can make it difficult for consumers to engage, to make an effective assessment and to act to change their service or provider. These barriers can be grouped around the following areas:

- 6.5.1 **Awareness of choice:** If consumers are not aware that they are even able to choose an alternative provider, then they are highly unlikely to be engaged.
- 6.5.2 **Attitude – perceptions of the market:** This could include perceptions that:
- the level of choice available in the market is too limited to warrant engagement – such as that options are limited or lack differentiation;
  - making choices between products or providers is expected to be too difficult, such as navigating a large volume of complex tariffs; or
  - providers or available information may not be trustworthy, meaning consumers anticipate not being able to rely on the information they could access.
- 6.5.3 **Attitude – perceptions of the outcome:** Consumers may not engage if they anticipate low benefits or high costs of switching. Consumers may perceive limited difference between prices or quality of service from current and alternative providers. Consumers may also anticipate financial costs (e.g. early termination charges) or non-financial costs (e.g. time or energy needed to seek out a better deal and switch) from switching.
- 6.5.4 **Ability – access to information:** This could include the absence of triggers to prompt engagement. Common triggers include:
- exposure to marketing materials;
  - the end of an existing fixed-term contract period;
  - an event leading to dissatisfaction with current product or provider; or
  - desire for a new product or service.
- 6.5.5 Separately, consumers could face difficulties in accessing information about current arrangements, usage patterns or alternatives. If consumers cannot easily access this information, they may be deterred from continuing their assessment, or make assumptions that may lead to a sub-optimal choice. In many sectors, price comparison websites are important in accessing this information.

- 6.5.6 **Ability – assessment of information:** Consumers may face difficulties in understanding information, making them less likely to engage. This could be due to low levels of familiarity or understanding of the products, services or providers available to them. Complexity and lack of transparency around products can also hamper consumer understanding. A lack of standardised comparison information or tools to address this complexity may also be a contributing factor.
- 6.5.7 **Ability – ability to effect change:** There may be a range of barriers and problems with switching processes that prevent consumers from acting to effect change. These could include:
- contractual barriers, such as early termination charges;
  - operational issues, such as contact with current provider or lack of portability;
  - transitional issues, such as loss of service during the switching process; or
  - eligibility issues, such as credit ratings.
- 6.5.8 **Consumer characteristics:** Internet users tend to be more likely to be engaged, as they have access to a wider range of information and so are more easily able to assess their options. In addition, factors such as age, affluence or numeracy can affect engagement levels.
- 6.5.9 Consumers may also exhibit a range of behavioural biases,<sup>33</sup> which may play a role in the barriers outlined above. Common behavioural biases, as set out in the UKRN report, which may be particularly relevant in the market for SFV services include:
- **Reference dependence and loss aversion:** People may underweight gains and overweight losses relative to a reference point.
  - **Status quo bias:** People prefer their current option.
  - **Projection bias:** People may expect their current preferences to continue in the future and underestimate the possibility of change.
  - **Framing, salience and limited attention:** Consumers may make different choices depending on how information or a decision is framed. Consumers may also not pay attention to important information if it is not presented prominently.
  - **Decision-making rules of thumb:** Consumers may simplify complex decisions by adopting heuristics.

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<sup>33</sup> By which we mean specific ways in which normal human thought systemically departs from being fully rational.

## Potential barriers to consumer engagement in the SFV markets

A6.6 The following paragraphs set out our current view of the barriers under the UKRN framework as they might apply to SFV customers. However, as noted in A6.3 above, we recognise that at present we have limited information on the different aspects of consumer engagement in this market, and will consider them further in our research programme.

### Awareness

A6.7 The extent to which SFV customers are aware of the possibility of switching provider is not clear from our survey evidence. While dual-play or other offers tend to be widely advertised, it is possible that SFV customers have limited information on other SFV providers or offers.

### Attitude: Perceptions of the market or outcome

A6.8 Gains from switching SFV services are currently relatively low of the order £2/month in terms of standard line rental price. Historically, they have been higher (as much as £4/month). In response to consumer research, “no cost benefit”, “no benefit/incentive”, “hassle” or “clarity of information” are cited as a reason for not being interested in changing provider by 23% of SFV customers.<sup>34</sup> This may indicate that perceptions of the market or outcome could play an important role for those who do not engage in switching. These perceptions could be broken into two areas: the hassle or complexity of finding a better offer and switching to it, and the potential gains to be made from switching.

A6.9 “Stay with trusted provider” is by far the biggest main reason given for not being interested in changing provider (62% of SFV customers). This differential in trust could be a reflection of brand loyalty, especially to BT as the “household name” provider of fixed line services. It could reflect a degree of mistrust of other providers (though this may be less likely in the case of well-known firms such as Post Office). It may also be a post-rationalisation given by respondents who have not thought about switching.

### Ability: Access to information

#### Few triggers prompting engagement

A6.10 The UKRN framework identifies a lack of triggers prompting engagement as a barrier to consumers taking steps to access information. There are reasons to believe that all of the potential triggers identified above may be lacking in the markets for SFV services.

A6.11 The markets for SFV services are declining, and several of the larger telecoms operators have little interest in marketing to these customers. This means many consumers have little exposure to information on competing offers.

A6.12 75% of SFV customers have been with their current provider for more than 4 years (88% of BT customers). These customers are highly likely to be outside a minimum contract period, and so will not be prompted to engage by the end of an initial term. Although moving home could act as a trigger for some, most of these customers are

<sup>34</sup> See Annex 8 for detailed discussion of this evidence

not likely to be frequently presented with a decision as to whether they should switch tariff or provider.

- A6.13 Desire for a new product or service is unlikely to act as a prompt. Broadband has been widely available for many years, so we anticipate the vast majority of customers who want broadband will be taking it. In addition, evidence suggests that 61% of voice-only customers would not be prepared to give up their landline. It appears that many in this market would be unlikely to be prompted to replace their landline with a different service.

#### Difficulties accessing information

- A6.14 Call plans are typically standardised between providers (weekend, evening and weekend, and anytime), and consumers are likely to have a general awareness of when they make calls and whether or not they have called mobiles often. For these reasons, we think an awareness and understanding of their usage of SFV services is not likely to be a significant barrier to accessing information for many consumers in this market. However, some consumers may find it more challenging to access this information.
- A6.15 SFV customers are less likely to have internet access – by definition voice-only customers do not have broadband access at home.<sup>35</sup> This would act as a barrier to accessing information on alternatives (such as through price comparison websites).

#### **Ability: Assessment of information**

- A6.16 Our current view is that alternative SFV services in the market are likely to be broadly comparable from the perspective of customers, but there are some potential caveats:
- The best value plan may depend on details of how much and when the customer uses their landline. This may make comparisons more complex for some customers (and indeed some may not be on the best plan with their current providers).
  - In considering the ability of customers to assess information, we need to take account of the fact that many customers are older (43% are aged 75 years or older), and some may struggle to assess different offers, particularly those who do not have access to a support network.

#### **Ability: Ability to effect change**

- A6.17 Switching between providers within the Openreach or KCOM copper networks can be done through a gaining provider led process. This means that consumers can switch their broadband and/or phone services within these networks simply by agreeing terms with their new provider. The gaining provider then manages the switch. This means that consumers only need to contact the provider they want to switch to, unless they are switching between different network infrastructure (e.g. to or from Virgin's cable network). In addition, number portability arrangements enable

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<sup>35</sup> By definition, the 60% of SFV customers who are voice-only do not have internet access at home. See paragraph 4.7.3.

customers (who are not moving home) to change their service provider whilst keeping their existing telephone number.<sup>36</sup>

- A6.18 As noted above, 75% of SFV customers have been with their current provider for more than 4 years. This suggests that many standalone voice customers are highly likely to be outside a minimum contract period, and so are less likely to face significant contractual barriers to switching.
- A6.19 Some consumers may not be aware of these features, or the steps they need to take. They may, for example, be concerned that switching would mean changing their phone number or contacting BT, when for many consumers this would not be the case.

### **Consumer characteristics**

- A6.20 We provide the distribution of SFV customers by age and evidence on other customer characteristics in Annex 8 (paragraphs A8.141-A8.145). As noted above, 43% of SFV customers are aged 75 years or older. While some older customers may be engaged and well-informed, others may not, and generally the demographics of this customer base may make them less likely than average to be able to engage effectively.<sup>37</sup> In addition, many SFV customers do not have fixed broadband access at home, which may mean they may lack access to the widest range of information.

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<sup>36</sup> Consumers that are moving home at the same time as they switch provider may be able to take their number with them if they are staying within the same exchange area.

<sup>37</sup> 34% of those aged 75 or over are classified as 'inactive' and just 8% are 'engaged' in our latest Switching Tracker research, compared to 28% and 18% respectively among all UK adults.



## Annex 7

# General analytical approach to market definition, SMP assessment and remedies

## Introduction

A7.1 This Annex sets out in general terms the processes that we have followed in defining the markets within this review, how and on what basis we assess whether any operator has SMP in a given market, whether SMP conditions should be imposed in a relevant market, and in what form. Sections 3, 4 and 5 (market definition, the three-criteria test and SMP analysis respectively) set out in more detail how we have applied our analytical approach in each of the markets we are considering.

## Overview of approach

A7.2 The market review procedure requires us to analyse markets in order to determine whether they are effectively competitive, and then to decide on appropriate remedies if necessary. Before an assessment of competitive conditions is possible it is necessary to define the relevant market.

A7.3 The definition of the relevant market does not simply entail identifying services that resemble each other in some way, but the set of services (and geographical areas) that exercise some competitive constraint on each other. It therefore has two dimensions:

- the relevant products or services to be included within the market; and
- the geographic extent of the market.

A7.4 It is often practical to define the relevant product market before exploring the geographic dimension of the market.

A7.5 The market definition exercise is not an end in itself, but a means to assessing whether there is effective competition and thus whether there is a need for *ex ante* regulation. It is in this light that we have conducted our market definitions in this review.

## 2014 EC Recommendation and the three-criteria test

A7.6 In defining markets for market review purposes, we are required to define relevant markets appropriate to national circumstances in accordance with the principles of competition law. In doing so we have taken due account of the 2014 EC Recommendation, the accompanying Explanatory Note and the EC SMP Guidelines.

A7.7 In the 2014 EC Recommendation identifies a set of product and service markets within the electronic communications sector in which *ex ante* regulation may be warranted. NRAs may also identify markets that differ from those in the 2014 EC Recommendation which may be susceptible to *ex ante* regulation having regard to the three-criteria test.

A7.8 The three-criteria test is related to the assessment of SMP and involves the assessment of similar evidence, but is analytically distinct. The three-criteria test focuses on overall market characteristics and structure, for the sole purpose of identifying those markets that are susceptible to *ex ante* regulation. In contrast, assessment of SMP involves determining whether an operator active in a market that has been identified as being susceptible to *ex ante* regulation should be made subject to *ex ante* regulation.<sup>38</sup>

### The time period under review

A7.9 Rather than just looking at the current position, market reviews look ahead to how competitive conditions may change in future. Our evaluation of the current market takes into account past developments and evidence, before then considering the foreseeable market changes that we expect to affect its development.

A7.10 The forward look period that we have used does not preclude us reviewing the market before that point should the market develop in a way we have not foreseen, to the extent that it is likely to affect the competitive conditions that are operating.

### Market review process

A7.11 The market review process begins with defining a relevant retail market. We then assess market power and, where appropriate, propose remedies to address the competition concerns.

A7.12 These steps are explained further in the following sub-sections.

## Market definition

### Demand-side and supply-side substitution

A7.13 The boundaries between markets are determined by identifying competitive constraints on the price setting behaviour of firms. There are two main constraints to consider:<sup>39</sup>

- to what extent it is possible for a customer to substitute other services for those in question in response to a relative price increase (demand-side substitution); and
- to what extent suppliers can switch, or increase, production to supply the relevant products or services in response to a relative price increase (supply-side substitution).

A7.14 The hypothetical monopolist test (HMT) is a useful tool often used to identify close demand-side and supply-side substitutes. In this test, a product is considered to constitute a separate market if the hypothetical monopolist supplier could impose a small but significant non-transitory increase in price (SSNIP) above the competitive level without losing sales to such a degree as to make this price rise unprofitable. If such a price rise would be unprofitable, because consumers would switch to other products or because suppliers of other products would begin to compete with the

<sup>38</sup> See the Commission Explanatory Note accompanying the 2014 EC Recommendation.

<sup>39</sup> See paragraph 38 of the SMP Guidelines, which also notes that potential competition also acts as a third source of competitive constraint on an operator's behaviour, but is taken into account in the SMP assessment.

hypothetical monopolist, then the market definition should be expanded to include the substitute products.

- A7.15 We must first therefore address the issue of which product(s) should form the starting point for the application of the HMT. We refer to this starting point as the ‘focal product’<sup>40</sup>, and start from the narrowest potential market definition.<sup>41</sup> Paragraph 41 of the SMP Guidelines states that “*As a starting point, an NRA should apply this test firstly to an electronic communications service or product offered in a given geographical area, the characteristics of which may be such as to justify the imposition of regulatory obligations...*”.
- A7.16 Having considered demand-side substitution we then, where relevant, assess supply-side substitution possibilities to consider whether they provide any additional constraints on the pricing behaviour of the hypothetical monopolist which have not been captured by the demand-side analysis. In this assessment, supply-side substitution is considered to be a low-cost form of entry which can take place within a reasonable timeframe (e.g. up to 12 months).
- A7.17 For supply-side substitution to be relevant not only must suppliers be able, in theory, to enter the market quickly and at low cost by virtue of their existing position in the supply of other products or geographic areas, but there must also be an additional competitive constraint arising from such entry into the supply of the service in question.
- A7.18 Therefore, in identifying potential supply-side substitutes, it is important that providers of these services have not already been taken into consideration. There might be suppliers who provide other services but who might also be materially present in the provision of demand-side substitutes to the service for which the hypothetical monopolist has raised its price. Such suppliers are not relevant to supply-side substitution since they supply services already identified as demand-side substitutes. As such, their entry has already been taken into account and so supply-side substitution from these suppliers cannot provide an additional competitive constraint on the hypothetical monopolist. However, the impact of expansion by such suppliers can be taken into account in the assessment of market power.

### Relevance of existing regulation – the modified Greenfield approach

- A7.19 When we conduct our analysis we use the modified Greenfield approach.<sup>42</sup> This requires us to assess whether markets are effectively competitive from a forward-looking perspective in the absence of any regulation that would result from a finding of SMP. To do otherwise would be circular.
- A7.20 However, it remains appropriate to take into account *ex ante* regulation arising from SMP findings in markets either upstream from, or horizontally related to, the services of interest.

<sup>40</sup> This reflects the terminology used by the OFT (OFT, *Market definition*, December 2004, OFT403, [www.of.gov.uk/shared\\_of/business\\_leaflets/ca98\\_guidelines/of403.pdf](http://www.of.gov.uk/shared_of/business_leaflets/ca98_guidelines/of403.pdf)).

<sup>41</sup> Paragraph 3.2 of the OFT Market Definition Guidelines explains that ‘previous experience and common sense will normally indicate the narrowest potential market definition, which will be taken as the starting point for the analysis’.

<sup>42</sup> See also Section 2.5 of the Explanatory Note to the 2014 EC Recommendation.

## Bundling

- A7.21 A common feature of the telecoms sector is the supply of bundles of different services. However, the Explanatory Note explains that the fact that bundling is a trend observed at the retail level does not require the definition of retail market(s) for bundles. This is because evidence to date has not indicated that there is a need for *ex ante* regulation of bundles, which may contain a previously regulated input.<sup>43</sup>
- A7.22 The Explanatory Note goes on to explain that what matters in this regard is *“that NRAs are able to ensure that the vertically integrated SMP operator’s regulated elements of the bundle can be effectively replicated (in terms of both technical and economic replicability) at the retail level, without an implicit extension of regulation to other components which are available under competitive conditions”*.

## Aggregating markets

- A7.23 In certain circumstances, it may also be appropriate to define a product or geographic market by grouping together services despite the absence of demand- and supply-side substitutability.

### Homogeneity of competitive conditions

- A7.24 Aggregating markets on the basis of the homogeneity of competitive conditions can help streamline the subsequent market power analysis by reducing the need to review multiple markets for products, the provision of which is subject to homogeneous competitive conditions.
- A7.25 However, combining products and services based on homogenous competitive conditions, is – by definition – only appropriate where this would not substantively alter any subsequent findings of SMP (relative to defining those markets separately).
- A7.26 Our approach also takes into account the SMP Guidelines. In particular, in the context of geographic market analysis, paragraph 56 of the SMP Guidelines states that:

*“According to established case-law, the relevant geographic market comprises an area in which the undertakings concerned are involved in the supply and demand of the relevant products or services, in which area the conditions of competition are similar or sufficiently homogeneous and which can be distinguished from neighbouring areas in which the prevailing conditions of competition are appreciably different...”*

- A7.27 Hence, subject to the relevant caveats above, where there are products (or geographic areas) where competitive conditions are sufficiently homogeneous, the definition of the relevant market will include all of those products (or geographic areas) within one market.

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<sup>43</sup> See Section 3.2 of the Explanatory Note to the 2014 EC Recommendation.

### Common pricing constraints

A7.28 Another factor that is sometimes considered in setting market boundaries is whether there exist common pricing constraints across customers, services or geographic areas (for example, areas in which a firm voluntarily offers its services at a uniform price). Where common pricing constraints exist, the products or geographic areas in which they apply could be included within the same relevant market even if demand-side and supply-side substitution is limited (or absent). Failure to consider the existence of a common pricing constraint could lead to unduly narrow markets being defined.

### **Geographic market**

A7.29 In addition to the product(s) to be included within a market, market definition requires us to specify the geographic extent of the market. The geographic market is the area within which demand side and/or supply side substitution can take place and is defined using a similar approach to that used to define the product market. We have considered the geographic extent of each product market covered in this market review.

A7.30 There are a number of possible approaches to geographic market definition. One approach would be to begin with a narrowly defined area and then consider whether a price increase by a hypothetical monopolist in that narrowly defined area would encourage customers to switch to suppliers located outside the area (demand-side substitution) or CPs outside the area to begin to offer services in the area (supply-side substitution). If demand- and/or supply-side substitution is sufficient to constrain prices, then it is appropriate to expand the geographic market boundary.

A7.31 We recognise that in certain communications (product) markets in the UK, there may be different competitive pressures in different geographic areas. In this case, we therefore have to consider whether it is appropriate to identify separate geographic markets for some services. Defining separate markets by geographic area may be problematic because, due to the dynamic nature of communications markets, the boundary between areas where there are different competitive pressures may be unstable and change over time, rendering the market definition obsolete.

A7.32 An alternative approach is to define geographic markets in a broader sense. This involves defining a single geographic market but recognising that this single market has local geographic characteristics. That is to say, recognising that within the single market there are geographic areas where competition is more developed than in other geographic areas. This avoids the difficulties of defining and remedying large numbers of markets and instability in the definition over time. Such an approach may also include the aggregation of markets as discussed above.

### **Market power assessment**

A7.33 Having identified the relevant product and geographic market(s) and, where relevant having identified the market as susceptible to *ex ante* regulation, we go on to analyse each market in order to assess whether any person or persons have SMP as defined in section 78 of the Act (construed in accordance with Article 14 of the Framework Directive). Section 78 of the Act provides that SMP is defined as being equivalent to the competition law concept of dominance in accordance with Article 14(2) of the Framework Directive which provides:

“An undertaking shall be deemed to have significant market power if, either individually or jointly with others, it 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.”

A7.34 Further, Article 14(3) of the Framework Directive states that:

“Where an undertaking has significant market power on a specific market, it may also be deemed to have significant market power on a closely related market, where the links between the two markets are such as to allow the market power held in one market to be leveraged into the other market, thereby strengthening the market power of the undertaking.”

A7.35 Therefore, in the relevant market, one or more undertakings may be designated as having SMP where that undertaking or undertakings enjoy a position of dominance. Also, an undertaking may be designated as having SMP where it could lever its market power from a closely related market into the relevant market, thereby strengthening its market power.

A7.36 In assessing whether an undertaking has SMP, we take due account of the SMP Guidelines as we are required to do under section 79 of the Act.

### **The criteria for assessing SMP**

A7.37 The SMP Guidelines require NRAs to assess whether competition in a market is effective. This assessment is undertaken through a forward-looking evaluation of the market (i.e. determining whether the market is prospectively competitive), taking into account foreseeable developments and a number of relevant criteria.<sup>44</sup>

### **Market shares**

A7.38 In the SMP Guidelines, the EC discusses market shares as being an indicator of (although not sufficient to establish) market power:

“...Market shares are often used as a proxy for market power. Although a high market share alone is not sufficient to establish the possession of significant market power (dominance), it is unlikely that a firm without a significant share of the relevant market would be in a dominant position. Thus, undertakings with market shares of no more than 25% are not likely to enjoy a (single) dominant position on the market concerned. In the Commission's decision making practice, single dominance concerns normally arise in the case of undertakings with market shares of over 40%, although the Commission may in some cases have concerns about dominance even with lower market shares, as dominance may occur without the existence of a large market share. According to established case-law, very large market shares — in excess of 50% — are in

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<sup>44</sup> See, for example, paragraphs 19 and 20, and the opening words of paragraph 75, of the SMP Guidelines.

themselves, save in exceptional circumstances, evidence of the existence of a dominant position...”<sup>45</sup>

A7.39 Market shares and market share trends provide an indication of how competitive a market has been in the past. If a firm has a persistently high market share, then that in itself gives rise to a presumption of SMP. However, changes in market share are also relevant to our assessment of prospects for competition. For example, a market share trend which shows a decline may suggest that competition will provide an effective constraint within the time period over which the SMP assessment is being conducted, although it does not preclude the finding of SMP.<sup>46</sup>

### **Other factors affecting competitive constraints**

A7.40 In addition to market shares, the SMP Guidelines set out a number of criteria that can be used by NRAs to measure the power of an undertaking to behave to an appreciable extent independently of its competitors, customers and consumers, including:<sup>47</sup>

- the overall size of the undertaking;
- control of infrastructure not easily duplicated;
- technological advantages or superiority;
- easy or privileged access to capital markets/financial resources;
- product/services diversification (e.g. bundled products or services);
- economies of scale;
- economies of scope;
- vertical integration;
- highly developed distribution and sales network;
- absence of potential competition; and
- barriers to expansion.

A7.41 A dominant position can derive from a combination of these criteria, which when taken separately may not necessarily be determinative.

A7.42 An SMP analysis may also take into account the extent to which products or services within the market are differentiated. The constraint from products or services outside the relevant market may also be a relevant factor.

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<sup>45</sup> Paragraph 75 of the SMP Guidelines.

<sup>46</sup> See, for example, paragraph 75 of the SMP Guidelines.

<sup>47</sup> SMP Guidelines, paragraph 78.

## Pricing and profitability

- A7.43 In a competitive market, individual firms should not be able to persistently raise prices above costs and sustain excess profits. As costs fall, we would generally expect prices to fall too if competition is effective.
- A7.44 The ability, therefore, to price at a level that keeps profits persistently and significantly above the competitive level is an important indicator of market power. The SMP Guidelines refer to the importance, when assessing market power on an *ex ante* basis, of considering the power of undertakings to raise prices without incurring a significant loss of sales or revenue (factors that may explain excess profits in the short term, such as greater innovation and efficiency, or unexpected changes in demand, should however be considered in interpreting high profit figures).<sup>48</sup>
- A7.45 The reverse is not true: consistently low profits, i.e. profits at or below the cost of capital, cannot be taken as evidence of an absence of market power. It may simply be evidence of inefficiency or other factors such as predatory pricing. For example, if a firm with SMP were to have inefficiently high costs, it may charge a price above the level we would expect to see in a competitive market but this would not result in high profits. In addition, price regulation exists in many of wholesale markets in the communications sector, and therefore low profits may simply be the result of existing regulation rather than a reflection of the underlying competitive conditions.

## Barriers to entry and expansion

- A7.46 Entry barriers are important in the assessment of potential competition.<sup>49</sup> The lower entry barriers are, the more likely it is that potential competition will prevent undertakings already within a market from profitably sustaining prices above competitive levels. Moreover, the competitive constraint imposed by potential entrants is not simply about introducing a new product to the market. To be an effective competitive constraint, a new entrant must be able to attain a large enough scale to have a competitive impact on undertakings already in the market. This may entail entry on a small scale, followed by growth. Accordingly, whether there are barriers to expansion is also relevant to an SMP assessment. Many of the factors that may make entry harder might also make it harder for undertakings that have recently entered the market to expand their market shares and hence their competitive impact.
- A7.47 A related factor is the growth in demand in the market. In general, CPs are more willing to invest in a growing market (and less willing in a declining market). As a result, barriers to entry and expansion tend to be less of an impediment to competition in rapidly growing markets.

## Countervailing buyer power

- A7.48 A concentrated market need not lead to harmful outcomes if buyers have sufficient countervailing buyer power to curtail the exercise of market power. In general, purchasers may have a degree of buyer power where they purchase large volumes and can make a credible threat to switch supplier or to meet their requirements through self-supply to a significant degree. It is important to note, however, that the

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<sup>48</sup> Paragraph 73 of the SMP Guidelines.

<sup>49</sup> Paragraph 80 of the SMP Guidelines.



volumes involved must be large enough to make a material difference to the profitability of the current supplier

## Remedies

- A7.49 Where we find SMP in a retail market, we must impose appropriate *ex ante* remedies which may range from pricing regulation to non-discrimination obligations.<sup>50</sup>
- A7.50 Any remedies imposed shall be based on the nature of the problem identified and be proportionate and justified in light of the objectives laid down in Article 8 of the Framework Directive.<sup>51</sup> The Act also specifically requires us to ensure that any condition imposed is:
- objectively justifiable in relation to the networks, services, facilities to which it relates;
  - not such as to discriminate unduly against particular persons or against a particular description of persons;
  - proportionate to what the condition or modification is intended to achieve; and
  - transparent in relation to what is intended to be achieved.<sup>52</sup>
- A7.51 In addition, retail level remedies shall only be imposed by Ofcom where it considers that it is unable to perform, or fully perform, its duties by means of conditions at the wholesale level.<sup>53</sup>
- A7.52 According to Section 91(6) of the Act, where Ofcom imposes regulatory control on tariffs, or other matters to which costs are relevant, it shall also set, and apply, an SMP condition which requires, to the extent that Ofcom considers appropriate, the use of cost accounting systems, the publication of an annual statement about compliance with this obligation and the annual auditing of such accounting systems by a qualifying auditor.

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<sup>50</sup> Section 91 of the Act and Article 17(2) of the Universal Service Directive.

<sup>51</sup> Article 16(2) of the Universal Service Directive.

<sup>52</sup> Section 47 of the Act.

<sup>53</sup> Section 91(2) of the Act.

## Annex 8

# Supporting evidence

A8.1 This Annex sets out evidence relating to the provision of residential standalone fixed voice (SFV) services in the UK (excluding Hull). We refer to the evidence in this annex in various sections in the main document, including Sections 3, 4 and 5 on market definition and SMP in SFV access and calls.

## Summary

- A8.2 Around 2.9 million<sup>54</sup> fixed voice lines are purchased on a standalone basis by residential customers, which accounts for 11%<sup>55</sup> of total residential fixed voice lines.<sup>56</sup> We estimate that approximately 60% of these customers are voice-only customers, who do not have fixed broadband.<sup>57</sup> The remaining 40% are split purchase customers, who purchase voice and fixed broadband as separate services on a standalone basis, i.e. they do not purchase a bundle.<sup>58</sup> The large majority of split purchase customers are split-supplier customers, who purchase fixed broadband and fixed voice from separate suppliers. A minority of split purchase customers purchase fixed broadband and fixed voice from the same supplier, but as separate services, i.e. unbundled. The total number of SFV customers has been declining, due in part to the increasing take-up of bundled services.<sup>59</sup>
- A8.3 BT supplies the majority of SFV lines and its market share is 79%. Other suppliers of SFV include Post Office, SSE, TalkTalk, Virgin Media and Sky. TalkTalk does not make these services available to new customers. However, Post Office, SSE and some smaller suppliers actively seek to acquire new SFV customers, with some offering promotional price discounts to the line rental price.
- A8.4 Retail line rental prices have increased significantly above the level of inflation since 2009, despite decreasing wholesale costs. Line rental prices have increased by between 25% and 49% in real (CPI-adjusted) terms from December 2009 to December 2016 (an average of between 3% to 6% a year). BT's line rental price is typically the most expensive in the market.<sup>60</sup> In recent years, other CPs' price increases have typically followed and matched BT's line rental price increases. Some SFV suppliers offer prices which are significantly lower than the rest of the market, but these suppliers have a limited number of customers.
- A8.5 The prices of call plans and out-of-plan calls increased significantly above inflation between 2012 and 2016. For instance, the average price of evening and weekend call plans increased by a CPI-adjusted average of 11% a year between 2012 and

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<sup>54</sup> S135 response data.

<sup>55</sup> The total volume of residential fixed voice lines is presented in paragraph A8.14 below.

<sup>56</sup> Throughout this annex, when we refer to fixed voice lines, we are referring exclusively to residential fixed voice lines. We exclude lines supplied to BT Basic customers from SFV lines, for reasons outlined in paragraphs A8.111 – A8.113, throughout this annex unless stated otherwise.

<sup>57</sup> S135 response data.

<sup>58</sup> S135 response data.

<sup>59</sup> For more detail see paragraph A8.13.

<sup>60</sup> In some cases, joint most expensive with another provider. See paragraph A8.59 for more detail.

2016, while the average price of UK geographic (out-of-plan) calls increased by an average of 6.5% per year over the same period.

- A8.6 The potential gains available to voice-only customers from switching are relatively limited, particularly if they want to switch to a major CP. However, split purchasers could potentially make savings by bundling their fixed voice and fixed broadband services into a single package with their existing, or a different, provider. Standard dual-play prices offer savings relative to purchasing these services separately, and promotional discounts offered to new customers make the potential savings even greater.
- A8.7 SFV customers<sup>61</sup> have some different characteristics from dual-play customers. SFV customers are older (43% are aged 75 years old or over) than dual-play customers (4% are aged 75 years old or over). The proportion of SFV customers living in DE socioeconomics group households (35%) is substantially higher than the equivalent proportion of dual-play customers (20%). The proportion of SFV customers who are not working (71%) is more than twice the proportion of dual-play customers who are not working (35%), as it is also the case for the proportion of customers with an income under £11.5k per annum (23% for SFV customers and 10% for dual-play customers).<sup>62</sup>
- A8.8 Only 70% of SFV customers have access to a mobile phone, compared to 96% of dual-play customers.<sup>63</sup> Engagement levels amongst SFV customers are lower than dual-play; only 9% of SFV customers are classified as engaged, compared to 20% of dual-play customers.<sup>64</sup> Moreover, 63% of SFV customers have been with their current landline provider for more than 10 years. Annual switching rates appear to be lower for SFV customers compared to dual-play customers; 3% of SFV customers reported switching within the past 12 months compared to 12% of dual-play customers.<sup>65</sup> Further, 70% of SFV customers reported that they have never switched their landline provider, compared to 45% of dual-play customers.<sup>66</sup> In fact, on average, SFV had been with their current landline provider for 22 years in Q2 2016.<sup>67</sup>
- A8.9 These characteristics are generally more pronounced for voice-only customers. For example, only 58% of voice-only customers have access to a mobile phone, compared to an overall 94% of split-supplier customers and 96% of dual-play customers. Further, a lower proportion are classified as engaged (6%), a higher proportion reported that they have never switched their landline provider (78%),

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<sup>61</sup> When referring to SFV customers in the context of survey evidence from the Ofcom Technology Tracker, the Ofcom Switching Tracker and the 2015 Jigsaw residential survey, we are referring to the combination of voice-only and split-supplier customers. We excluded split-service customers from these surveys' evidence due to the base size being inconsistent with S135 data. We are of the view that excluding split-service customers does not invalidate the evidence from these surveys given that split-service customers only account for approximately 8% of SFV lines (See paragraph A8.29).

<sup>62</sup> See paragraphs A8.142 to A8.146 (Age, socioeconomics, working status and income levels of SFV customers).

<sup>63</sup> This difference is statistically significant (at the 95% confidence level). Unless otherwise stated, all comparisons of survey evidence between customer groups in this annex are statistically significant.

<sup>64</sup> *Ofcom, Switching Tracker, 2016.*

<sup>65</sup> *Ofcom, Switching Tracker, 2016.*

<sup>66</sup> *Ofcom, Switching Tracker, 2016.*

<sup>67</sup> *Ofcom / operators.* Data as of Q2 2016; weighted average tenure calculated using number of customers and average tenure for different providers.

compared to 15% and 56% of split-supplier customers and 20% and 45% of dual-play customers.

- A8.10 However, split-supplier<sup>68</sup> customers have some characteristics which are similar to dual-play customers. For example, 94% of split-supplier customers have access to a mobile phone, compared to 96% of dual-play customers. 15% of split-supplier customers are classified as engaged, compared to 20% of dual-play customers.<sup>69</sup> 56% of split-supplier customers reported they have never switched compared to 45% of dual-play customers.

## Evidence topics in this annex

- A8.11 This annex includes the following:

8.11.1 An overview of fixed voice services, covering:

- a) Trends in the bundling of retail services (paragraphs A8.12 to A8.13);
- b) Trends in the volume of lines and calls (paragraphs A8.14 to A8.20);
- c) An account of the different types of SFV customers (paragraphs A8.21 to A8.29);

8.11.2 Our estimates of market share in the relevant markets (paragraphs A8.30 to A8.54);

8.11.3 An account of CPs' views of the market (paragraphs A8.55 to A8.56);

8.11.4 Retail pricing, covering:

- a) Retail line rental prices (paragraphs A8.57 to A8.60);
- b) Timing of line rental price increases (paragraphs A8.61 to A8.65);
- c) Discussion of line rental increases in CPs' internal documents (paragraphs A8.66 to A8.79);
- d) Retail call prices (paragraphs A8.80 to A8.108);

8.11.5 A description of current market offers (paragraphs A8.109 to A8.118);

8.11.6 Estimates of revenue per line (paragraphs A8.119 to A8.123);

8.11.7 Evidence on wholesale market prices (paragraphs A8.124 to A8.128);

8.11.8 Comparisons of SFV prices with dual play prices, covering:

- a) Voice-only customers (paragraph A8.130);
- b) Split purchasers (paragraphs A8.131 to A8.134);

<sup>68</sup> As explained in paragraph A8.139, in the context of survey evidence, we do not have data for split-service customers, and therefore use split-supplier customers in place of split purchasers (who account for the majority (80%) of this segment).

<sup>69</sup> Neither of these differences are statistically significant (at the 95% confidence level).

c) Average dual-play prices over time (paragraphs A8.135 to A8.137);

8.11.9 SFV consumer characteristics, covering:

- a) Survey evidence introduction (paragraphs A8.138 to A8.141);
- b) Age, socioeconomics, working status and income levels of SFV customers (paragraphs A8.142 to A8.146);
- c) Landline and mobile use, engagement, switching and satisfaction levels of SFV customers (paragraphs A8.147 to A8.176);

8.11.10 Our estimates of consumer detriment experienced by SFV customers, covering:

- a) Current consumer detriment (paragraphs A8.177 to A8.181); and
- b) Forecast consumer detriment (paragraphs A8.182 to A8.184).

## An overview of fixed voice services

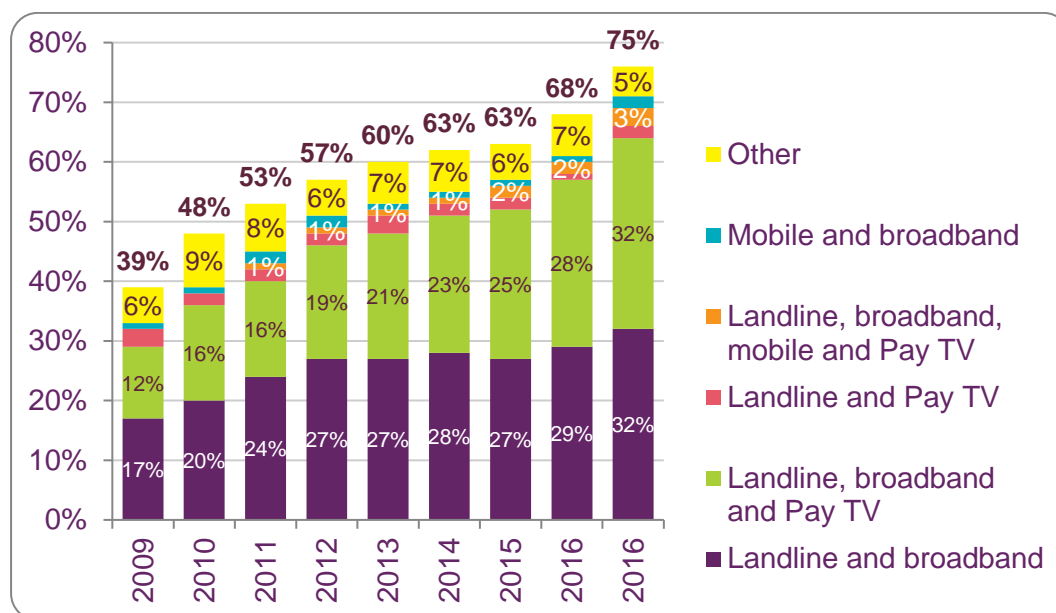
### Trends in the bundling of retail services

A8.12 Consumers are increasingly shifting away from purchasing their communications services separately and towards bundling their services. Bundling describes the process of combining multiple telecommunications services as a single package from one supplier.

A8.13 Figure A8.1 shows the proportion of households that take bundled services, with the 2016 proportion measured by two different means (as explained in the chart notes). The take-up of bundling has grown since 2009. In 2016, 67% households reported that they purchased at least landline and fixed broadband from the same provider.<sup>70</sup> Under the old methodology, 59% of households reported taking a bundle of at least landline and fixed broadband in 2016. Dual-play bundles of fixed voice and broadband, or triple-play bundles of fixed voice, broadband and TV, are the most common services to bundle, accounting for the large majority of retail bundling.

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<sup>70</sup> The remaining households are made up of those who purchase their landline on a standalone basis and those who do not have a landline, some of whom live in a mobile-only home.

**Figure A8.1: Take-up of bundled services: 2009 – 2016** <sup>71</sup>

Source: Ofcom, *Technology Tracker*. Data from Q1 of each year 2009 – 2014, then H1 2015 – 2016.

Notes: Revised methodology for 2016 data (to the right of the dotted line) as outlined in footnote 71.

### Trends in the volume of lines and calls

#### Line volumes

A8.14 According to Ofcom's Quarterly Telecoms data updates, the number of residential lines in the UK has increased by 13% since Q4 2009, from 23.4 million in Q4 2009 to 26.4 million in Q3 2016.<sup>72</sup> These figures refer to the total number of residential lines, i.e. including those within and outside the scope of this review. The increase in the total number of residential lines partially reflects the increase in the number of households in the UK, which is why the take-up of fixed telephony among households shows a more stable trend (the take-up of fixed telephony ranged between 84% and 87% of households from 2009 to 2016).<sup>73</sup> While the number of

<sup>71</sup> Methodology revised in 2016 to report the proportion of UK adults purchasing multiple services from a single provider, based on the main provider used for each service. Previously, data related to the proportion of customers self-reporting a bundle of services. Analysis for 2016 now includes those who pay line rental in addition to their broadband service as a bundle. This revised definition classifies a small proportion of customers defined as 'split-service customers' i.e. taking multiple services from one provider but not as a package, as bundle customers. While this does not precisely fit our definition, this methodology more accurately measures the proportion of consumers who bundle their services. Further, it is not possible to accurately identify 'split-service' customers in the research.

<sup>72</sup> We estimate that approximately 1.2 million residential lines in the UK are purchased by SMEs. This estimate is based on the fact that around 30% of SMEs reported not having a business-specific contract in 2016 (31% for those with 1-9 employees and 10% for those with 10-49 employees and 5% for those with 50-249 employees. See Figure 103 from the Jigsaw report on *SME experience of communications services*, available here:

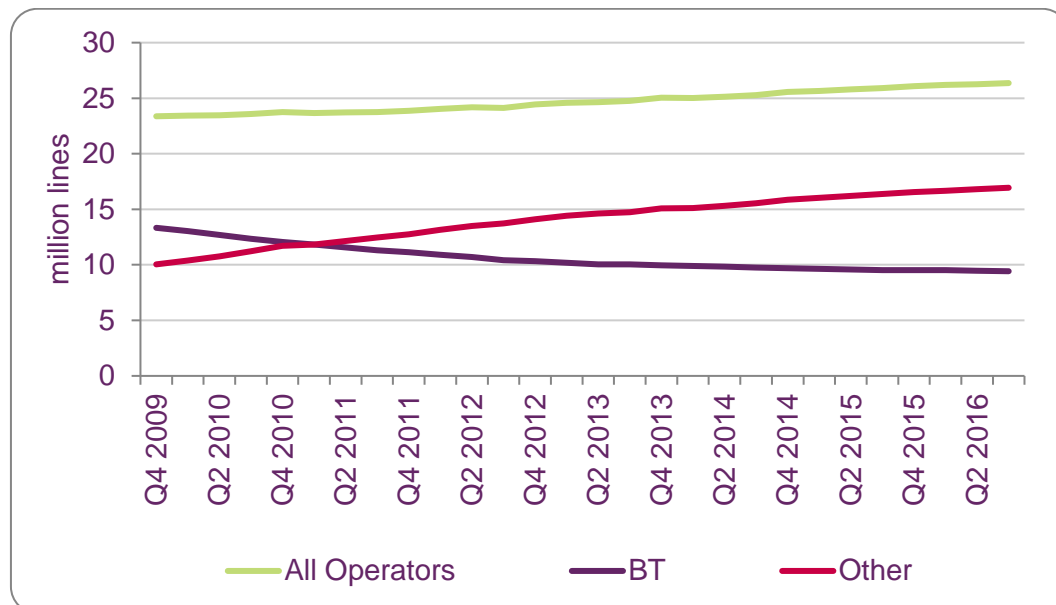
[https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0030/96348/Ofcom-SME-consumer-experience-research-2016-Report.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0030/96348/Ofcom-SME-consumer-experience-research-2016-Report.pdf)) and that there were approximately 5.4 million SMEs in the UK in 2016 (See Paragraph 4.16 from Ofcom's *Connected Nations Report 2015*, available here: [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0018/72432/fixed\\_broadband\\_services.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0018/72432/fixed_broadband_services.pdf)).

<sup>73</sup> Ofcom *Technology Tracker*. Data from Q1 for 2009-2014, then H1 for 2015-16. See Figure 4.35 of *CMR 2016*, available here:

[https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0026/26648/uk\\_telecoms.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0026/26648/uk_telecoms.pdf).

BT residential lines has decreased, this has been more than offset by an increase in the number of residential lines supplied by other operators. This has translated into a decrease in BT's share of residential lines from 57% in Q4 2009 to 36% in Q3 2016. Figure A8.2, below, presents the number of residential lines in the UK.

**Figure A8.2: Number of residential lines in the UK**



Source: Ofcom/operators<sup>74</sup>

A8.15 In Q3 2016, out of the 26.4 million residential lines, approximately 2.9 million (i.e. 11%) were SFV lines.<sup>75</sup> The number of SFV lines has consistently decreased since Q1 2013, from 6.1 million in Q1 2013 to 2.9 million in Q3 2016 (a 52% fall).<sup>76</sup> Figure A8.3, below, presents the number of SFV lines in the UK.<sup>77</sup>

<sup>74</sup> See Ofcom's Telecoms data updates here: <https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates>

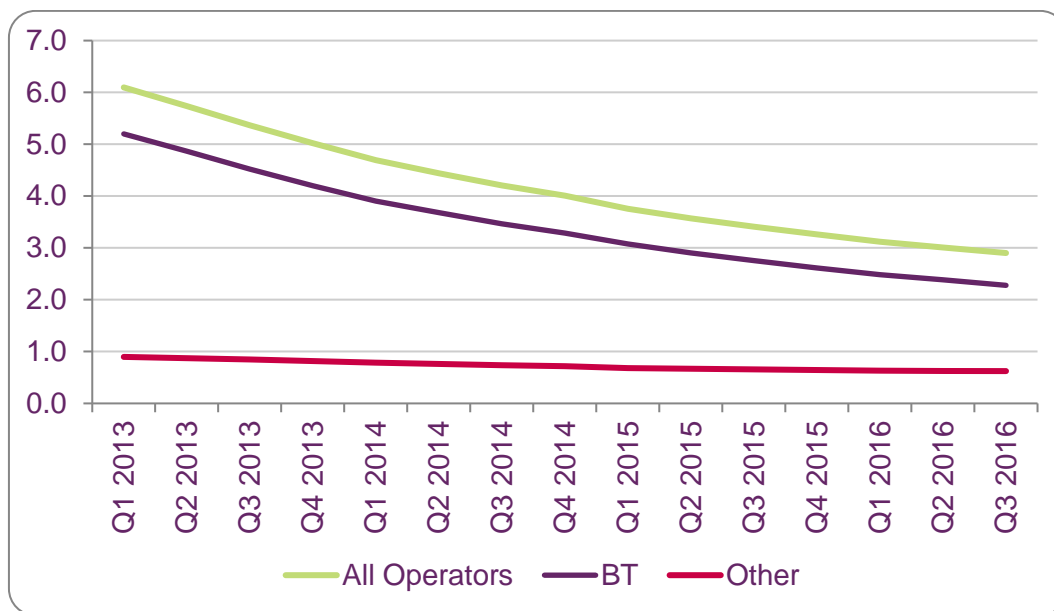
<sup>75</sup> In total, 9% of SMEs purchase a (residential) SFV service. With 5.4 million SMEs in the UK, this would suggest around 490,000 out of 2.9 million SFV customers are SMEs – around 17%. Based on data provided to Ofcom by Jigsaw as part of *The SME experience of communications services: Research Report*. Note that this statistic does not appear in the report.

[https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0030/96348/Ofcom-SME-consumer-experience-research-2016-Report.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0030/96348/Ofcom-SME-consumer-experience-research-2016-Report.pdf)

<sup>76</sup> We have estimated that, on average, each SFV customer has a single fixed line. Therefore, the line figures presented here can also be interpreted as customer figures.

<sup>77</sup>The figures exclude BT Basic lines. BT Basic is a social telephony scheme for customers who are recipients of specific means-tested Government benefits. See <http://btplc.com/inclusion/ProductsAndServices/BTBasic/index.htm>

**Figure A8.3: Number of SFV lines in the UK (million lines)**

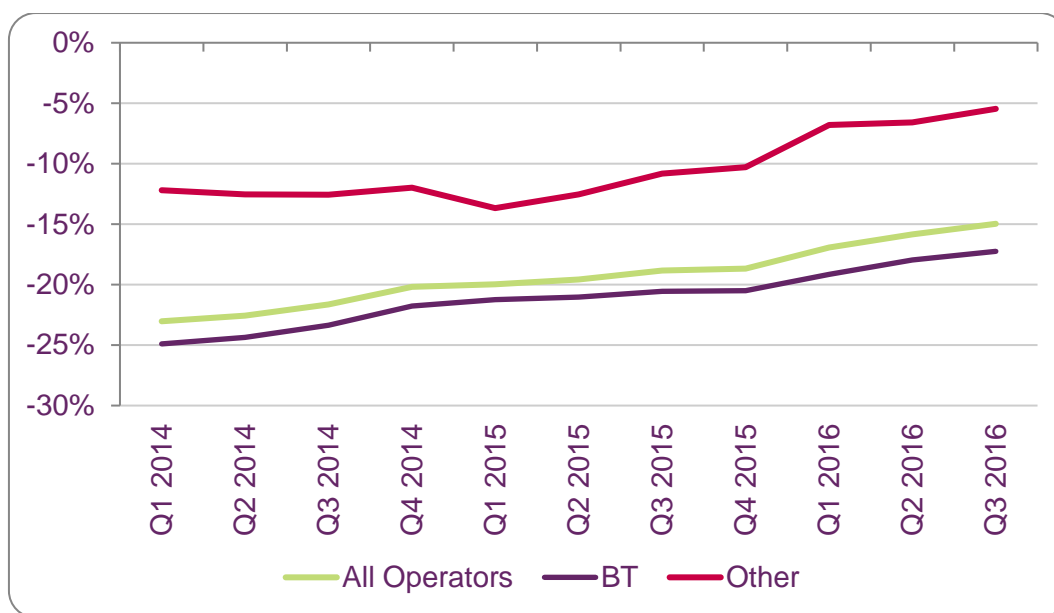


Source: S135 responses

A8.16 The fall in SFV lines has generally been experienced by all providers although BT, which provides the large majority of SFV lines, has seen a faster rate of decline.

A8.17 Figure A8.4 below presents the annual percentage rates of decline in the number of SFV lines. The rate of decline has slowed from around 23% in the year up to Q4 2014, to around 15% in the year up to Q3 2016. However, the rate of decline has slowed less for BT (from 25% in the year up to Q1 2014 to 17% in the year up to Q3 2016) than for other CPs (from 12% in the year up to Q1 2014 to 5% in the year up to Q3 2016). BT’s rate of decline is, on average, 11 percentage points faster than for other CPs.

**Figure A8.4: Rate of decline in the number of SFV lines (% change against same quarter in previous year)**



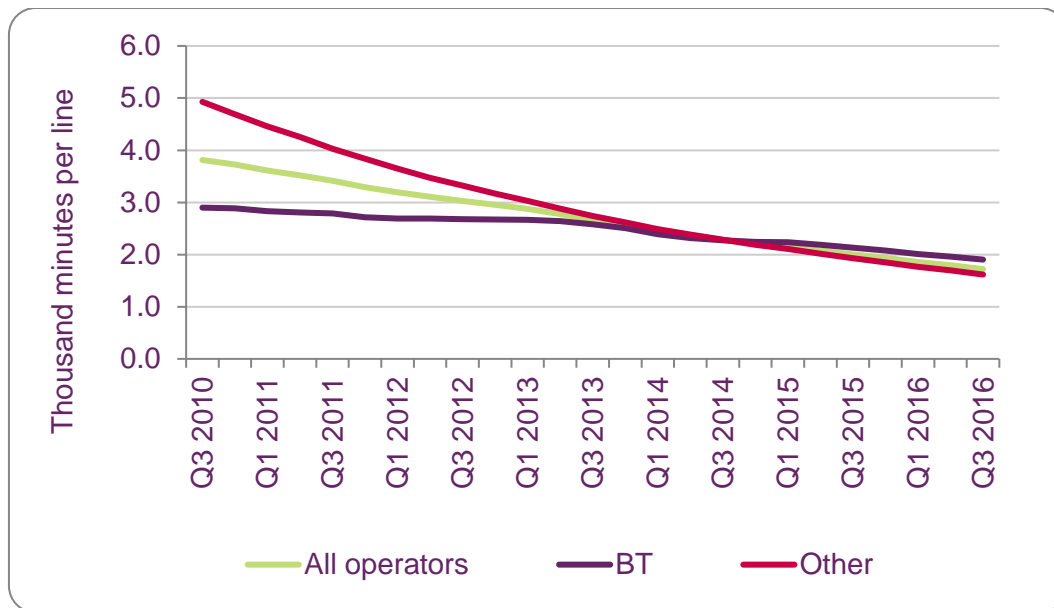
Source: s. 135 responses



Call volumes

A8.18 Call minutes per residential line – i.e. including both bundled and SFV lines – have decreased since Q3 2010, from 3.8 thousand minutes per line in the year up to Q3 2010 to 1.7 thousand minutes per line in the year up to Q3 2016 (a 55% fall). Figure A8.5, below, presents call minutes per residential line in the UK. BT customers historically made fewer call minutes on average than customers of other CPs, but now make slightly more calls on average.

**Figure A8.5: Call minutes per residential line per year in the UK**



Source: Ofcom/operators<sup>78</sup>

A8.19 Call minutes from SFV lines have also decreased. Annual SFV call minutes for all operators fell from 2.5 thousand minutes per line in the year up to Q4 2013 to 2.3 thousand minutes in the year up to Q3 2016 (i.e. a 9.3% fall). In comparison with the same quarter in the previous year, the average rate of decline in BT’s SFV call volumes has been [redacted]. Figure A8.6, below, presents the call minutes per SFV line.

**Figure A8.6: Call minutes per SFV line per year in the UK (thousand minutes per line in the last year)**

[redacted]

Source: s. 135 responses.

A8.20 Call minutes generated from BT’s lines have [redacted]. Within these, call volumes from BT SFV lines have [redacted]. Figure A8.7, below, presents the change in call volumes per line for all residential lines and SFV lines.

<sup>78</sup> See Ofcom’s Telecoms data updates here: <https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates>

**Figure A8.7: Rates of change in call volumes per line in the UK (% change against same quarter in previous year)**

[X]

Source: Ofcom/operators<sup>79</sup> for all residential lines and s135 responses for SFV lines.

**An account of the different types of SFV customers**

A8.21 Customers who purchase SFV services can be divided into three distinct customer segments:

- Voice-only customers: these customers purchase a SFV service but do not take fixed broadband from any supplier;
- Split-supplier customers: these customers purchase a SFV service and a standalone fixed broadband service from two separate suppliers; and
- Split-service customers: these customers purchase a SFV service and a standalone fixed broadband service from the same supplier, i.e. they do not bundle these services.

A8.22 When we refer to SFV customers, we are describing any customer who purchases a SFV service, i.e. all of the segments above. When we refer to split purchasers, we are describing split-supplier customers and split-service customers, i.e. any customer who purchases both a SFV service and a standalone fixed broadband service, from either the same or different suppliers.

A8.23 We collected data from BT, the Phone Co-op, Post Office, Sky, SSE, TalkTalk and Virgin Media on:

- the number of fixed voice lines purchased on a standalone basis (excluding lines purchased by split-service customers);
- The number of fixed voice lines purchased by split-service customers, if any; and
- The number of customers who purchase a standalone fixed broadband service.<sup>80</sup>

A8.24 A retailer of SFV lines does not necessarily know whether a customer takes standalone fixed broadband from another CP (i.e. whether this is a voice-only customer or a split-supplier customer). Therefore, we need to estimate how SFV lines are split between voice-only customers and split-supplier customers (excluding those sold to split-service customers).

A8.25 BT provided us with estimates of the number of its SFV customers who purchase a separate standalone fixed broadband service from other CPs.<sup>81</sup>

<sup>79</sup> See Ofcom's Telecoms data updates here: <https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates>

<sup>80</sup> This data is based on the volume of customers not lines (for October 2016). We assume that each split-supplier customer purchases one SFV line.

<sup>81</sup> Our estimates of the number of split-supplier lines include [X] BT standalone fixed broadband customers, who take a voice line from a non-BT supplier. However, we do not have S135 data that would allow us to identify split purchase customers who take *neither* their voice nor broadband service from BT. We assume that the number of split purchasers who take neither voice nor broadband service from BT is not material. One piece of evidence that goes against this is the 2015 Jigsaw

- A8.26 Approximately [redacted] customers buy standalone fixed broadband from BT, the Phone Co-op, Sky or TalkTalk (s. 135 response data). These customers are necessarily split purchasers since they must pay a separate line rental to receive a standalone fixed broadband service.
- A8.27 Approximately [redacted] customers take standalone fixed broadband from Virgin Media (s. 135 response data). However, Virgin Media standalone fixed broadband customers do not necessarily take line rental from another CP.
- A8.28 Using a combination of the above data, we have estimated the total number of voice-only and split-supplier lines, and providers' shares of provision of SFV lines to voice-only and split-supplier customers.<sup>82</sup>
- A8.29 As Figure A8.8 shows, we estimate that of the 2.9 million SFV lines in September 2016, approximately 1.7 million (60%) were supplied to voice-only customers, with split-supplier customers accounting for around 0.9 million lines (32%). We have actual lines data, which indicates that split-service customers account for 0.2<sup>83</sup> million lines (8%).<sup>84</sup> We estimate that there are a total of 1.2 million split purchasers.<sup>85</sup> Having conducted sensitivity checks around the assumptions made in our estimation of the number of split-supplier customers, we estimate the number of lines purchased by voice-only customers could range from between 1.6 million and 1.9 million. The number of split supplier customers could range from between 0.7 million and 1.1 million. This does not have a substantial effect on the shares within each customer segment.

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survey (wave 1), which indicates that up to 24% of total split-supplier customers' fixed voice line could be supplied by a non-BT supplier. However, we have some concerns about the reliability of this survey data as a basis for calculating market shares. As discussed in paragraph A8.40, if we assumed that this 24% figure was in fact accurate, this would not change BT's market shares for SFV lines overall, and would not have substantive implications for its share of lines within each segment.

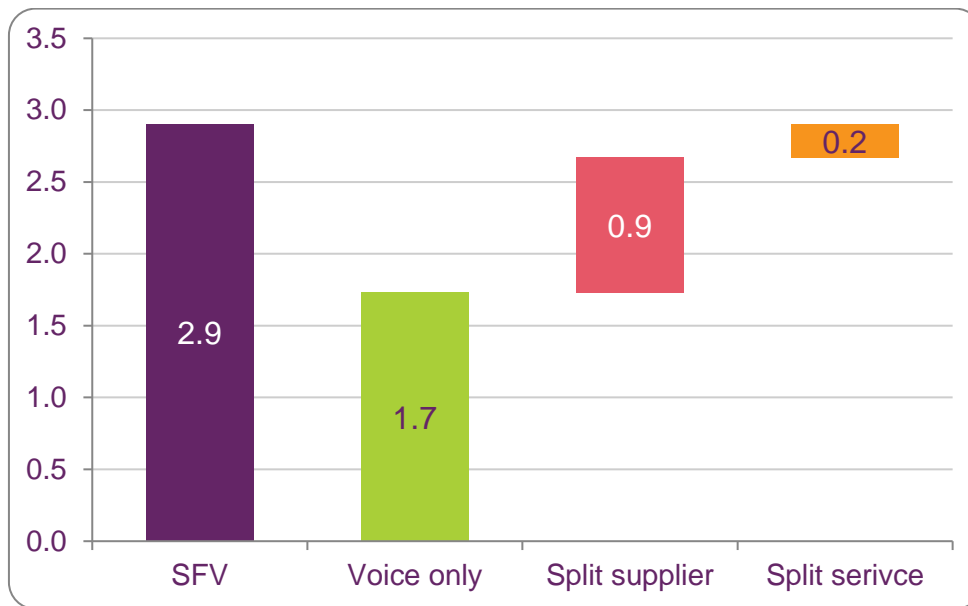
<sup>82</sup> We primarily rely on standalone broadband customer numbers provided by suppliers for our estimates of split-supplier customers, and make adjustments based on BT estimates (a) to reflect that Virgin Media standalone broadband customers do not necessarily have a voice line from another provider; and (b) where BT has identified another CP as providing standalone broadband to a BT SFV customer, but we do not have data directly from that CP, or BT has not specified the CP.

<sup>83</sup> This figure includes a small number of customers ([redacted]), who take an SFV line in addition to a bundle of services (including voice). We have used customer volumes as a proxy for SFV lines for this group, since the lines data may include the voice line from the bundle of services.

<sup>84</sup> The segments presented do not sum to 2.9 million due to rounding.

<sup>85</sup> The split-supplier and split-service segments presented do not sum to 1.2 million due to rounding.

**Figure A8.8: Volume of lines in September 2016 for each customer segment (millions)**



Source: s. 135 response data

### Our estimates of market share in the relevant markets

A8.30 This section sets out the market shares for the main CPs in the SFV access market and SFV calls market; BT, Post Office, SSE, TalkTalk, Virgin Media, Sky and the Phone Co-op. For all of BT's market shares, we exclude SFV lines sold to BT Basic customers and calls originated on these lines. We also exclude BT Basic from access and calls revenue market shares. We received data for September 2016 from Direct Save Telecom, Plusnet (BT's value brand) and Utility Warehouse on the number of SFV lines, which imply each of these CPs has a market share of <1%. In the absence of time series data, these suppliers have been excluded from the analysis.

A8.31 Below we present market shares (a) in the SFV access market, for lines and revenues and (b) in the SFV calls market, for call minutes and revenues. Further, we estimate the shares of SFV lines each CP has across the three customer segments in the SFV access market.

#### SFV access

A8.32 We calculate market shares based on the average monthly volume of SFV lines for each year. In 2016, the average is calculated from January – September. BT's 2013 and 2014 market shares contain a lower-bound estimate of split-supplier lines sold.<sup>86</sup> We have estimated Virgin Media's SFV line volumes for January –

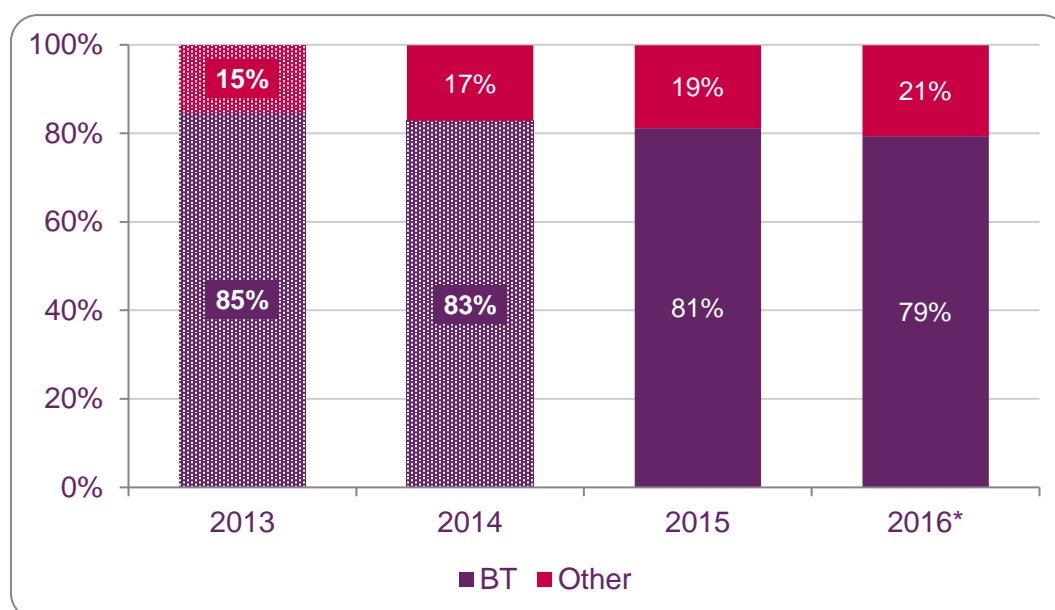
<sup>86</sup> We did not receive total data for volumes of split-service lines customers with BT. We use lines sold to split-service customers with an SFV line and a separate contract without voice, as a proxy for total split service lines (i.e. excluding SFV lines sold in addition to a bundle (including voice services)), which could not be accurately provided for the period October 2012 – October 2014).

December 2013, since Virgin Media were only able to provide SFV lines data from January 2014 to September 2016.<sup>87</sup>

A8.33 Figure A8.9 below shows that BT is by far the largest supplier of SFV lines. BT's market share of SFV lines has been at least 79% over the four years for which we have been able to collect data. BT's market share has declined by six percentage points since 2013.

A8.34 To the extent that market shares have been changing over the past four years, the evidence indicates this is mainly due to providers' customer bases declining at differing rates, rather than customers switching between suppliers, as discussed below.

**Figure A8.9: Market shares of SFV lines by BT and Other CPs**



Source: s135 response data

Notes: \*Market shares for 2016 are averaged across January – September. Pattern fill indicates market share contains estimated volumes of lines, as described in paragraph A8.32.

A8.35 As shown in Figure A8.10, Post Office has a market share of 5% - 15%. SSE, TalkTalk and Virgin Media have each had a market share of 5% or less. However, TalkTalk only supplies SFV services to legacy customers, rather than making them available (or competing) for new customers. Sky and the Phone Co-op supply a small number of SFV lines (<1%).

**Figure A8.10: Market shares of SFV lines by CP (in ranges)**

	BT	Post Office	SSE	TalkTalk	Virgin Media	Sky	Phone Co-op
2013	85%	5% - 15%	< 5%	< 5%	< 5%	< 1%	< 1%

<sup>87</sup> We estimated Virgin Media's volume of lines, using the average monthly growth rate calculated from the data provided.

2014	83%	5% - 15%	< 5%	< 5%	< 5%	< 1%	< 1%
2015	81%	5% - 15%	< 5%	< 5%	< 5%	< 1%	< 1%
2016*	79%	5% - 15%	< 5%	< 5%	< 5%	< 1%	< 1%

Source: s. 135 response data

### Figure A8.11: Market shares of SFV lines by CP

[X]

Source: s. 135 response data

Notes: \*Market shares for 2016 are averaged across January – September. Pattern fill indicates market share contains estimated volumes of lines, as described in paragraph A8.32.

- A8.36 We collected information on the number of customers as well as the number of lines. However, the number of customers and lines for each CP is very similar, such that there is essentially no difference in the market shares of SFV access between customers and lines.
- A8.37 All major CPs' SFV line volumes have been in decline since November 2012, with the exception of SSE, which has experienced an increase in the volume of lines between November 2015 and September 2016.<sup>88</sup> The rates of decline vary between CPs. For example, BT's volume of SFV lines declined by approximately 17% between September 2015 and September 2016, whereas [X] experienced a somewhat smaller [X]% decline in SFV lines across the same period.
- A8.38 Meanwhile, switching appears to have had a limited effect on market shares. For example, gross customer additions reported by other CPs suggest that switching could account for at most a small proportion of gross customer losses reported by BT. For example, from November 2014 to September 2016, BT's gross customer losses (for voice-only and split-supplier customers) was [X] customers per month. The next two largest suppliers can account for only a small proportion of BT's losses. [X].<sup>89</sup> [X].<sup>90</sup>

### Voice-only access

- A8.39 Using the customer segment estimates discussed in paragraph A8.29, we have estimated shares for each customer segment in September 2016. Figure A8.12 below outlines the estimated share of voice-only lines. BT has an estimated share of voice-only access in excess of 66%. Post Office and SSE have an estimated share of voice-only access between 5% - 15%. TalkTalk and Virgin Media have an estimated share of below 5%; Sky and the Phone Co-op have a supply a small number of voice-only customers (< 1%). Using sensitivity checks, BT's share of voice-only customers remains in excess of 60%.<sup>91</sup> Other suppliers' shares for voice-only customers are generally unaffected by these sensitivities.

<sup>88</sup> SSE's volume of lines increased by around [X] lines between April 2015 and September 2016, though overall its volume of lines is lower in September 2016 than in November 2012.

<sup>89</sup> [X].

<sup>90</sup> [X].

<sup>91</sup> While we have collected data on the number of SFV lines in the UK, there is some uncertainty about how many of these are split-supplier customers, as this is not necessarily known to the SFV

**Figure A8.12: Shares of voice-only lines by CPs (in ranges)**

	BT	Post Office	SSE	TalkTalk	Virgin Media	Sky	Phone Co-op
<b>Sep-16</b>	66%	5% - 15%	5% - 15%	< 5%	< 5%	< 1%	< 1%

Source: s. 135 data

**Figure A8.13: Shares of voice-only lines by CPs**

[X]

Source: s. 135 data

### Split-supplier access

A8.40 We estimate that BT supplies almost all SFV lines (97%) to split-supplier customers. There is a small proportion of split-supplier customers who purchase standalone broadband from BT and an SFV line from other CPs. As outlined in footnote 81, we have no clear evidence of split-supplier customers who purchase neither their SFV service nor standalone fixed broadband services from BT, and we have assumed that the number of such split-supplier customers is not material. We conducted sensitivity checks regarding the total number of split-supplier customers, and the proportion that take a SFV line from BT. Altering this assumption would affect BT's market shares within different segments, though under a range of sensitivities, BT's market share across segments remains high (>60%).

### Split-service access

A8.41 From the data provided in s. 135 responses, it appears BT supplies essentially all SFV lines to split-service customers. [X].

### Split-purchaser access

A8.42 We estimate that BT supplies almost all SFV lines (97%) to split purchasers. We estimate that there is a small proportion of split purchasers who take a line from other CPs.

A8.43 While split purchase customers largely receive SFV services from BT, they receive standalone fixed broadband service from a variety of CPs. We estimate that each CP has a share of less than 30% of total standalone fixed broadband services supplied to split-purchase customers.

### SFV access revenue

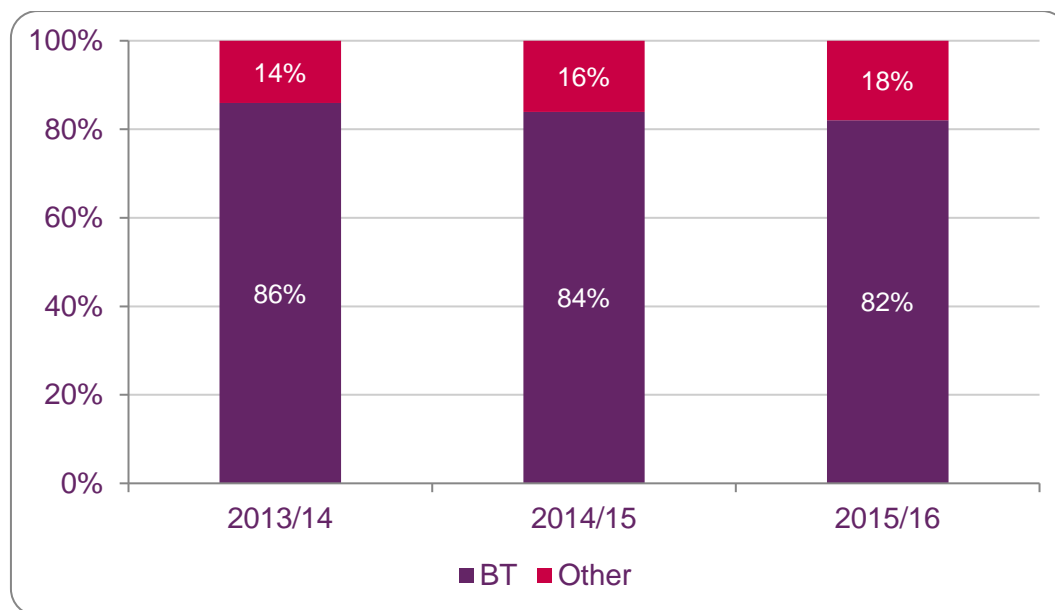
A8.44 We have estimated SFV access revenue for BT, Post Office, SSE, TalkTalk, Virgin Media and Sky for three financial years (2013/14, 2014/15 and 2015/16) by multiplying each CP's average line rental by the average number of SFV lines in the

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access provider. These sensitivities calculate voice-only shares based on different assumptions of the number of split-supplier customers (the remaining being voice-only customers, along with a limited number of split-service customers on which we have data).

months within each financial year.<sup>92</sup> We have then calculated each CPs' market share of total SFV access revenues. BT's and Other CPs' (aggregated) market shares of SFV access revenue are set out in Figure A8.14, below.

**Figure A8.14: Market shares of SFV access revenue by BT and Other CPs**



*Source: Ofcom estimate based on S135 responses and Pure Pricing UK Broadband Updates*

A8.45 BT had by far the largest market share of SFV access revenue (over 80%) in the financial year 2015/16. BT's market share has been decreasing since 2013/14 at approximately two percentage points per year. Figure A8.15, below, presents the market shares of SFV access revenue by CP.

**Figure A8.15: Market Shares of SFV access revenue by CP**

[X]

*Source: Ofcom estimate based on S135 responses and Pure Pricing UK Broadband Updates*

A8.46 [X].

### SFV calls

A8.47 We calculate market shares based on the average monthly volume of SFV call minutes in each year. In 2016, the average is calculated from January – September. We estimated: BT split-service call volumes for January 2013 – October 2014<sup>93</sup>; Post Office SFV call volumes for January 2013 – October 2014; TalkTalk from

<sup>92</sup> This methodology overestimates access revenue because some CPs include a call allowance with the line rental (e.g. BT includes weekend calls). We are of the view, however, that this is unlikely to materially affect our access revenue estimates.

<sup>93</sup> We estimated BT's volume of split-supplier calls by applying the average minutes per line from voice-only and split-supplier lines for each month between January 2013 – October 2014. We applied this average to our lower bound estimate of split-service lines between January 2013 and October 2014 to estimate the total volume of minutes originated on split-service lines.



January 2013 – July 2015; and Virgin Media for 2013.<sup>94</sup> For the periods for which we have data from CPs, we did not estimate any call minutes.

A8.48 [REDACTED]. BT's market share has been in excess of 76% over the past four years. [REDACTED].

#### Figure A8.16: Market shares of SFV call minutes by BT and other CPs

[REDACTED]

Source: s. 135 response data.

Notes: \*Market shares for 2016 are averaged across January – September. Pattern fill indicates market share contains estimated volumes of call minutes, as described in paragraph A8.47.

A8.49 As shown in Figure A8.17, Post Office has a market share of 5% - 15%. SSE, TalkTalk and Virgin Media have each had a market share of 5% or less. Sky and Phone Co-op supply a small number of SFV calls (<1%).

#### Figure A8.17: Market shares of SFV call minutes by CPs (in ranges)

[REDACTED]

Source: S135 response data

Notes: \*Market shares for 2016 are averaged across January – September.

#### Figure A8.18: Market shares of SFV call minutes by CPs

[REDACTED]

Source: s. 135 response data

Notes: \*Market shares for 2016 are averaged across January – September. Pattern fill indicates market share contains estimated volumes of call minutes, as described in paragraph A8.47.

#### SFV non-access revenue

A8.50 As a proxy for SFV calls revenue we have estimated SFV non-access revenue for BT, Post Office, SSE, TalkTalk, Virgin Media and Sky for three financial years (2013/14, 2014/15 and 2015/16). We have done so by subtracting our estimate of SFV access revenue from the SFV total revenue within each financial year. We are aware that SFV non-access revenue is an overestimate of SFV calls revenue given that some revenues which are neither from access nor calls (e.g. charges for paper billing and ancillary services) would be included. However, in our view non-access revenue is a reasonable proxy for actual calls revenue for the purpose of calculating each CP's market share of SFV calls revenue. Figure A8.19, below, sets out BT's and Other CP's market shares of SFV non-access revenue.

#### Figure A8.19: Market shares of SFV non-access revenue by BT and other CPs

[REDACTED]

Source: Ofcom estimate based on S135 responses and Pure Pricing UK Broadband Updates

<sup>94</sup> We estimated Post Office, TalkTalk and Virgin media's call volumes by calculating a weighted average minutes per line, from Phone Co-op, Sky and SSE data, for each month. We then applied this to the relevant months for Post Office, TalkTalk and Virgin media, to estimate the volume of total SFV lines.

A8.51 [redacted] Figure A8.20, below, sets out the market shares of SFV non-access revenue by CP.

### Figure A8.20: Market shares of SFV non-access revenue by CP

[redacted]

*Source: Ofcom estimate based on S135 responses and Pure Pricing UK Broadband Updates*

A8.52 [redacted].

### SFV total revenue shares

A8.53 Figure A8.21 below shows that BT has the largest share of SFV total revenues.<sup>95</sup> [redacted].<sup>96</sup> [redacted].

A8.54 [redacted].

### Figure A8.21: Market shares of SFV total revenues by CPs (in ranges)

[redacted]

*Note: asterisk indicates that the average revenue was calculated using SFV revenue. Other suppliers' average revenue was calculated using total voice revenue*

### Figure A8.22: Market shares of SFV total revenues by CPs

[redacted]

*Note: asterisk indicates that the average revenue was calculated using SFV revenue. Other suppliers' average revenue was calculated using total voice revenue.*

## An account of CPs' views of the market

A8.55 BT provided internal documents with information about its SFV customer base in the context of meetings with Ofcom and in response to s.135 notices. These documents include results from market research conducted or commissioned by BT over the past three years. The following points summarise the content of BT's internal documents with information about its SFV customer base:

- [redacted],<sup>97</sup> [redacted].<sup>98</sup>
- [redacted].<sup>99</sup>
- [redacted].<sup>100</sup>

<sup>95</sup> We applied each suppliers' average revenue generated through voice services, from both line rental and calls, to the average volume of SFV lines for each financial year, to estimate each suppliers' total annual revenue generated through SFV lines.

<sup>96</sup> BT's average revenue includes revenue from BT Basic customers, since we were unable to calculate average revenue excluding basic. Excluding BT Basic revenue in 2015/16 led to an increase in the average revenue of approximately [redacted]. BT Basic customers are still excluded from BT's volume of lines used to calculate these shares.

<sup>97</sup> [redacted] (response dated 18 November 2016 to question 1 of the 1<sup>st</sup> BT s.135).

<sup>98</sup> BT presentation to Ofcom 30 November 2016, slide 3.

<sup>99</sup> BT presentation to Ofcom 30 November 2016, slides 10.

<sup>100</sup> BT presentation to Ofcom 8 February 2017, slide 5.

- [REDACTED].<sup>101</sup>
- [REDACTED];<sup>102</sup> [REDACTED].<sup>103</sup>
- [REDACTED].<sup>104</sup>
- [REDACTED].<sup>105</sup> [REDACTED]<sup>106</sup> [REDACTED].<sup>107</sup>
- [REDACTED].<sup>108</sup>

A8.56 Other CPs also provided internal documents with information about their SFV customer base in response to s.135 notices, and/or verbally expressed their view of the SFV market in meetings with Ofcom. The documents provided include results from market research conducted or commissioned by these CPs over the past three years. The following points summarise the content of the internal documents provided by CPs other than BT and the views they expressed verbally in meetings with Ofcom:

- Post Office mentioned that it has three acquisition channels for voice-only customers: online (20%), call centre (40%) and in-branch (40%). It described customers as inert and noted that despite regular contact (in Post Office branches) Post Office struggles to gain much traction. It considered that inertia seems to come from concerns about the switching process even though the potential savings from switching are significant for some customers. However, it said it had successfully reached some of BT's SFV customers by launching various marketing campaigns.<sup>109</sup>
- Post Office recently launched an introductory offer to incentivise BT's SFV customers to switch. The offer entails paying a 12-month contract at a price of £14.99 a month instead of the full monthly price of £16.99. At the end of the contract, the customer will pay the full monthly price. Post Office marketing material also shows that they try to alleviate customer's concerns about the switching process. For example, in the marketing material for the new offer, the Post Office notes that the end user will keep the same phone line so no engineer will need to visit their home, they can keep the same phone number that everyone knows and there will be no break in service as the switch takes place.
- [REDACTED].<sup>110</sup>
- [REDACTED].<sup>111</sup>
- TalkTalk no longer offers SFV access services to new customers [REDACTED].<sup>112</sup>

<sup>101</sup> Response dated 18 November 2016 to question 1 of the 1<sup>st</sup> BT s.135.

<sup>102</sup> [REDACTED] (response dated 18 November 2016 to question 1 of the 1<sup>st</sup> BT s.135)

<sup>103</sup> BT presentation to Ofcom 30 November 2016, slide 4.

<sup>104</sup> BT presentation to Ofcom 30 November 2016, slide 4.

<sup>105</sup> [REDACTED]. See BT presentation to Ofcom 30 November 2016, slide 6.

<sup>106</sup> BT presentation to Ofcom 30 November 2016, slides 5-9.

<sup>107</sup> BT presentation to Ofcom 8 February 2017, slide 4.

<sup>108</sup> Response dated 18 November 2016 to question 1 of the 1<sup>st</sup> BT s.135.

<sup>109</sup> Notes of phone conversation with Post Office on 20 October 2016.

<sup>110</sup> Response dated 29 November 2016 to question 1 of the 1<sup>st</sup> Post Office s.135.

<sup>111</sup> Notes of phone conversation with SSE on 1 December 2016.

- [§].<sup>113</sup>
- [§].<sup>114</sup>
- [§].<sup>115</sup>
- [§].<sup>116</sup>
- [§].<sup>117</sup>
- [§].<sup>118</sup>
- [§].<sup>119</sup>

## Retail pricing

### Retail line rental prices

- A8.57 This section analyses price data collected by PurePricing, which monitors the line rental prices of the main suppliers of broadband services. We analyse BT, Virgin Media, TalkTalk, Sky and Post Office’s line rental prices.<sup>120</sup> Line rental charges are paid by all SFV customers for access to a fixed voice line.<sup>121</sup> Some calls may be included in the price of line rental, however these inclusions vary across suppliers.<sup>122</sup>
- A8.58 Up until 2006, BT was subject to retail price regulation. In 2006, Ofcom<sup>123</sup> decided to allow retail price controls to lapse, though the market remained regulated until 2009.<sup>124</sup> As Figure A8.23 below shows, line rental prices were generally decreasing in real (i.e. inflation adjusted) terms across this period. All line rental prices fell by between 4% and 9%, in real terms, from December 2006 to December 2009, with the exception of Post Office, which increased its line rental prices by 9%, in real terms.

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<sup>112</sup> TalkTalk email to Ofcom, November 2016.

<sup>113</sup> Notes of phone conversation with Virgin Media on 1 November 2016.

<sup>114</sup> Notes of phone conversation with Sky on 15 November 2016.

<sup>115</sup> Notes of phone conversation with Sky on 15 November 2016.

<sup>116</sup> Notes of phone conversation with Sky on 15 November 2016.

<sup>117</sup> Notes of phone conversation with Direct Save on 21 November 2016.

<sup>118</sup> Notes of phone conversation with Direct Save on 21 November 2016.

<sup>119</sup> Notes of phone conversation with Direct Save on 21 November 2016.

<sup>120</sup> The prices of other suppliers in the SFV market, including SSE, have not been tracked by PurePricing. A more exhaustive list of current SFV prices is in Figure A8.37 below.

<sup>121</sup> The line rental component of a dual-play service is no longer advertised as a distinct price, following the ASA’s ruling. Some CPs now state that they do not charge a price for line rental, however the overall bundled price will still provide fixed voice access.

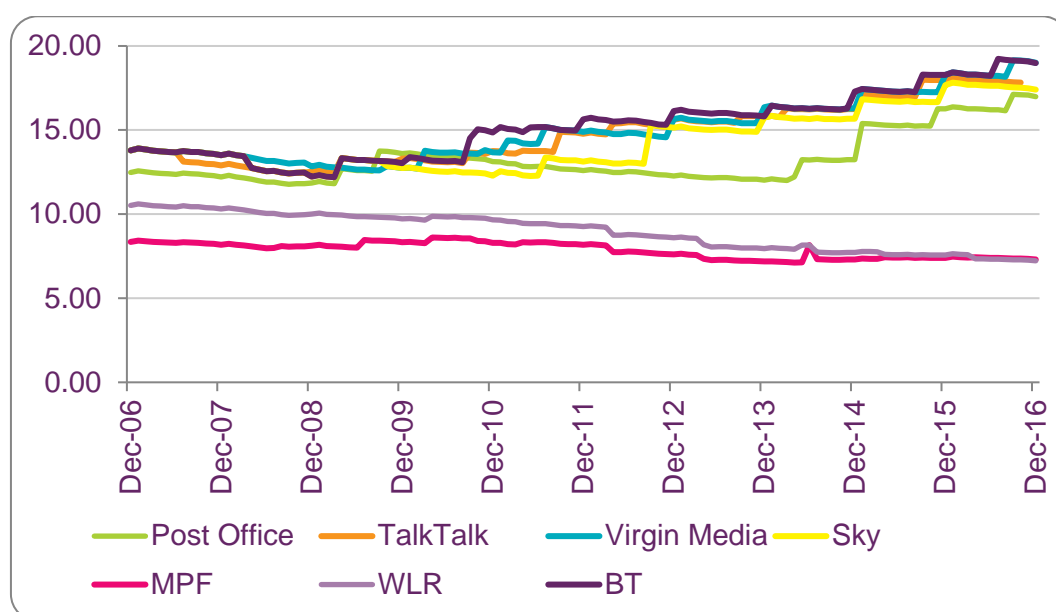
<sup>122</sup> For example, some suppliers such as BT include free weekend calls with their line rental. Due to restricted available data, these differences are not reflected in the analysis. A detailed list of current market offerings is provided in Figure A8.37 below. We take into account that some CPs include some free calls with their line rental when we estimate the shares of SFV non-access revenue as a proxy for the shares of SFV calls revenue, see paragraph A8.50.

<sup>123</sup> Ofcom replaced Oftel as the regulator with responsibility for electronic communications markets from 29 December 2003.

<sup>124</sup> Ofcom, *Retail Price Controls*, Statement of 19 July 2006 (“2006 Retail Price Control Statement”), [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0012/42114/rpcstatement.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0012/42114/rpcstatement.pdf)

A8.59 However, since deregulation of the retail narrowband market in 2009, line rental prices have generally been increasing, in real terms, despite decreasing wholesale access prices as discussed in paragraph A8.126. Line rental prices have increased, by between 25% and 49% depending on the provider, in real (i.e. inflation-adjusted) terms between December 2009 and December 2016. This is an average of between 3% and 6% per year. Since December 2009, BT has offered the single most expensive line rental price in the market for 40 out of the 85 months, and for a further 31 months it was jointly most expensive with Virgin Media. Since September 2016, Virgin Media's line rental price has been the most expensive in the market at £19.00 per month, although this is only one penny more expensive than BT. Line rental prices have converged to some degree in recent years, having diverged after 2009, due mainly to significant increases in price by Sky and Post Office.<sup>125</sup>

**Figure A8.23: Wholesale and retail line rental price movements (£/month in December 2016 prices)**

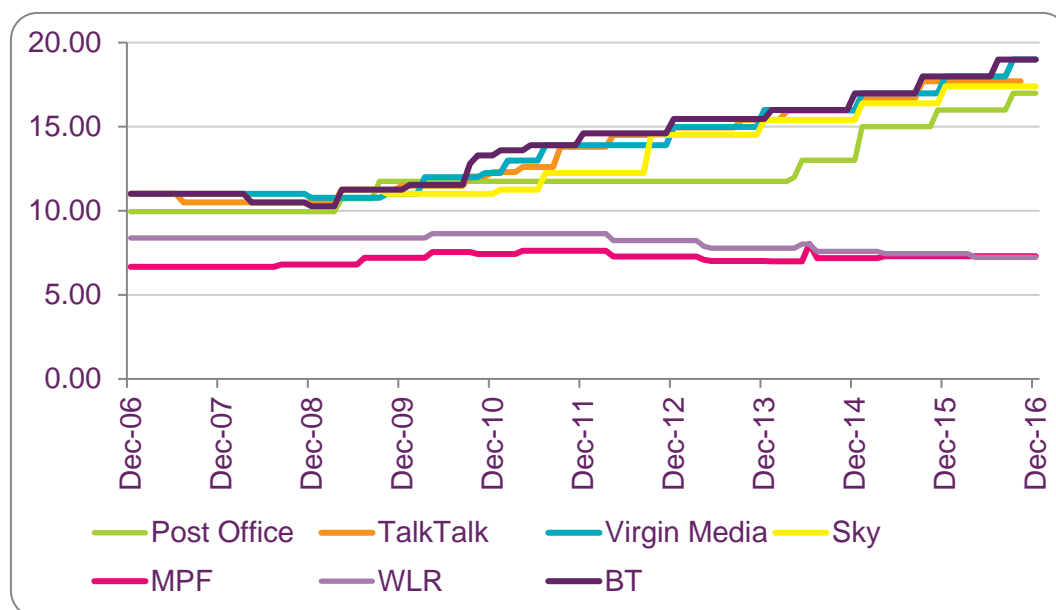


Source: Ofcom/Pure Pricing UK Broadband Updates

Notes: Adjusted for CPI; excludes line rental saver pre-payment tariffs

A8.60 Figure A8.24 below shows the line rental prices in nominal terms, i.e. without adjusting for inflation, since December 2006. These are the line rental prices and changes that would have been visible to consumers in the market.

<sup>125</sup> For the CPs behind the data we have on average call plan prices (i.e. BT, Sky, TalkTalk and Virgin Media) as discussed in paragraphs A8.80–A8.102 (Call plan prices), monthly line rental prices have increased, on average, 17% in real terms between the end of 2012 and the end of 2016 (or an annual average increase of 4%). This is equivalent to an average increase of £2.70 in real terms between the end of 2012 and the end of 2016.

**Figure A8.24: Wholesale and retail line rental price movements (£/month)**

Source: Ofcom/Pure Pricing UK Broadband Updates

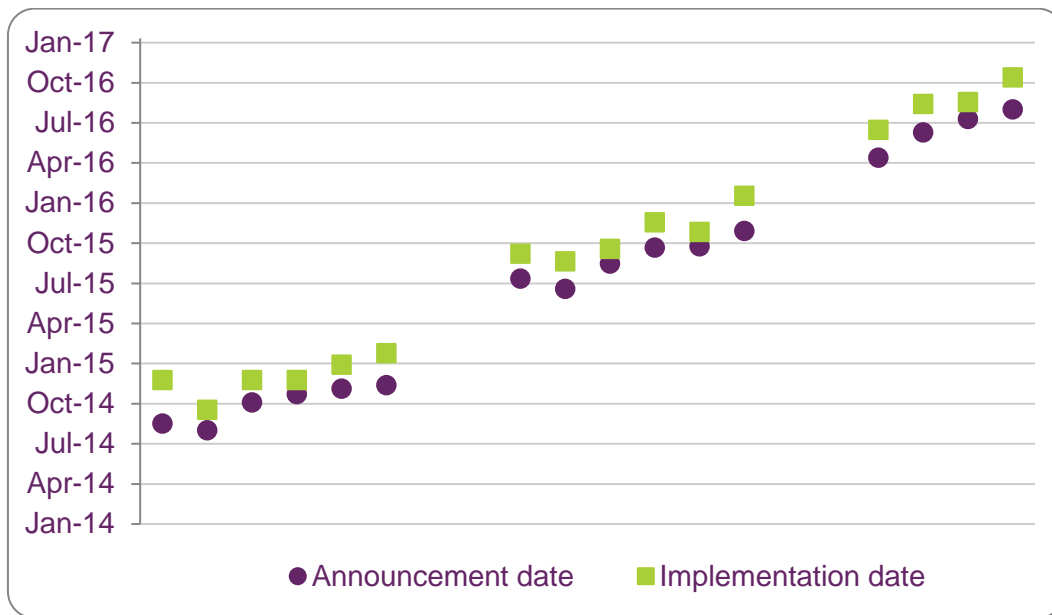
Notes: excludes line rental saver pre-payment tariffs

### Timing of line rental price increases

- A8.61 Next we outline the timings of CPs' announcements, and implementation, of line rental price increases. The price increases discussed here relate to prices charged to CPs existing customer bases, rather than prices offered to new customers.<sup>126</sup> The announcement and implementation dates were collected from ispreview.co.uk, an independent internet service provider review website which publishes articles informing readers of telecoms price increases. Where the announcement date of the price increase is not stated in the article, we have used the publication date of the article as a proxy for the announcement date. Where possible, we have checked these dates and/or months against (a) internal pricing documents we received from BT, Sky and TalkTalk and (b) other press sources of price increases. Information from these sources is consistent with the price increases and dates from ispreview.co.uk.
- A8.62 Figure A8.25 below shows the announcement and implementation dates of line rental price increases across the main CPs, with each pair of data points for announcement and implementation dates relating to a supplier. In the past three years, price increase announcements have typically clustered within a four to five-month period, followed by at least a five-month period of no price increases (with implementation following within months of the announcement).

<sup>126</sup> In a small number of instances, suppliers implement the price increases to new customers 2-3 months prior to the price increase for existing customers. Therefore, the timings of these increases do not necessarily correspond to the price increase dates in Figure A8.24

**Figure A8.25: Line rental price increase announcement and implementation dates, 2014 - 2017**



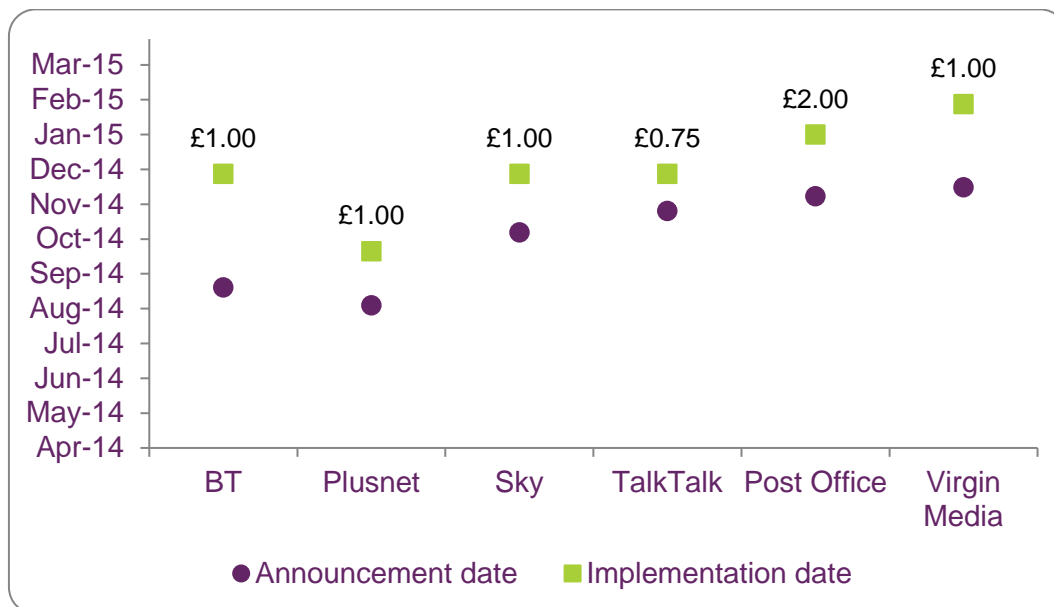
Source: [ispreview.co.uk](http://ispreview.co.uk), <https://www.lovemoney.com/> (TalkTalk 2015 source)  
<http://www.moneysavingexpert.com> (Plusnet 2014 source)

A8.63 As Figures A8.26, A8.27 and A8.28 show below, BT has typically announced and implemented its line rental price increases before any other supplier over the past three years. Other suppliers then appear to follow BT in the subsequent months.<sup>127</sup> CPs typically increase their line rental by the same amount (usually by £1.00 per month) on an annual basis. The data labels represent the size of the line rental price increase.

<sup>127</sup> The exception to this is Plusnet's announcement and implementation in 2015. However, BT Group has owned Plusnet since 2007.

Line rental price increases in 2014/15

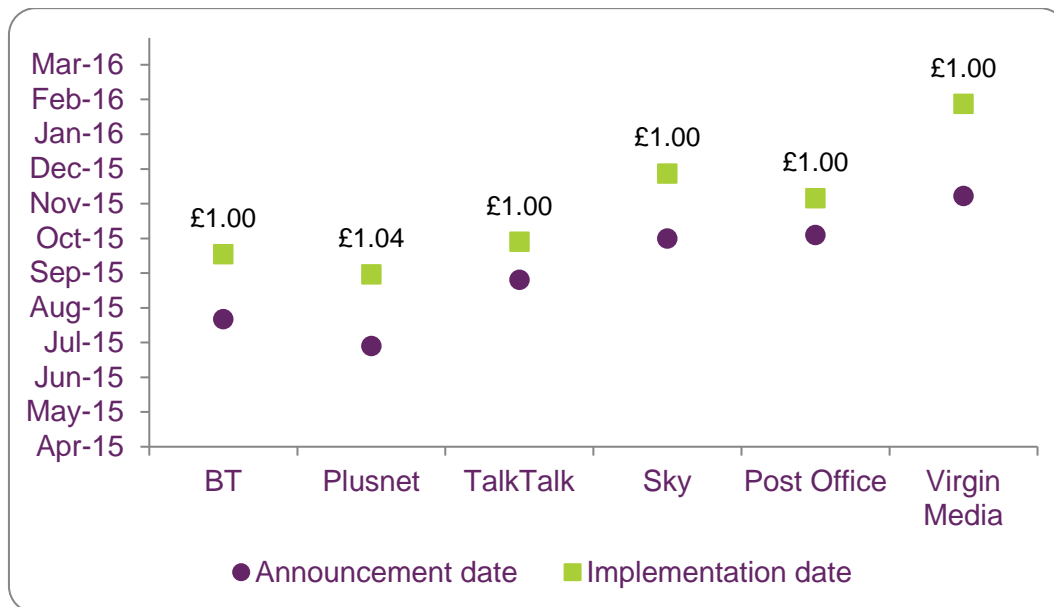
**Figure A8.26: Line rental price increase announcement and implementation dates, 2014/15**



Source: *ispreview.co.uk*

Line rental price increases in 2015/16

**Figure A8.27: Line rental price increase announcement and implementation dates, 2015/16**



Source: *ispreview.co.uk*, *www.lovemoney.com* (TalkTalk source)

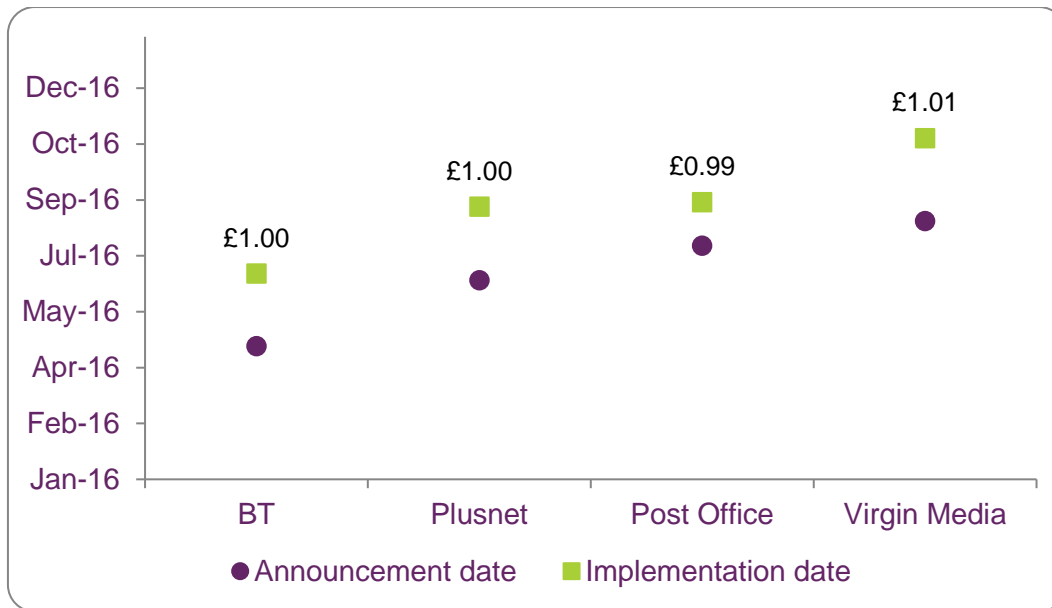
Line rental price increases in 2016/17

A8.64 In January 2017 Sky announced it is increasing the line rental price by £1.59 to £18.99. This price will not affect SFV customers, who will pay a price of £17.40. This is the case for both existing and new SFV customers with Sky.



A8.65 TalkTalk did not increase line rental in 2016 and stopped advertising line rental as a distinct price, following the ASA ruling (see Section 2, paragraph 2.3).

**Figure A8.28: Line rental price increase announcement and implementation dates, 2016**



Source: *ispreview.co.uk*

Notes: Following the ASA ruling outlined in Section 2, paragraph 2.3, TalkTalk stopped advertising a distinct line rental price in November 2016. For this reason, TalkTalk are excluded.

### Discussion of line rental increases in CPs' internal documents

A8.66 Our 1<sup>st</sup> s.135 request to CPs included the request:

A8.67 *“Please provide any documents submitted to your internal governance body responsible for approving the prices for Residential Analogue Voice-Only Retail Lines or Residential Analogue Voice Retail Lines Sold Under a Separate Contract, over the last three years, and any documents recording the final decision of that body, relating to the setting of prices for these lines.”*

A8.68 In the following section, we discuss the information which CPs provided to us in response to this request.

#### BT line rental pricing decisions

A8.69 [redacted].<sup>128</sup>

A8.70 [redacted].

A8.71 [redacted].<sup>129</sup> [redacted].

A8.72 [redacted].

<sup>128</sup> [redacted].

<sup>129</sup> Some parts of the documents were redacted.

A8.73 [redacted].<sup>130</sup> [redacted].<sup>131</sup> [redacted],<sup>132</sup> [redacted].<sup>133</sup> 134

A8.74 [redacted].<sup>135</sup> [redacted]<sup>136</sup>

### Other suppliers' line rental pricing decisions

A8.75 [redacted].

A8.76 [redacted]. [redacted]. [redacted].<sup>137</sup> [redacted].<sup>138</sup> [redacted]. [redacted].<sup>139</sup>

A8.77 [redacted]. [redacted].<sup>140</sup> [redacted].<sup>141</sup> [redacted]. [redacted]. [redacted].<sup>142</sup> [redacted].<sup>143</sup>

A8.78 [redacted].<sup>144</sup> [redacted]. [redacted].<sup>145</sup> [redacted].<sup>146</sup> [redacted]. [redacted].<sup>147</sup>

A8.79 [redacted]. [redacted].<sup>148</sup>

### **Retail call prices**

A8.80 SFV customers typically buy a package which includes line rental and a call plan. The line allows customers to make and receive calls, while the call plan provides customers with an allowance to make calls to fixed lines at no additional cost.

A8.81 The package specifies what is included in the call allowance. This is usually set in terms of the times of the day and/or the week when calls be made (e.g. evenings and weekends) rather than specifying a limit on the total number of call minutes. The package also specifies the prices (a set-up fee per call and a price per minute) of calls outside the call plan for fixed lines and mobiles, respectively.

A8.82 For a given supplier – including BT – the stated line rental price is the same across different packages, as are the unit costs of out-of-plan calls.

A8.83 Given the different ways in which consumers are charged for calls, examining overall price changes can be difficult. We first set out how the prices of different types of calls have changed over time for call plans and out-of-plan calls separately, before looking at changes in both in summary and finally, trying to get a sense of overall changes for calls both in and out-of-plans using a proxy measure of non-

<sup>130</sup> Response dated 18 November 2016 to question 3 of the 1<sup>st</sup> BT s.135, 3(a).

<sup>131</sup> Response dated 18 November 2016 to question 3 of the 1<sup>st</sup> BT s.135, 3(b).

<sup>132</sup> Response dated 18 November 2016 to question 3 of the 1<sup>st</sup> BT s.135, 3(c).

<sup>133</sup> Response dated 18 November 2016 to question 3 of the 1<sup>st</sup> BT s.135, 3(a).

<sup>134</sup> [redacted].

<sup>135</sup> Response dated 18 November 2016 to question 3 of the 1<sup>st</sup> BT s.135, 3(b).

<sup>136</sup> Response dated 18 November 2016 to question 3 of the 1<sup>st</sup> BT s.135, 3(b).

<sup>137</sup> Response dated 29 November 2016 to question 3 of the 1<sup>st</sup> Post Office s.135.

<sup>138</sup> Response dated 29 November 2016 to question 3 of the 1<sup>st</sup> Post Office s.135.

<sup>139</sup> Response dated 29 November 2016 to question 3 of the 1<sup>st</sup> Post Office s.135.

<sup>140</sup> Response dated 8 December 2016 to question 3 of the 1<sup>st</sup> Sky s.135.

<sup>141</sup> Response dated 8 December 2016 to question 3 of the 1<sup>st</sup> Sky s.135.

<sup>142</sup> Response dated 8 December 2016 to question 3 of the 1<sup>st</sup> Sky s.135.

<sup>143</sup> Response dated 8 December 2016 to question 3 of the 1<sup>st</sup> Sky s.135

<sup>144</sup> Response dated 13 January 2017 to question 6 of the 1<sup>st</sup> SSE s.135.

<sup>145</sup> Response dated 13 January 2017 to question 6 of the 1<sup>st</sup> SSE s.135.

<sup>146</sup> Response dated 13 January 2017 to question 6 of the 1<sup>st</sup> SSE s.135.

<sup>147</sup> Response dated 13 January 2017 to question 6 of the 1<sup>st</sup> SSE s.135.

<sup>148</sup> Response dated 8 December 2016 to question 3 of the 1<sup>st</sup> TalkTalk s.135.

access revenue per minute. We set out below further detail on call price changes across all fixed voice customers:

- 8.83.1 First, we set out changes in the prices of different call plans from different providers. This covers call plans offering weekend and evening calls and free international calls, as well as plans offering discounted international and mobile calls. We consider overall average price changes, as well as those for particular CPs. This data comes from Simplify Digital.
- 8.83.2 Second, we consider out-of-bundle calls. This includes pricing data from Simplify Digital for particular calls types. Again, this considers both average prices in the market and prices for individual CPs. We also set out changes in revenue per minute for out-of-plan calls for different providers to give an indication in overall out-of-bundle call price changes. This is based on Ofcom telecoms market data updates.<sup>149</sup>
- 8.83.3 Finally, we set out data on non-access revenue per minute as a proxy for changes in call prices overall. This is based on data received from BT, Post Office, SSE, Sky, TalkTalk and Virgin Media in response to s.135 information requests.

### Call plan prices

- A8.84 Regarding call plans, Figure A8.35 shows that the average price of evening and weekend plans increased by 52% in real terms between the end of 2012 and the end of 2016 (an annual average increase of 11%), while the average price of anytime call plans increased 32% for the same period (an annual average increase of 7.3%).
- A8.85 These figures suggest that call plan prices have increased significantly more, in relative terms, than line rental prices.<sup>150</sup> However, the increase in call plan prices is less significant in absolute terms (monthly call plan prices were, on average, £1.70 more expensive in real terms by the end of 2016 than they were by the end of 2012 (compared to £2.70 for line rental).
- A8.86 We have examined further the prices for four call plans from a number of different CPs. This is based on data from Simplify Digital, whose data allows an analysis of overall trends in tariffs, as well as specific types of call plans. We note that this analysis only covers certain CPs, and only certain call plans for which we have data and so is indicative only.
- A8.87 Figure A8.29 shows the prices for Weekend & Evening call plans from BT, Sky and Virgin. BT has increased its per month prices for these plans by approximately £1.45 (71%) over the last three years, compared to an increase of £0.29 (6%) by Virgin over the same period and a £0.06 (2%) decrease by Sky between 2015 and 2016 in real terms.<sup>151</sup> However, over the whole period shown, BT's monthly prices have only increased by 6%, compared to 52% across the market. Further, BT's monthly prices are still below those of these other providers by £0.50-£1.50 (12.5%-

<sup>149</sup> <https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates>

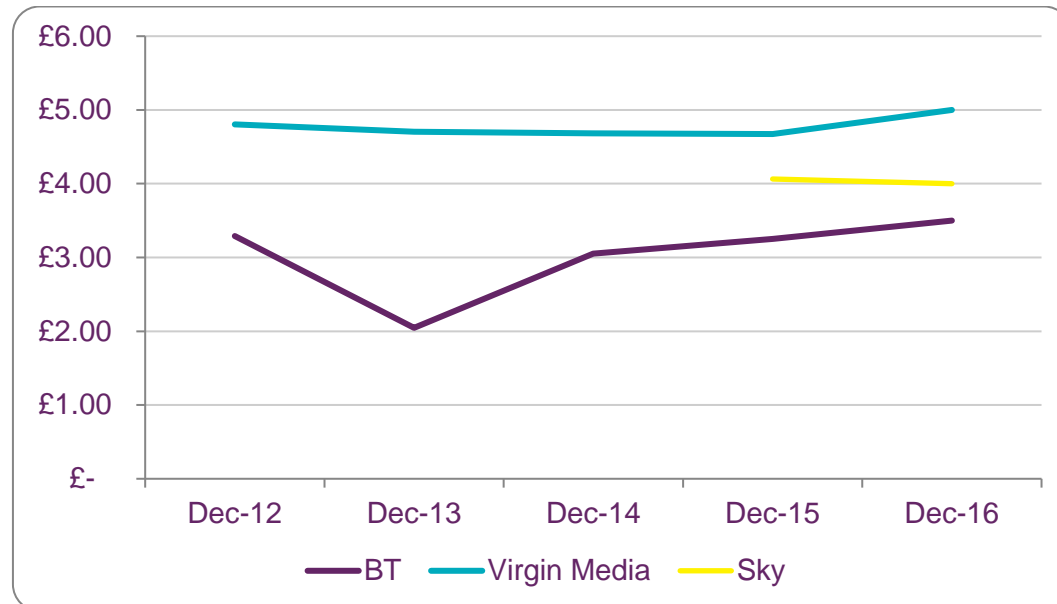
<sup>150</sup> As mentioned in footnote 125 to paragraph A8.59, the monthly line rental prices of BT, Sky, TalkTalk and Virgin Media increased, on average, 17% in real terms between the end of 2012 and the end of 2016 (or an average annual increase of 4%). This is equivalent to an average increase of £2.70 in real terms between the end of 2012 and the end of 2016.

<sup>151</sup> Sky's prices were constant in nominal terms.

30%), and below the average across the market shown in Figure A8.35 below (£3.50 vs. £4.17 in December 2016 prices).

A8.88 As noted above, this does not include all CPs, such as Post Office. We note that such providers do offer similar packages,<sup>152</sup> but we do not have data on how these have changed over time.

**Figure A8.29: Weekend & Evening call plan prices (£/month), December 2016 prices**



Source: Simplify Digital. Data as at end of the year

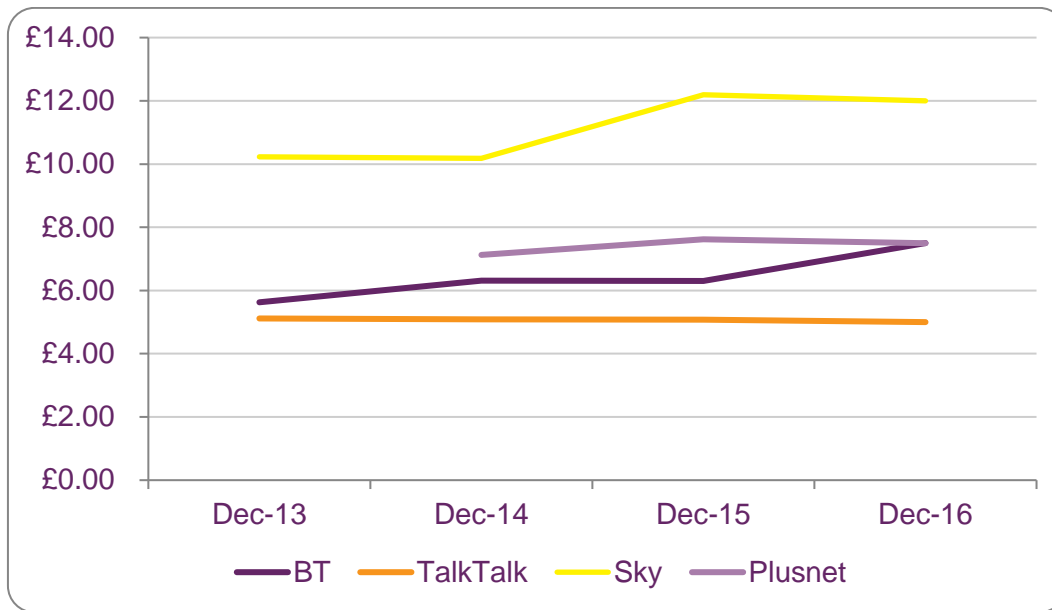
A8.89 “Free international calls” packages allow subscribers to make international calls at no extra charge above the package price. Figure A8.30 shows the prices for free international calls packages for BT, Sky, Plusnet (which is owned by BT and used as a ‘value brand’) and TalkTalk between 2013 and 2016. We note that Virgin had also introduced a similar plan by the end of 2016, priced at £15. The figure shows that BT and Plusnet’s prices have been below those of Sky over this period, while TalkTalk’s prices were the lowest among these providers throughout the period.

A8.90 All of these providers except TalkTalk have raised prices since the end of 2014. Sky had the largest real terms price increase in absolute terms (an increase of £1.82 on the per month price, or 18%) although it was similar in percentage terms to that of BT (£1.19, or 19%). Plusnet increased its prices by a much lower amount, both in absolute and percentage terms (£0.37, or 5%). TalkTalk’s prices have been constant in nominal terms, and so have decreased in real terms due to inflation (by 2%).

A8.91 Again, we note that this does not cover every CP in the market due to data limitations.<sup>153</sup>

<sup>152</sup> For example, Post Office offers an evening and weekend plan for £2.50 per month, which also includes calls made during these times to certain international destinations. See <http://www.postoffice.co.uk/broadband-phone/home-phone> (accessed 13 February 2017).

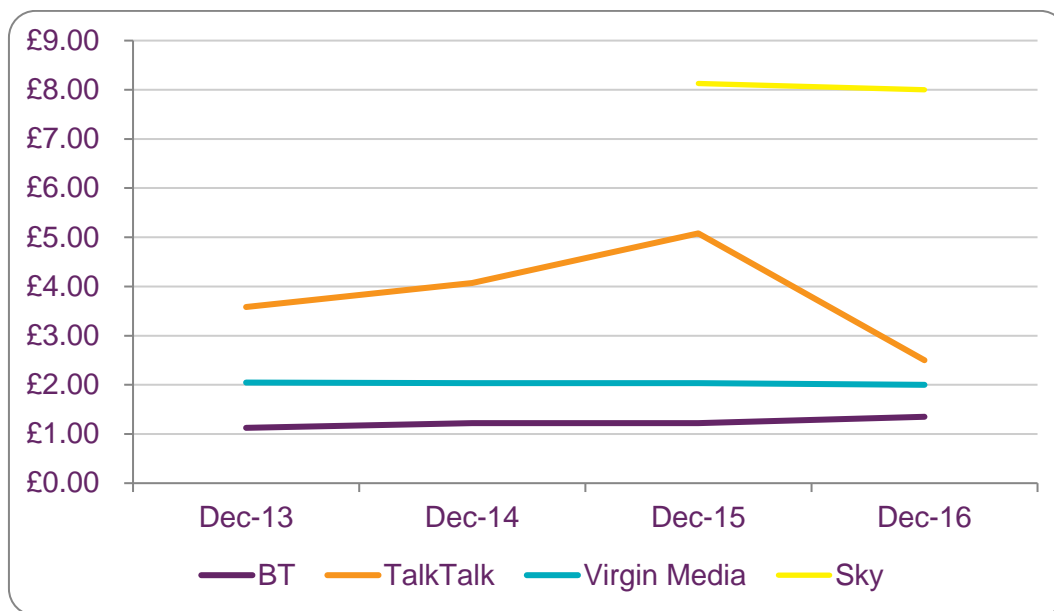
<sup>153</sup> For example, Post Office offers an International Saver tariff for £4 per month. See <http://www.postoffice.co.uk/broadband-phone/home-phone> (accessed 13 February 2017).

**Figure A8.30: Free International call plan prices, December 2016 prices**

Source: Simplify Digital. Data as at end of the year

- A8.92 “Discounted international calls” packages give subscribers a lower per minute cost for international calls. BT’s prices are the lowest of the providers shown at £1.35 by the end of 2016, compared to £2 and £2.50 for Virgin and TalkTalk respectively. Sky’s price for this plan is significantly higher than the other providers shown at £8 in 2016.
- A8.93 BT prices increased slightly between December 2013 and December 2016 in real terms (by £0.22 or 20%). Prices for Virgin and Sky have fallen by a small amount (Virgin reduced its price by £0.05 or 2% over this period, while Sky’s price fell by £0.13, a reduction of 2% between December 2015 and December 2016). TalkTalk increased its prices substantially between December 2013 and December 2015 (by £1.50 or roughly 40%), before more than halving them during 2016 to £2.50.
- A8.94 Evidence on these two call plans indicates BT is not particularly highly priced for international calls.

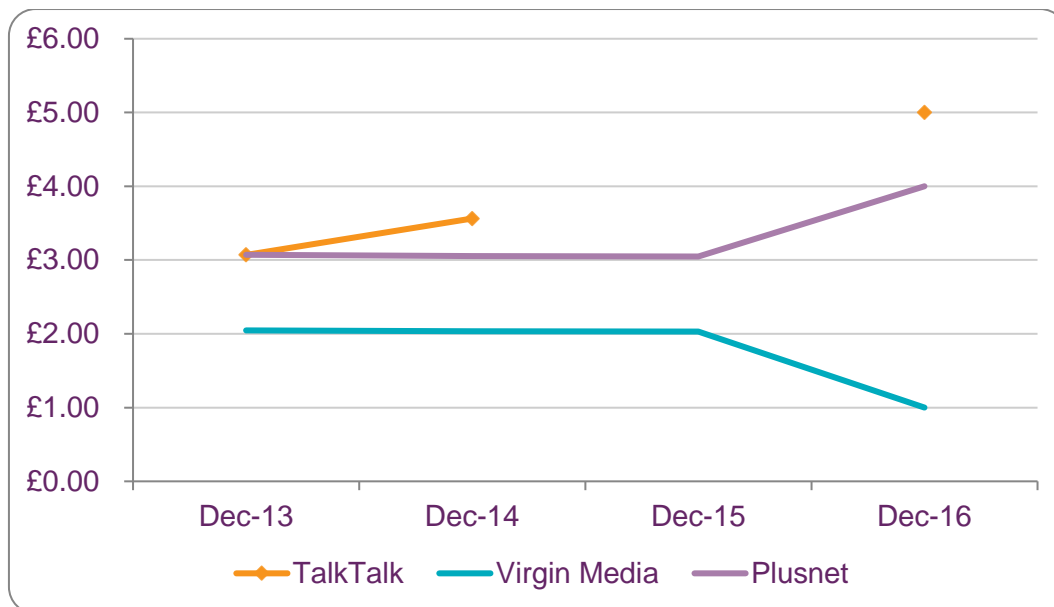
**Figure A8.31: Discounted International call plan prices, December 2016 prices**



Source: Simplify Digital. Data as at end of the year

A8.95 Finally, we have information on plans for discounted calls to mobiles. As for the other plans, this only covers a small number of CPs. In particular, our data on these plans do not include BT. However, it does include Plusnet, which is owned by BT. This data is set out in Figure A8.32.

**Figure A8.32: Discounted Mobile call plan prices, December 2016**



Source: Simplify Digital. Data as at end of the year

A8.96 TalkTalk’s prices for this call plan were higher than those of Plusnet and Virgin over this period. There is no price data for TalkTalk in December 2015. However, by December 2016 TalkTalk’s price had increased to £5, compared to £4 for Plusnet and £1 for Virgin. Plusnet’s 2016 price represented an increase of more than 30% on previous years, where prices were stable at £3 in nominal terms (therefore falling

slightly in real terms due to inflation). Virgin meanwhile reduced its prices in 2016 by £1, or roughly half.

### Out-of-plan calls

A8.97 Regarding out-of-plan calls, Figure A8.35 shows that the average price of UK geographic calls<sup>154</sup> increased 29% in real terms between 2012 and 2016 (an annual average increase of 6.5%). That is quite similar to the increase in the average price of set-up fees (30% in real terms between 2012 and 2016, or an average annual increase of 6.7%). Call to mobile charges have been largely steady in real terms.

A8.98 Figure A8.33 sets out the prices for different out-of-plan call types by different providers, and the increase in prices between 2013 and 2016.

**Figure A8.33: Out-of-plan call prices**

Call Plan	BT		Sky		Plusnet		TalkTalk		Virgin Media	
	Dec 2016 price	% (2013 - 2016)	Dec 2016 price	% (2013 - 2016)	Dec 2016 price	% (2013 - 2016)	Dec 2016 price	% (2013 - 2016)	Dec 2016 price	% (2013 - 2016)
0845 numbers	£0.11	166.8%	£0.12	69.5%	£0.10	11.3%	£0.08	-18.5%	£0.11	7.6%
UK geographic day time	£0.11	33.2%	£0.12	26.3%	£0.13	45.7%	£0.13	35.8%	£0.12	18.0%
UK geographic evening	£0.11	166.8%	£0.12	26.3%	£0.13	45.7%	£0.13	35.8%	£0.12	92.3%
Mobile day time	£0.15	26.7%	£0.12	-12.0%	£0.13	2.1%	£0.13	1.8%	£0.19	-2.3%
Mobile evenings	£0.15	126.6%	£0.12	46.7%	£0.13	2.1%	£0.13	1.8%	£0.14	-2.3%
Call connection fee	£0.19	33.9%	£0.17	19.1%	£0.19	33.9%	£0.18	17.3%	£0.19	16.5%
NTS access fee	£0.11	-	£0.12	-	£0.10	-	£0.08	-	£0.11	-

Source: Simplify Digital

A8.99 We note the following from this data:

- BT's prices for 0845 numbers are in line with the market average shown in Figure A8.35, and similar to those of other providers shown above (within £0.01-£0.03 of all other providers shown). BT has seen a larger increase in these prices, as its prices were below the market average in 2013.
- BT's prices for UK geographic calls (£0.11) are broadly in line with the market average shown in Figure A8.35, and is similar (but £0.01 to £0.02 lower) than those of the other providers shown. Plusnet (which is owned by BT) by contrast has similar but slightly higher prices than others at £0.13. BT's price increases are among the highest of the providers shown, particularly for evening calls.<sup>155</sup>

<sup>154</sup> This refers to calls to UK fixed-line telephone numbers that begin with '01' and '02'.

<sup>155</sup> Comparison against changes the market averages shown in Figure A8.35 is more difficult as in previous years, because charges differed between daytime and evening calls.

- BT's prices for calls to mobiles are among the highest of the providers shown (lower only than Virgin's price for day time calls), but broadly in line with the average price shown in Figure A8.35. BT's price increases have also been higher than those of the other providers shown in Figure A8.33 above.
- BT's call connection fee is £0.19, the same as Plusnet and Virgin and slightly (£0.01-0.02) higher than TalkTalk and Sky. BT and Plusnet have seen the greatest increase in these prices at 33% between the end of 2013 and the end of 2016, where others have increased this price by between 10-20%. BT's price is also similar but slightly higher (by £0.01) than the average price shown in Figure A8.35, with a similar (but again slightly higher) increase (33% vs 28%).
- BT's NTS access fee is £0.11, £0.01 lower than that of Sky and £0.03 higher than TalkTalk. Separate NTS access fees were generally introduced in 2015, and so we do not have a comparison across time in the same way as for other call types.

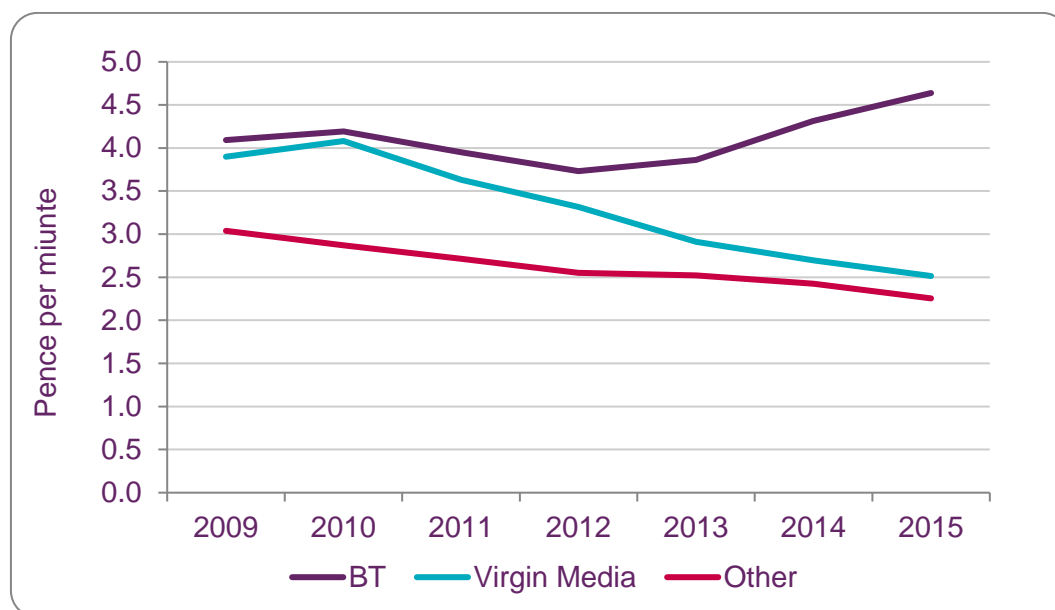
A8.100 In addition to comparing call tariffs over time, we have calculated changes to revenue per minute (RPM) in real terms across residential out-of-plan calls as a proxy for price. This is based on data from Ofcom's telecoms market updates, and so covers volumes and revenues across all fixed voice customers and all call types.

A8.101 The revenue figures used in these calculations only cover calls made out-of-plan;<sup>156</sup> volumes include calls made both in and out-of-plans. This is shown in Figure A8.34. Revenue per minute could differ from equivalent call prices (as set out in Figure A8.35) if usage patterns change over time, either in response to price changes or due to other factors.

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<sup>156</sup> This includes calls where a consumer did not purchase a call plan, even where a plan is available (e.g. daytime calls made by consumers not purchasing an 'anytime' call plan). This is based on the same data source as our analysis set out in Figure 3.13 in the 2016 NMR (available: [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0016/95011/Narrowband-Market-Review.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0016/95011/Narrowband-Market-Review.pdf)), but includes additional types of calls (such as special services, premium rate and directory enquiries).



**Figure A8.34: Residential out-of-plan call revenues per minute (Dec 2016 prices)**

Source: Ofcom/operators<sup>157</sup>

A8.102 This shows that BT's out-of-plan revenue per minute has been higher than that of other CPs across the period shown. It has particularly diverged since 2012. BT's out-of-plan revenue per minute increased by 24% between 2012 and 2015, while those for Virgin and other CPs declined by 24% and 12% respectively. There could be a number of reasons for this, such as BT increasing prices, changes in the types of calls made or changes in calling patterns between in- and out-of-plan calls.

#### Summary of market call prices for call plans and out-of-plan calls

A8.103 Figure A8.35 below presents the average retail call prices for a group of call plans and out-of-plan calls. The call prices data available to us (i.e. average call prices collected by Simplify Digital for BT, Sky, TalkTalk and Virgin Media customers) suggest that, between 2012 and 2015, most call prices have increased significantly above inflation. We do not have comparable pricing data for the period between deregulation (in 2009) and 2012.

A8.104 Call plans have increased well above inflation, with 11% year-on-year increases for Evenings and Weekends and over 7% for Anytime. Calls to UK numbers have also increased well above inflation, except for calls to mobiles which have been largely steady in real terms. This data does not include information on international calls.

A8.105 The pricing documents we received from suppliers<sup>158</sup> [redacted].

<sup>157</sup> See Ofcom's Telecoms data updates here: <https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates>

<sup>158</sup> See paragraphs A8.69-A8.74 (BT) and A8.75-A8.79 (Other suppliers) for a discussion of the pricing documents.

**Figure A8.35: Average retail call prices (in December 2016 prices)**

	2012	2013	2014	2015	2016	CAGR
<b>Call plan prices</b>						
Evening & weekend call plan (£/month)	£2.75	£3.38	£3.36	£4.00	£4.17	11.0%
Anytime call plan (£/month)	£6.04	£6.52	£7.00	£7.87	£8.00	7.3%
<b>Out-of-plan call prices</b>						
Call set-up fee (pence/call)	13.8p	14.0p	15.1p	17.4p	18.0p	6.7%
UK geographic call (pence/minute)	8.9p	9.4p	10.3p	11.3p	11.5p	6.5%
0845 0870 call (pence/minute)	9.3p	9.6p	7.3p	10.0p	10.3p	2.7%
Non-Three UK mobile call (pence/minute)	14.5p	14.2p	14.1p	14.2p	14.3p	-0.3%
Three UK mobile call (pence/minute)	17.7p	17.3p	17.3p	14.2p	14.3p	-5.2%

Source: Simplify Digital

Notes: Call plan prices do not include line rental. Data as at end of each year; figures are the CPI-adjusted average of the prices offered by BT, Sky, TalkTalk and Virgin Media.

### Non-access revenues per minute

A8.106 The above analysis is limited to only certain call types or plans due to data availability. We have also considered changes in revenues across all call types, using non-access revenue as a proxy.<sup>159</sup> Figure A8.36, below, presents the annual non-access revenues per minute by operator for the past three financial years.

**Figure A8.36: Non-access revenues per minute (£/minute, December 2016 prices)**

[X].

Source: s.135 responses

A8.107 [X].

A8.108 [X].

## **A description of current market offers**

A8.109 This section summarises the current market prices for SFV services. This lists line rental and call plan prices offered by active suppliers of SFV services. We also provide details on BT Basic, BT Home Phone Saver 2019 and Virgin Media Talk Protected.

<sup>159</sup> As stated in paragraphs A8.50, non-access revenue is an overestimate of call revenue because non-access includes revenues which are neither from calls nor access (e.g. charges for paper billing and ancillary services).

## Current standard line rental and call plan prices

A8.110 Figure A8.37 summarises the current prices for SFV services: monthly line rental (including annual pre-payment) and call plans.

**Figure A8.37: Prices for SFV services: line rental and call plans (per month)**

	Monthly line rental	Annual line rental pre-payment	Weekend calls (in addition to line rental)	Evening and weekend calls (in addition to line rental)	Anytime calls (in addition to line rental)
BT <sup>160</sup>	£18.99	£17.09	Inclusive	£3.50	£8.50
Phone Co-op	£17.00	£15.00	-	£3.00	£7.00
Direct Save Telecom	£15.95	£13.50	-	£2.95	£6.75
Fuel	£17.60	-	-	-	£3.00
Post Office <sup>161</sup>	£14.99*	-	Inclusive	£2.50	£7.00
Sky <sup>162</sup>	£17.40	-	-	£4.00	£8.00
SSE <sup>163</sup>	£13.50*	-	-	Inclusive	£2.25
Utility Warehouse	£17.35	-	-	Inclusive	£6.00
Virgin Media	£19.00	-	£1.00	£5.00	£8.00

Source: Operator websites (accessed 1 February 2017).

Notes: asterisk indicates a promotional price.

## BT Basic

A8.111 BT offers a SFV service called BT Basic, which is a tariff for vulnerable consumers. BT offers a separate service called BT Basic + Broadband, which is a dual-play variant of the SFV BT Basic service. To qualify for BT Basic, a customer must be receiving one of the following benefits:

- Income Support;
- Income-based Job Seekers Allowance;
- Pension Credit (Guaranteed Credit);
- Employment and Support Allowance (income related); and
- Universal Credit (and are on zero earnings)

<sup>160</sup> BT has announced a series of changes to its voice service prices, due to come into effect from 2 April 2017. The price of Unlimited Anytime Calls will rise by 49 pence to £8.99 and Evening and weekend calls will rise by 30 pence to £3.80. BT has held the price of line rental and Line Rental Saver at £18.99 per month and £205.09 per annum, respectively.

<sup>161</sup> The price currently offered by Post Office is a promotional price, and is being offered until 2 April 2017. This promotional price applies to a 12-month contract, after which customers will pay the standard price for line rental with inclusive weekend calls of £16.99.

<sup>162</sup> All Sky customers, except SFV customers, pay the new line rental price of £18.99.

<sup>163</sup> The price currently offered by SSE is a promotional price, and is being offered until 29 June 2017. The standard price for line rental with inclusive evening and weekend calls is £18/month. The standard price of its anytime calls package is £3.00.

A8.112 The line rental price for BT Basic customers is £5.10 per month (27% of BT's standard monthly line rental of £18.99), which includes a call allowance of £1.50 which would allow a customer to make around ten one-minute calls or one thirteen-minute call in a month.<sup>164</sup> Calls beyond this allowance can be made at an additional cost, which has a monthly cap of £10, subject to a Fair Use policy.<sup>165</sup>

A8.113 There are around [X] SFV lines supplied to BT Basic customers.<sup>166 167</sup>

### Home Phone Saver 2019

A8.114 BT offers a product called Home Phone Saver 2019, which bundles line rental, calls and additional features together in a package.<sup>168</sup> This is a standalone service, i.e. it is not offered as part of any bundle with broadband from BT. This product is offered at a price of £21.99 per month, which is fixed until 2019.<sup>169</sup> Figure A8.38 below compares Home Phone Saver 2019 with the individual prices of the products and features included in Home Phone Saver 2019.

A8.115 In September 2016, there were around [X] lines supplied to Home Phone Saver customers, accounting for [X]% of BT's SFV lines (excluding BT Basic).<sup>170</sup> The number of BT customers on Home Phone Saver in September 2016 has increased by [X]% compared to September 2015.

A8.116 A customer purchasing these SFV services at standard prices could make substantial savings by taking up Home Phone Saver 2019. A customer who purchases standard line rental and unlimited anytime calls from BT could save £5.50/month by switching to Home Phone Saver 2019. After the price of Unlimited Anytime Calls increases on 2 April 2017, this saving would increase to £5.99. A customer who purchases all of the products included with Home Phone Saver 2019, on an individual basis at standard prices could save up to £13.05/month by switching to Home Phone Saver 2019. This potential saving would increase following BT's price increase would increase the potential saving to £13.54/month. However, for customers purchasing line rental and weekend calls, Home Phone Saver 2019 is more expensive than their current plan, while for those purchasing line rental, evening and weekend calls, Home Phone Saver is 50p cheaper per month (assuming no out-of-plan calls).

<sup>164</sup> BT Basic line rental does not include free weekend calls.

<sup>165</sup> If a customer exceeds the call allowance, they are charged 11.3 pence per minute (plus 3.3 pence for each phone call) for all normal UK calls.

<sup>166</sup> BT estimated that there are around a further [X] BT Basic + Broadband customers (*source: BT presentation to Ofcom, 30 October 2016*).

<sup>167</sup> Source: s. 135 response data.

<sup>168</sup> There are a number of iterations of Home Phone Saver, signalled by the associated date.

<sup>169</sup> Source: Operator website (accessed 31 January 2017).

<sup>170</sup> Source: s. 135 response data.

**Figure A8.38: Comparison of Home Phone Saver 2019 with individual product prices**

	BT Home Phone Saver 2019	Individual standard prices
Line rental	Included	£18.99/month
Unlimited Anytime Calls <sup>171</sup>	Included (for up to an hour)	£8.50/month <sup>172</sup>
Inclusive calls to 0845 and 0870 numbers at any time	Included (for up to an hour)	Included
1471 call returns	Included	26.5p charge plus the cost of the call
BT Privacy with Caller Display	Included (when you opt-in)	£1.75/month
Anonymous Call Reject	Included (when you opt-in)	£5.80/month
<b>Total</b>	<b>£21.99</b>	<b>£35.04/month</b>

Source: Operator website (accessed 1 February 2017).

### BT Line Rental Saver

A8.117 BT offer an SFV product called Line Rental Saver, which offers BT customers 10% off the price of 12 months of standard line rental when paying up front. Therefore, instead of paying the monthly rate of £18.99 for 12 months (£227.88 per annum) Line Rental Saver customers pay a single (non-refundable) instalment of £205.08 (which equates to £17.09 per month). Line Rental Saver is not compatible with Home Phone Saver are unable to receive, i.e. the annual price of Home Phone Saver cannot be paid up front in order to receive a 10% discount.

### Virgin Media Talk Protected

A8.118 Virgin Media has launched a new product called Talk Protected, which freezes the line rental price at £17.99, for elderly and disabled customers. In addition, customers will receive additional benefits, such as inclusive evening and weekend calls to UK landlines and mobiles and inclusive voicemail and caller display, among other benefits. Customers who are identified as being eligible for this plan will have been automatically upgraded to Talk Protected after 10 January 2017. To qualify for Talk Protected a customer must be identified as being over 65, or have additional accessibility needs including limited hearing, sight, speech and mobility.

## Estimates of revenue per line

A8.119 In this section we estimate the revenue per line, across CPs.

A8.120 Figure A8.39 presents SFV total revenue per line figures, calculated by dividing SFV total revenues by the number of SFV lines for BT, Post Office, SSE, TalkTalk, Virgin Media, Sky and the Phone Co-op.

**Figure A8.39: SFV total revenue per line (in December 2016 prices)**

[X]

Source: s.135 responses

<sup>171</sup> Calls to non-BT phone mobile numbers incur a charge of 7.5 pence per minute in the Unlimited Anytime Calls package, compared with 15 pence per minute under Home Phone Saver 2019.

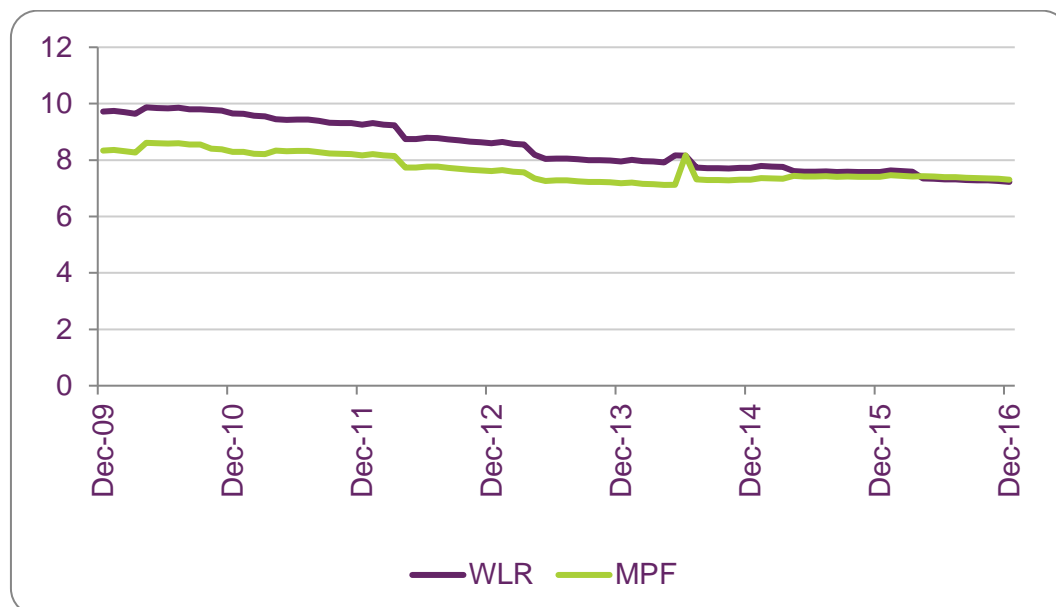
<sup>172</sup> This price will increase to £8.99 on 2 April 2017.

- A8.121 BT's revenue per line from access and calls is the highest in the market, and has [X] per month in 2015/16, in December 2016 prices. This represents an [X]% increase above inflation over two years. During the same period, BT's access revenue has increased its share of revenue per line from [X]% to [X]%.
- A8.122 In Annex 5 (Figure A5.4), we show the breakdown of BT's revenues per line between line rental and calls. This indicates that, [X].
- A8.123 [X]. Revenue per line is lower for all other CPs than BT by between £[X] and £[X] per line per month.] We do not have sufficiently granular data on other CPs' revenues to tell whether these changes are due to changes in access or call revenues, or a combination of both.

## Evidence on wholesale market prices

- A8.124 Suppliers use different access and call services at the wholesale level in order to provide access and calls to SFV customers at the retail level. When they buy these inputs they pay wholesale market prices.
- A8.125 Regarding access inputs, suppliers that rely on BT's copper network pay Openreach (BT's wholesale access division) for Wholesale Line Rental (WLR) or Metallic Path Facility (MPF). WLR allows only the provision of voice services, while MPF allows both voice and broadband services to be provided. Suppliers, such as Virgin Media, that have their own network may use it to provide access to its SFV customers.<sup>173</sup>
- A8.126 Between 2009 and 2016 BT's WLR and MPF prices decreased significantly. WLR prices fell 26% in real terms between 2009 and 2016 (MPF prices fell 12%). Figure A8.40, below, presents WLR and MPF prices.

**Figure A8.40: BT's WLR and MPF prices (£/month in December 2016 prices)**



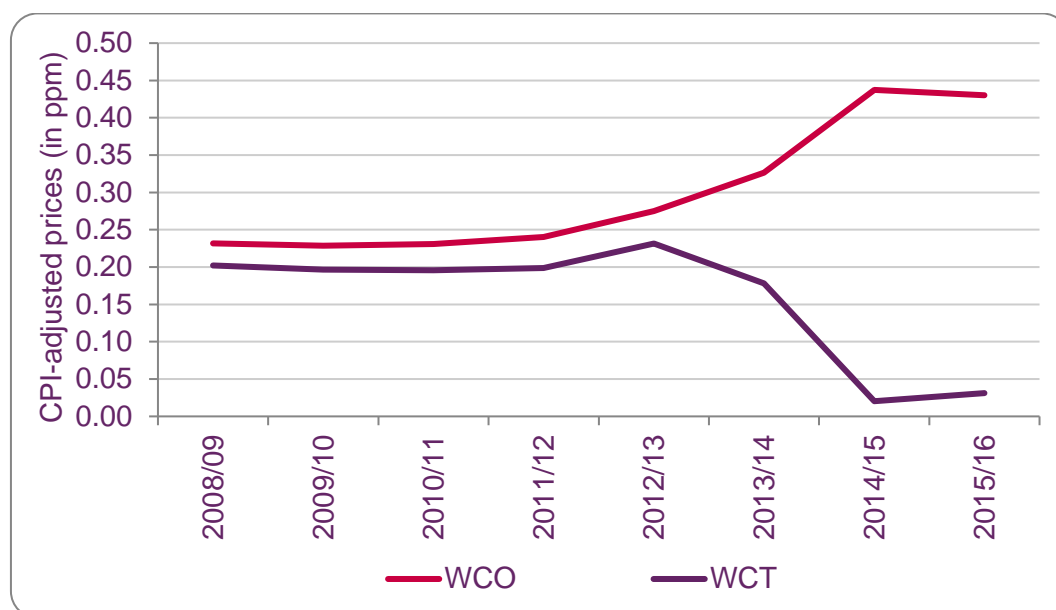
<sup>173</sup> We are also aware that generally CPs that have their own network may still rely on BT's copper network to provide voice - it is common, some CPs rarely use their own LLU network to provide voice-only services.

Source: *BT Openreach*

A8.127 Regarding call inputs, suppliers most commonly purchase Wholesale Call Origination (WCO) from BT, and Wholesale Call Termination (WCT) from either BT or other fixed telecoms suppliers. WCO is a service that enables SFV customers to make calls over their lines, while WCT enables these customers to terminate their calls to UK geographic numbers (a number starting 01 or 02).

A8.128 Between 2008/09 and 2015/16 BT's WCO and WCT prices have changed significantly in real terms. BT's WCO increased 86% in real terms between 2008/09 and 2015/16, while BT's WCT fell 84% in real terms. Figure A8.41, below, presents WCO and WCT prices.

**Figure A8.41: BT's WCO and WCT prices (March 2016 prices)**



Source: *BT Regulatory Financial Statements*

## Comparisons of SFV prices with dual-play prices

A8.129 In this section we compare the prices voice-only customers and split purchasers are paying for their services with the prices of dual-play services.

### Voice-only customers

A8.130 Figure A8.42 below compares the SFV access price (line rental) with the cheapest available dual-play price. In comparison to the price of SFV access, the price of a dual-play service with ADSL broadband sold at a promotional price is on average £6.18 (35%) more expensive per month, while dual-play with ADSL sold at a standard (non-promotional) price is £13.98 (79%) more expensive.

**Figure A8.42: Line rental and promotional and standard dual-play prices (£/month)**

	(1) Monthly line rental	(2) Cheapest promotional dual-play price	(3) Cheapest standard dual-play price	(2) – (1) Difference to promotional dual-play price	(3) – (1) Difference to standard dual-play price
BT	18.99	24.99	33.99	6.00	15.00
Phone Co-op	17.00	22.00	27.00	5.00	10.00
Post Office	14.99*	20.99	26.99	6.00	12.00
Sky	17.40	18.99	28.99	1.59	11.59
SSE	13.50*	19.50	26.00	6.00	12.50
TalkTalk	17.70	£22.95	£22.95	£5.25	£5.25
Virgin Media	19.00	32.00	40.00	13.00	21.00
<b>Weighted average</b>	<b>17.80</b>	<b>23.99</b>	<b>31.78</b>	<b>6.18</b>	<b>13.98</b>

Source: Operator websites (accessed 20 February 2017). TalkTalk price based on latest available data.<sup>174</sup>

Notes: \*asterisk indicated promotional line rental price. Price differences are weighted by the estimated number of voice-only customers with each CP. All promotional prices apply to a 12-month period. All dual-play prices are for speed of 17Mb, i.e. ADSL, except for Virgin Media (50Mb – the lowest speed offered).

### Split purchasers

A8.131 As outlined in paragraph A8.26, we received s.135 data for [redacted] standalone fixed broadband customers from BT, Sky and TalkTalk. This contained information on the broadband speed, usage allowances and prices provided to these customers.<sup>175</sup>

A8.132 [redacted]. [redacted].<sup>176, 177</sup> In total, around 93% of standalone fixed broadband customers, supplied by BT, Sky and TalkTalk, receive a standalone fixed broadband with a speed of 17Mb.<sup>178</sup> Figure A8.43 below shows the price for each standalone broadband service (in terms of speed and usage limit) provided by BT, Sky and TalkTalk. We present average price, weighted by the number of customers on each speed, usage and price combination, for each standalone fixed broadband service. In some instances, customers receiving the same service are paying different prices. In addition, this Figure shows the prices of dual-play bundles from the standalone broadband supplier, which includes broadband with equivalent speed and usage and line rental to the standalone broadband service in the same row.

A8.133 Figure A8.43 shows that on average standalone fixed broadband customers pay around £20 for a fixed broadband service and a further £18.99 for line rental.<sup>179</sup>

<sup>174</sup> PurePricing

<sup>175</sup> However, we exclude around [redacted] of these customers, for reasons explained in footnotes 176 - 177. To receive standalone fixed broadband from these CP's a customer must be taking an SFV line, and are by definition a split purchaser.

<sup>176</sup> We exclude customers who receive a standalone fixed broadband service from BT (a) free of charge, (b) which has a speed of 100Mb+ and (c) where the price and service combinations are provided to fewer than 100 customers.

<sup>177</sup> We exclude around [redacted] Sky customers who take a 17Mb/2Gb service and a 6Mb/Unlimited service, since there is no closely comparable dual play product, in terms of speed/usage combinations.

<sup>178</sup> Approximately 85% of these customers had unlimited usage, whilst 15% have a capped usage.

<sup>179</sup> We use a line rental price of £18.99, since we estimate that the majority of split purchasers take their line from BT.



Compared to the average dual-play prices which split purchasers would pay if they bundled these services, they are paying an average of just over £14.50 more per month (compared to promotional dual-play prices) or £8 more per month (compared to standard dual-play prices) by buying them as standalone services.

**Figure A8.43: Standalone fixed broadband and dual-play prices (£/month): BT, Sky and TalkTalk**

	(1) Standalone fixed broadband weighted average price (31/10/2016)	(2) Standalone fixed broadband plus line rental (£18.99)	(3) Dual-play: promotional price (per month)	(4) Dual- play: standard price (per month)	(5) = (2)–(3) Price difference for split purchaser compared to promotional dual-play price	(6) = (2)–(4) Price difference for split purchaser compared to standard dual-play price
<b>BT</b>						
17Mb/12Gb	24.80	43.79	24.99*	33.99	18.80	9.80
17Mb/25Gb <sup>180</sup>	24.00	42.99	24.99*	33.99	18.00	9.00
17Mb/Unlimited	30.77	49.76	32.99*	40.99	16.77	8.77
52Mb/Unlimited	28.58	47.57	39.99*	47.49	7.58	0.08
76Mb/Unlimited	36.26	55.25	49.99*	53.99	5.26	1.26
<b>Sky</b>						
17Mb/Unlimited <sup>181</sup>	13.00	31.99	18.99*	28.99	13.00	3.00
38Mb/Unlimited <sup>182</sup>	20.00	38.99		38.99		0.00
<b>TalkTalk</b>						
17Mb/Unlimited <sup>183</sup>	20.31	39.30	22.95*	22.95*	16.35	16.35
<b>Weighted average</b> <sup>184</sup>	<b>20.16</b>	<b>39.15</b>	<b>24.58</b>	<b>31.14</b>	<b>14.57</b>	<b>8.01</b>

Source: s. 135 response data; dual-play promotional and standard prices from operator websites (accessed 1 February 2017).

Notes: asterisk indicates the promotional price applies to a 12-month period. This table excludes a small number of Phone Co-op standalone fixed broadband customers (<1000).

A8.134 We received data for approximately [§] customers who take standalone fixed broadband from Virgin Media, though some proportion of these customers will not purchase a separate line rental.<sup>185</sup> This means that only a proportion are split-purchase customers, with the remainder taking only a standalone fixed broadband service, with no separate line rental, given Virgin Media's network capabilities. [§]. For this reason, we cannot robustly estimate the average prices paid by split purchasers with a standalone fixed broadband service supplied by Virgin Media.

<sup>180</sup> We use the promotional and standard price of a 17Mb/12Gb service as a proxy for 17Mb/25Gb, since this usage limit is no longer available.

<sup>181</sup> Around 5% of these customers receive Unlimited Broadband Pro, which includes ancillary services.

<sup>182</sup> There is currently no promotional price for this service. The price applies to an 18-month contract.

<sup>183</sup> There is currently no promotional price for this service.

<sup>184</sup> Dual-play prices are weighted by the number of customers with a standalone fixed broadband service of equivalent speed and usage.

<sup>185</sup> This is because Virgin Media has its own network, which allows it to provide broadband services without the need to use Openreach's network.

## Average dual-play prices over time

A8.135 Below we compare the average price of SFV services against dual-play prices, using data from Simplify Digital from Q1 2013 to Q3 2016. We use the price of line rental and calls, which we refer to as SFV services, averaged across BT, Post Office, SSE and Fuel.<sup>186</sup> ADSL dual-play refers to a dual-play bundle with a standard broadband with headline speeds of <30Mbit/s. We use average standard (non-promotional) ADSL dual-play prices and average prices including promotions.<sup>187</sup> These prices include an average call subscription fee. The average prices for ADSL dual-play are based on prices offered by BT, Sky and TalkTalk, the three largest providers in the ADSL market.

A8.136 Figure A8.44 below compares the price of SFV services with ADSL dual-play prices in real (inflation-adjusted) terms, between Q1 2013 and Q3 2016. The price of SFV services increased by 17% (£3.20). Across the same period, the standard (non-promotional) price of ADSL dual-play increased by 15% (£4.92), while the price including promotions decreased by 7% (£2.10).

A8.137 Figure A8.44 also compares the price difference between SFV services and ADSL prices. The average price difference between SFV services and standard ADSL services has increased by 12% (£1.72) between Q1 2013 and Q3 2016. However, the average price difference between SFV services and ADSL prices including promotions has decreased by 53% (£5.30) across the same period.

**Figure A8.44: Prices for SFV services and ADSL dual-play bundles (£/month, September 2016 prices)**

	Q1 2013	Q3 2016	Percentage change	Change
(1) SFV services (line rental + calls)	18.64	21.84	17%	3.20
(2) ADSL dual-play price: standard	33.29	38.21	15%	4.92
(3) ADSL dual-play price: including promotions	28.63	26.53	-7%	-2.10
Difference to line rental + calls				
(2) – (1) ADSL standard prices	14.65	16.37	12%	1.72
(3) – (1) Promotional prices	9.99	4.69	-53%	-5.30

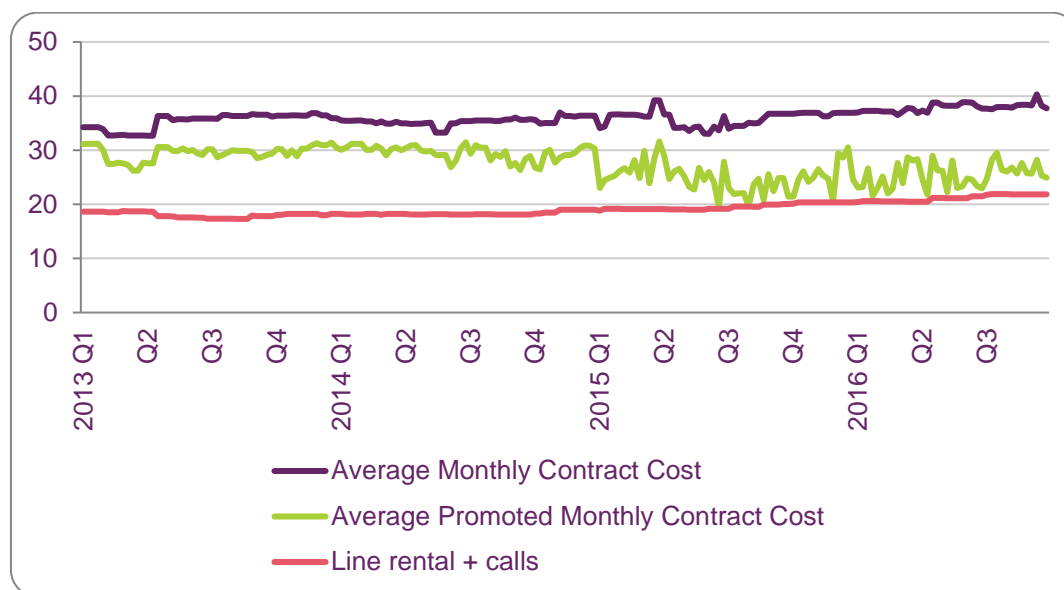
Source: Simplify Digital

Notes: CPI adjusted.

<sup>186</sup> And “other packages”. These are prices advertised to new SFV customers.

<sup>187</sup> This price is averaged across all tariff types, i.e. standard and promotional, not exclusively across promotional tariffs.

**Figure A8.45: Prices for SFV services and ADSL dual-play bundles (£/month, September 2016 prices)**



Source: Simplify Digital

Notes: CPI adjusted.

## SFV consumer characteristics

### Survey evidence introduction

A8.138 This section presents some of the characteristics of SFV customers based on three consumer research studies (the Ofcom Technology Tracker study, 2016 H2;<sup>188</sup> the Ofcom Switching Tracker, July to August;<sup>189</sup> and the 2015 Jigsaw residential survey<sup>190</sup>). We rely primarily on Switching Tracker for survey evidence, however, in some cases we also present figures for equivalent questions from the Jigsaw survey where possible. Where we do not have evidence available from Switching Tracker, we use results from the Jigsaw survey.

A8.139 Figure A8.46 below outlines the groups we have defined for our analysis of consumer survey evidence. In the context of consumers surveys, isolating the split-service customer segment is problematic. The number of customers who reported that they do not bundle landline and broadband was unreligably high, and therefore not comparable with more reliable s.135 data. This may be due to respondents either (a) not realising that the line rental component of a dual-play bundle equates to bundling voice services with fixed broadband or (b) not acknowledging that they bundle landline and fixed broadband when they pay the same supplier for both of

<sup>188</sup> Run by Saville Rossiter-Base on behalf of Ofcom to track the attitudes and behaviour of the general public with respect to the residential telecommunications market as well as broadcasting more generally.

<sup>189</sup> Run by Saville Rossiter-Base on behalf of Ofcom to monitor the general public's switching and engagement behaviour with communications services.

<sup>190</sup> Run by Jigsaw Research on behalf of Ofcom to understand the choices that residential consumers, SME and larger businesses make regarding their use of fixed telecoms services, and to explore how they might react to hypothetical changes in the prices of their services.

these services. For this reason, we have defined the following groups in the context of our analysis of survey evidence.

**Figure A8.46: Groups used for consumer survey evidence**

	Group name	Definition
(1)	Voice only	Landline, no fixed broadband
(2)	Split supplier	Landline and fixed broadband, with different suppliers <sup>191</sup>
(3) = (1) + (2)	SFV	Landline, without fixed broadband bundled <sup>192</sup>
(4)	Dual-play	Landline and fixed broadband with the same supplier <sup>193</sup>

A8.140 There may be some small differences in the voice-only figures reported from the 2015 Jigsaw residential survey throughout this document compared to those reported in the 2016 NMR. This is due to a revised approach to isolating this group of customers; we placed an additional filter on the data which excluded a small number of respondents who provided inconsistent answers about bundling their services.

A8.141 In the following sections we present data on (a) age, socioeconomics, working status and income levels and (b) landline and mobile use, engagement, switching and satisfaction levels.

### **Age, socioeconomics, working status and income levels of SFV customers**

A8.142 This section presents evidence on SFV customer characteristics in terms of age, socioeconomics, working status and income. Where possible, it also provides the breakdown of SFV customers into voice-only and split-supplier customers. The source of this data are S135 responses and the Ofcom Technology Tracker study (2016 H2).

A8.143 The main takeaways from this section are the following:

- S135 responses indicate that 43% of SFV customers are aged 75 years old or over (12% are aged between 75 and 79, 15% are aged between 80 and 84, and 16% are aged 85 or over). This is substantially higher than the equivalent proportion for dual-play customers (4% according to the Ofcom Technology Tracker, 2016 H2) and for the UK population over 15 years old (10% according to the ONS).
- The Ofcom Technology Tracker (2016 H2) study suggests that:

<sup>191</sup> We estimate that split-supplier customers account for around 80% of split purchasers, with the remaining 20% being split-service customers. Split-supplier figures used from the Jigsaw survey only reflect split-supplier customers with a BT voice line (though as explained in paragraph A8.40, we estimate this is the case for almost all split-supplier customers).

<sup>192</sup> This group is comprised of voice-only and split-supplier customers (92% of SFV customers). The remaining 8% are split-service customers.

<sup>193</sup> This group will include an immaterial number of split-service customers, which does not affect our analysis of this group within our analysis of survey evidence.

- 34% of SFV customers are aged 75 years old or over. This is lower than the 43% figure based on S135 responses. We rely on the 43% figure as it is based on actual customer information held by CPs, rather than on survey responses. The Technology Tracker also suggests that voice-only customers tend to be older (47% are aged 75 or over) than split-supplier customers (4% are aged 75 or over, as is the case for dual-play customers).<sup>194</sup>
- 35% of SFV customers live in DE socioeconomic group households, which is substantially higher than the equivalent proportion for dual-play customers (20%). In terms of customer segments, the proportion of voice-only customers who live in DE socioeconomic group households (41%) is materially higher than the equivalent proportion of split-supplier customers (21%). The high proportion of DE is partially explained by the fact that pensioners are automatically classified as living in E socioeconomic group households under the National Readership Survey's classification system.
- 71% of SFV customers indicated they are not working, which is materially higher than the equivalent proportion for dual-play customers (35%). In terms of customer segments, 81% of voice-only customers indicated they are not working which is markedly higher than the equivalent proportion for split-supplier customers (45%).
- 23% of SFV customers said they have an income under £11.5k, which is significantly higher than the equivalent proportion for dual-play customers (10%). In terms of customer segments, the proportion of voice-only customers with an income under £11.5k (28%) is notably higher than the equivalent proportion for split-supplier customers (10%). All of these income figures should be interpreted with caution given the high proportion of non-responses (48% for SFV customers, 49% for voice-only customers, 50% for split-supplier customers, and 37% for dual-play customers).

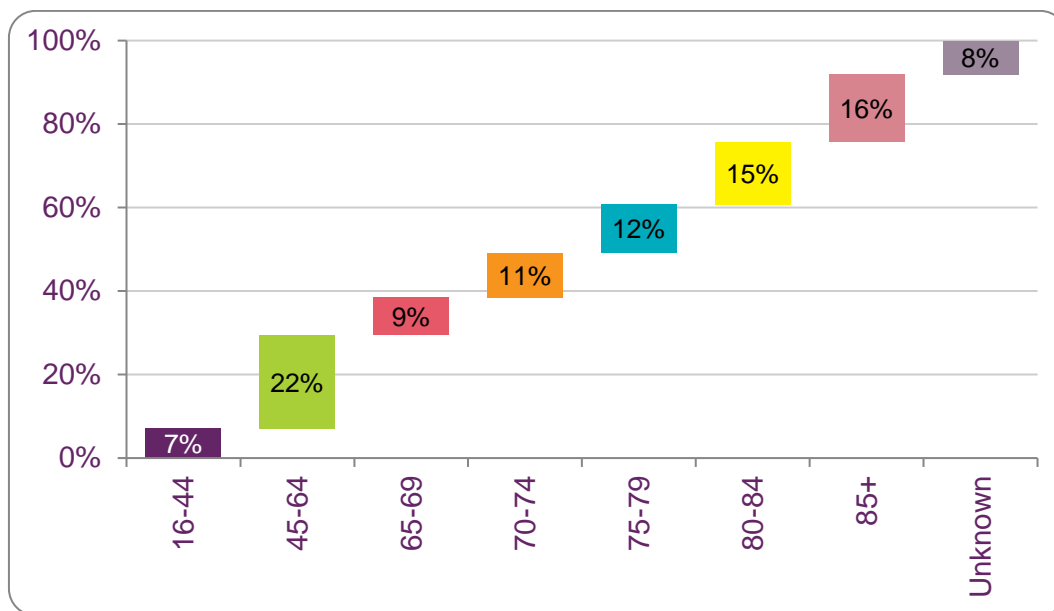
### **Evidence on age and socioeconomics of SFV customers**

A8.144 The two figures below present the distribution by age groups of SFV customers (Figure A8.47) and of the overall UK population over 15 years old (Figure A8.48).

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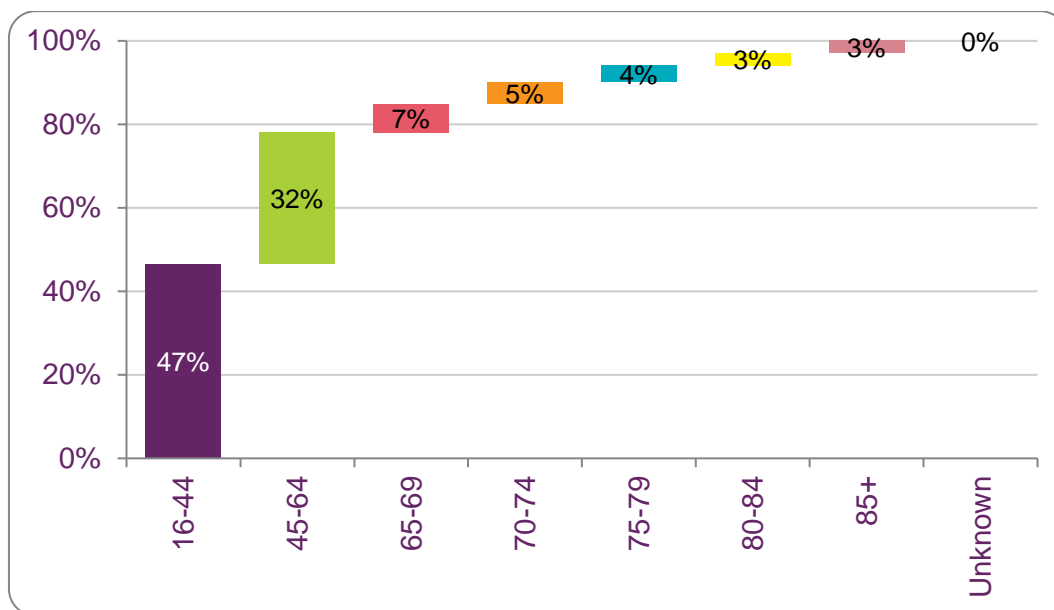
<sup>194</sup> The December 2016 Narrowband Market Review (See Figure 1.3, available here: [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0016/95011/Narrowband-Market-Review.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0016/95011/Narrowband-Market-Review.pdf)), estimated that 38% of voice-only customers were 75 years old or over, which is nine percentage points lower than our current estimate of 47%.

**Figure A8.47: Distribution of SFV customers by age groups**



Source: s.135 responses

**Figure A8.48: Distribution of the UK population over 15 years old by age groups**



Source: ONS

A8.145 At a more granular level, the Technology Tracker study collected age and socioeconomic information about SFV, voice-only, split-supplier, and dual-play customers. Figure A8.49 (below) summarises this information.

**Figure A8.49: Age and socioeconomic information**

	SFV customers	Voice-only customers	Split-supplier customers	Dual-play customers
<b>Unweighted base</b>	<b>535</b>	<b>407</b>	<b>149</b>	<b>2007</b>
<b>% of all fixed line at home</b>	17%	12%	5%	82%
Age				
16-24	9%	3%	25%	14%
25-34	5%	2%	10%	18%
35-54	17%	9%	36%	38%
55-64	13%	12%	15%	15%
65-74	22%	27%	11%	10%
75+	34%	47%	4%	4%
Socio-economic-grade				
AB	19%	13%	32%	31%
C1	21%	18%	29%	29%
C2	25%	28%	18%	21%
DE	35%	41%	21%	20%

Source: Ofcom technology tracker H2 2016.

### Evidence on working status and income levels of SFV customers

A8.146 The Technology Tracker study also collected information about working status and income levels. Figure A8.50 (below) summarises this information.

**Figure A8.50: Working status and income information on SFV customer segments and all residential customers**

	SFV customers	Voice-only customers	Split-supplier customers	Dual-play customers
<b>Unweighted base</b>	<b>535</b>	<b>407</b>	<b>149</b>	<b>2007</b>
<b>% of all fixed line at home</b>	17%	12%	5%	82%
Working status				
<b>Working</b>	29%	18%	55%	65%
<b>Not working</b>	71%	81%	45%	35%
Income				
<b>Under £11.5k</b>	23%	28%	10%	10%
<b>11.5 – 17.49k</b>	12%	15%	4%	9%
<b>17.5 – 29.9k</b>	9%	6%	15%	13%
<b>30k +</b>	9%	2%	21%	31%
<b>Non-response</b>	48%	49%	50%	37%

Source: Ofcom technology tracker H2 2016.

## Landline and mobile use, engagement, switching and satisfaction levels of SFV customers

### Summary of survey evidence

A8.147 The following evidence suggests that, in general, SFV customers have lower levels of engagement (9%) and lower annual switching rates (3%), compared to dual-play customers (20% and 12%, respectively). Further, a higher proportion of SFV customers reported that they have never switched their landline supplier (70%) compared to dual-play customers (45%). The main reason reported by SFV customers for not being interested in changing their landline provider is that they want to stay with a trusted brand (62%\*), compared to (46%) of dual-play customers. Other key reasons were hassle and there being no cost benefit. A higher proportion of SFV customers (69%\*) are very satisfied with the overall service provided by their landline provider, compared to dual-play customers (54%\*).

A8.148 These characteristics are generally more pronounced for voice-only customers. For example, only 58% of voice-only customers have access to a mobile phone, compared to an overall 70% of SFV customers and 96% of dual-play customers. Further, a lower proportion are classified as engaged (6%), a higher proportion reported that they have never switched their landline provider (78%), compared to 15% and 54% of split-supplier customers and 20% and 45% of dual-play customers.

A8.149 However, split-supplier customers have some characteristics which are similar to dual-play customers. For example, 94% of split-supplier customers have access to a mobile phone, compared to 96% of dual-play customers. 15% of split-supplier



customers are classified as engaged, compared to 20% of dual-play customers.<sup>195</sup> 56% of split-supplier customers reported they have never switched compared to 45% of dual-play customers.

### Landline and mobile usage

- A8.150 A considerably lower proportion of SFV customers (70%) have access to a mobile phone, compared to 96% of dual-play customers.<sup>196</sup> This is even lower for voice-only customers compared to dual-play customers; just 58% of voice-only customers have access to a mobile phone.<sup>197</sup> However, a similar proportion (94%) of split-purchase customers have access to a mobile phone.<sup>198</sup>
- A8.151 The Jigsaw survey suggests that SFV customers have a stronger attachment to their landline. 61% of SFV customers slightly or strongly disagreed that they would be willing to give up their landline under certain circumstances, compared to 41% of dual play customers.<sup>199</sup> Across the customer segments, 63% of voice-only customers and 54%\* split-supplier customers, slightly or strongly disagreed that they would be willing to give up their landline.<sup>200</sup>
- A8.152 The Jigsaw survey also suggests that 4% of voice-only customers have access to mobile broadband (despite not having access to fixed broadband, by definition). Approximately 9% of split-supplier customers who have access to mobile broadband (in addition to access to fixed broadband, by definition).

### Engagement levels

- A8.153 The Ofcom Switching Tracker uses an engagement index which measures past and current switching behaviour and interest in the market through survey questions. Those who are “inactive” may have had some past involvement, but have a low interest in the market. Those who are “passive” are more likely to have participated in the past and indicate some interest in the market. Those who are “interested” are similar to those who are passive, but are more likely to keep an eye on the market and look out for better deals. Those who are “engaged” are the most active group in terms of past and current behaviour. The index scores associated with the consumer’s behaviour categorises the consumer.
- A8.154 Figure A8.51 below suggests that SFV customers are less engaged than dual-play customers. Only 9% of SFV customers were classified as engaged compared to 20% of dual-play customers.
- A8.155 Only 6% of voice only customers are classified as engaged, compared to 20% of dual play customers. Split-supplier customers have a higher level of engagement, with 15% classified as engaged, and are relatively similar to dual-play customers (the difference between split-supplier and dual-play is not statistically significant).

<sup>195</sup> Neither of these differences are statistically significant (at the 95% confidence level).

<sup>196</sup> *Ofcom, Technology Tracker, H2 2016.*

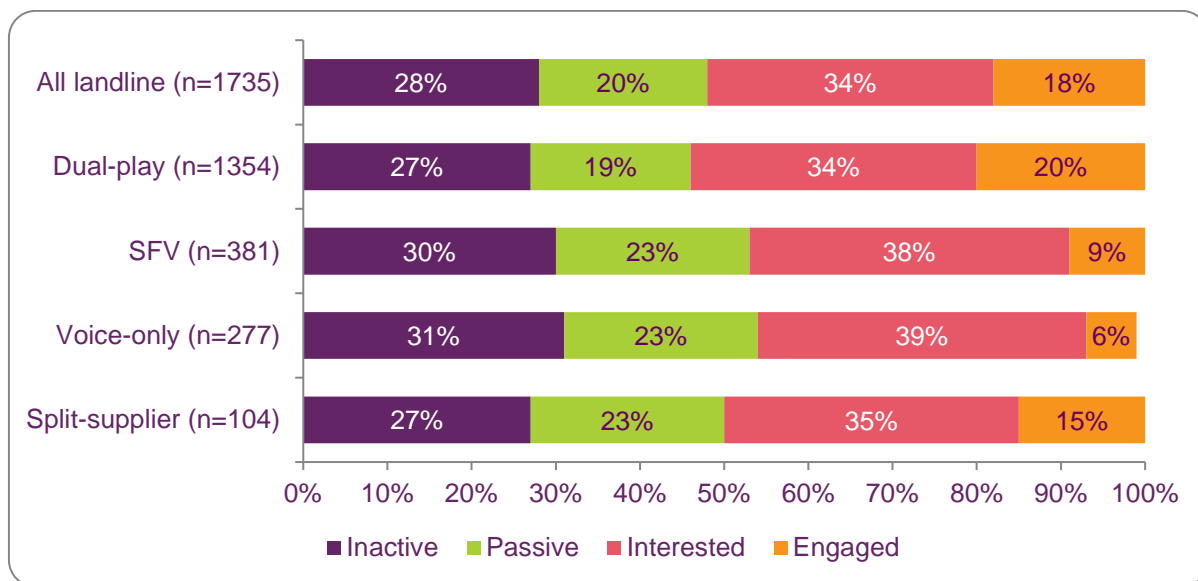
<sup>197</sup> *Ofcom, Technology Tracker, H2 2016.*

<sup>198</sup> *Ofcom, Technology Tracker, H2 2016.* The difference is not statistically significant (at the 95% confidence level).

<sup>199</sup> *2015 Jigsaw residential survey (wave 1).*

<sup>200</sup> *2015 Jigsaw residential survey (wave 1).* The difference is not statistically significant (at the 95% confidence level).

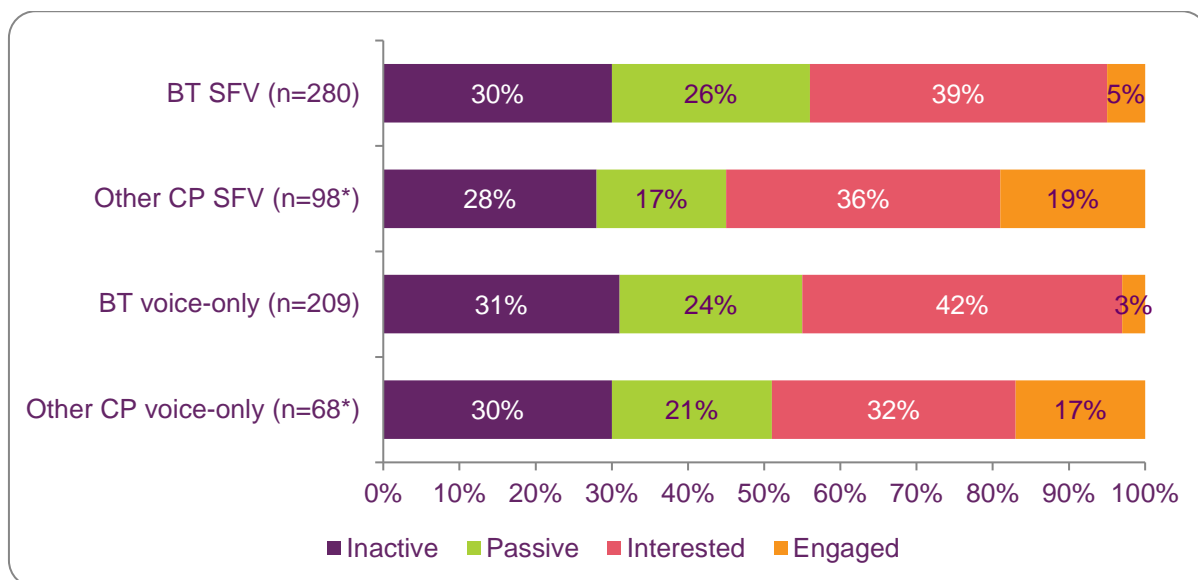
**Figure A8.51: Engagement levels in relation to fixed line services**



Source: Ofcom switching tracker, July – August 2016

A8.156 Figure A8.52 below indicates that BT SFV and BT voice-only customers are less engaged compared to customers of other CPs. Only 5% of BT SFV customers are classified as engaged, compared to 19% of other CP SFV customers. Further, only 3% of voice-only customers are classified as engaged compared to 17% of other CP voice-only customers. We do not have a sufficient base to present figures for split-supplier customers with BT and other CPs.

**Figure A8.52: Engagement levels in relation to fixed line services: BT versus Other CPs**



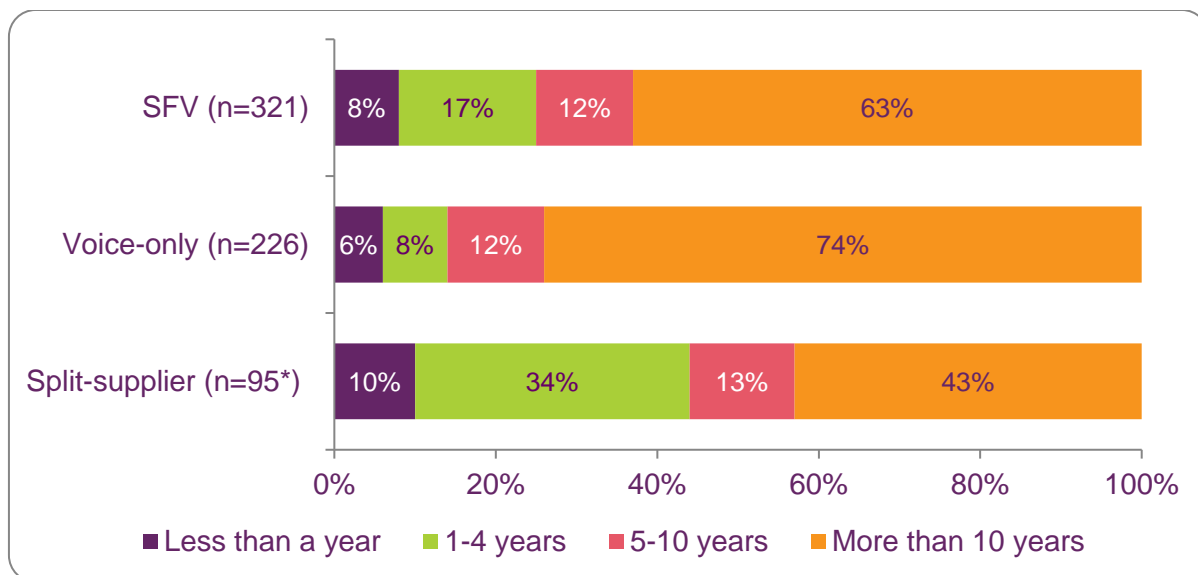
Source: Ofcom switching tracker, July – August 2016

Notes: \*Caution: base under 100.

### Length of time with current provider

A8.157 Figure A8.53 below indicates that a high proportion of SFV customers have been with their current landline provider for more than 10 years. In total, 63% of SFV customers reported that they have been with the same provider for more than 10 years, and 12% have been with their current provider for 5-10 years. 74% voice-only customers and 43%\* of split-service customers reported that they have been with their current landline provider for more than 10 years.

**Figure A8.53: Length of time with current landline provider**

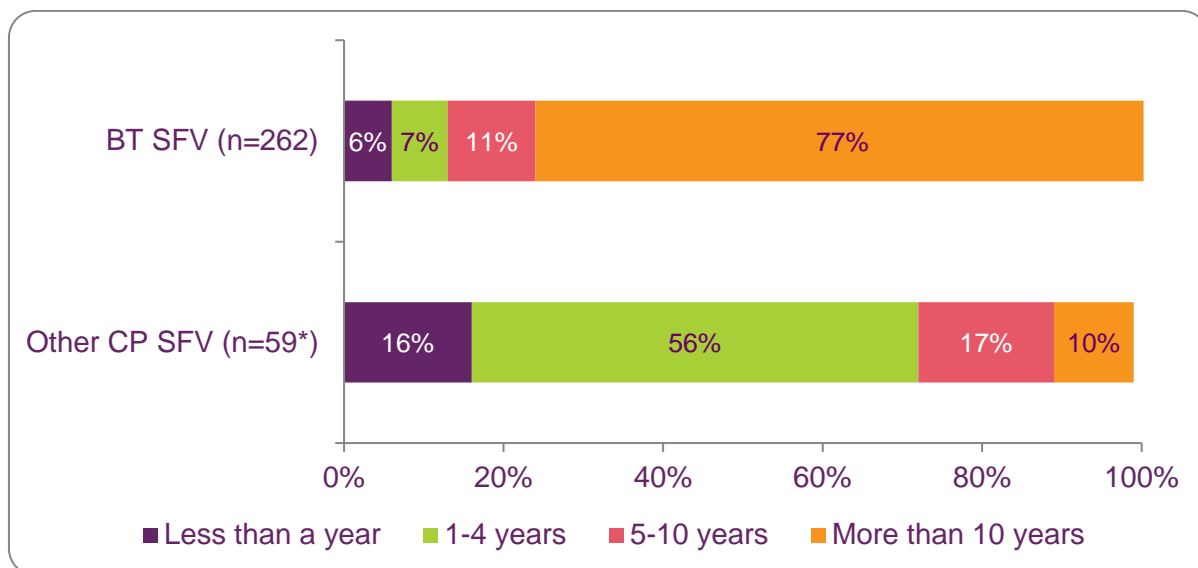


Source: Ofcom switching tracker, July – August 2016

Notes: \*Caution: base under 100

A8.158 Figure A8.54 below shows that a substantially higher proportion of BT SFV customers have been supplied by BT for more than 10 years as compared to SFV customers with other CPs. In total, 77% of BT SFV customers reported they had been supplied by BT for more than 10 years, compared to 10%\* of SFV customers with other CPs who reported they have been supplied by their current provider for more than 10 years. We do not have a sufficient base to present figures for split-supplier and voice-only customers with BT and other CPs.

**Figure A8.54: Length of time with current landline provider: BT versus other CPs**



Source: Ofcom, Switching Tracker, July to August 2016.

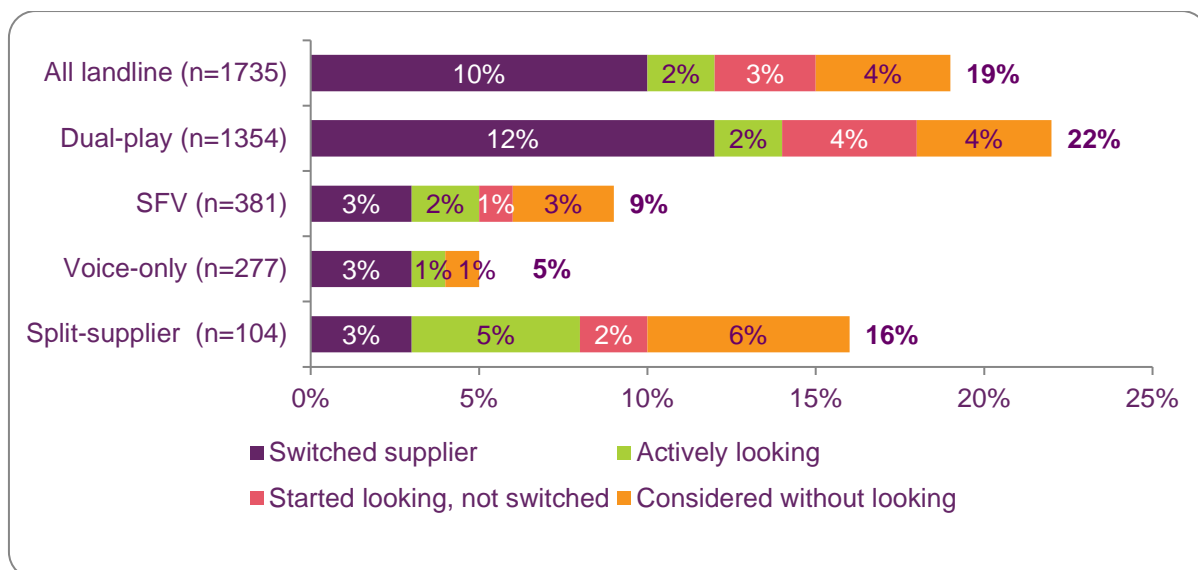
Notes: \*Caution: base under 100

**Switching activity levels**

A8.159 Figure A8.55 below shows that SFV customers reported rates of switching are lower than for dual-play customers. Only 3% of SFV customers reported switching within the last 12 months, compared to 12% of dual-play customers.

A8.160 SFV customers have a relatively low rate of switching; only 3% of SFV customers reported having switched within the past 12 months. Reported switching rates is 3% for both voice-only and split-supplier customers (the difference is not statistically significant).

**Figure A8.55: Switching activity in the past 12 months**



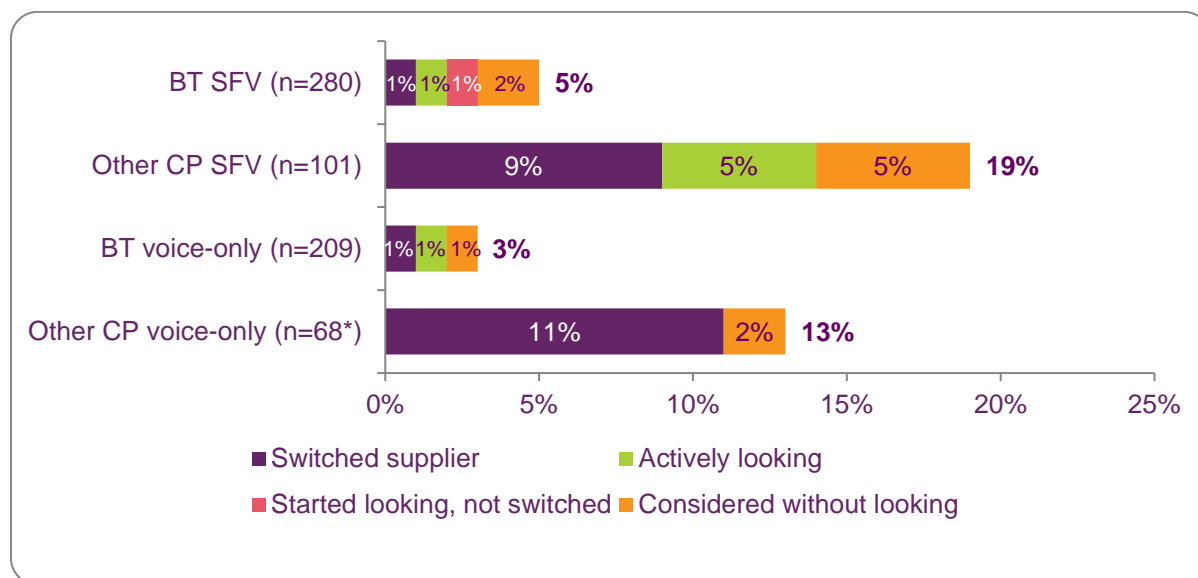
Source: Ofcom, Switching Tracker, July to August 2016.

Notes: \*Caution: base under 100

A8.161 Results from the Jigsaw survey also show low levels of switching among SFV customers. 4% of SFV customers reported having switched in the past 12 months, lower than the reported 10% of dual-play customers.<sup>201</sup> A further breakdown shows that 5% of voice-only customers, and 3%\* of split-supplier customers, reported switching in the past 12 months.<sup>202</sup>

A8.162 Figure A8.56 below indicates that BT SFV and BT voice-only customers have lower reported switching rates compared to other CP's customers. Only 1% of BT SFV customers reported switching within the past 12 months, compared to 9% of SFV customers with other CPs. Further, only 1% of BT voice-only customers reported switching within the past 12 months, compared to 11%\* of voice-only customers with other CPs.

**Figure A8.56: Switching activity in the past 12 months: BT versus other CPs**



Source: Ofcom, *Switching Tracker, July to August 2016*.

Notes: \*Caution: base under 100

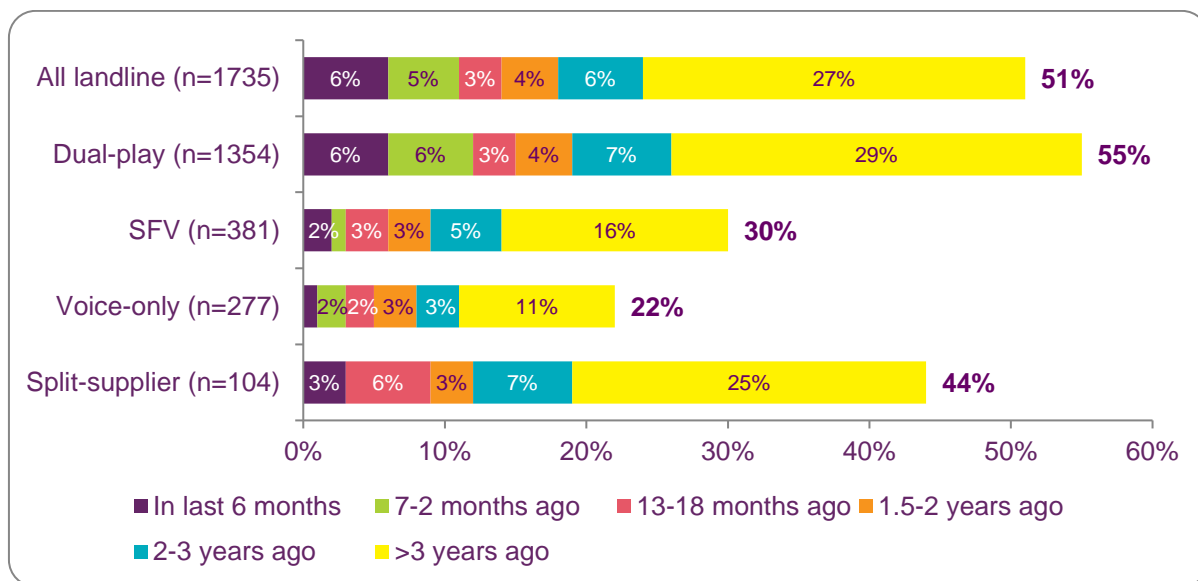
A8.163 Figure A8.57 below shows that 30% of SFV customers reported having ever switched their landline provider, i.e. 70% of SFV customers reported that they have never switched their landline provider. 78% of voice-only customers and 56%\* of split-supplier customers, reported that they have never switched their landline provider.

A8.164 SFV customers are less likely to have ever switched their landline (70%) than dual-play customers, with only 45% of dual-play customers reporting that they have never switched their landline provider.

<sup>201</sup> 2015 Jigsaw residential survey (wave 1).

<sup>202</sup> 2015 Jigsaw residential survey (wave 1).

**Figure A8.57: Whether switched landline provider**

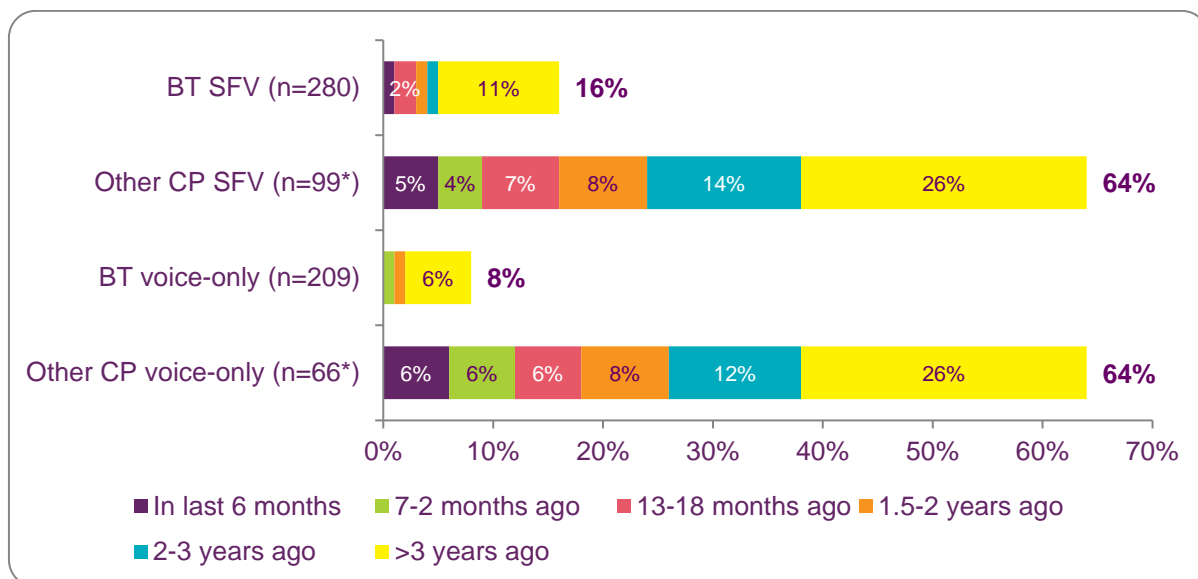


Source: Ofcom, Switching Tracker, July to August 2016.

A8.165 We also have slightly different evidence on the proportions of customers that have never switched supplier from a different source, the Jigsaw survey. Evidence from the Jigsaw survey suggests that 83% of SFV customers have never switched their landline provider, which is considerably higher than dual-play customers (61%). This proportion is the same for both voice-only and split-supplier customers.

A8.166 Figure A8.58 (based on the Switching Tracker) shows that a considerably lower number of BT SFV and voice-only customers reported having ever switched suppliers compared to customers with other CPs. Only 16% of BT SFV customers reported having ever switched their landline provider compared to 64%\* of SFV customers with other CPs. Further, only 8%\* of BT voice-only customers reported having ever switched their landline provider compared to 64%\* of voice-only customers with other CPs. We do not have a sufficient base to present figures for split-supplier customers with BT and other CPs.

**Figure A8.58: Whether switched landline provider: BT versus other CPs**

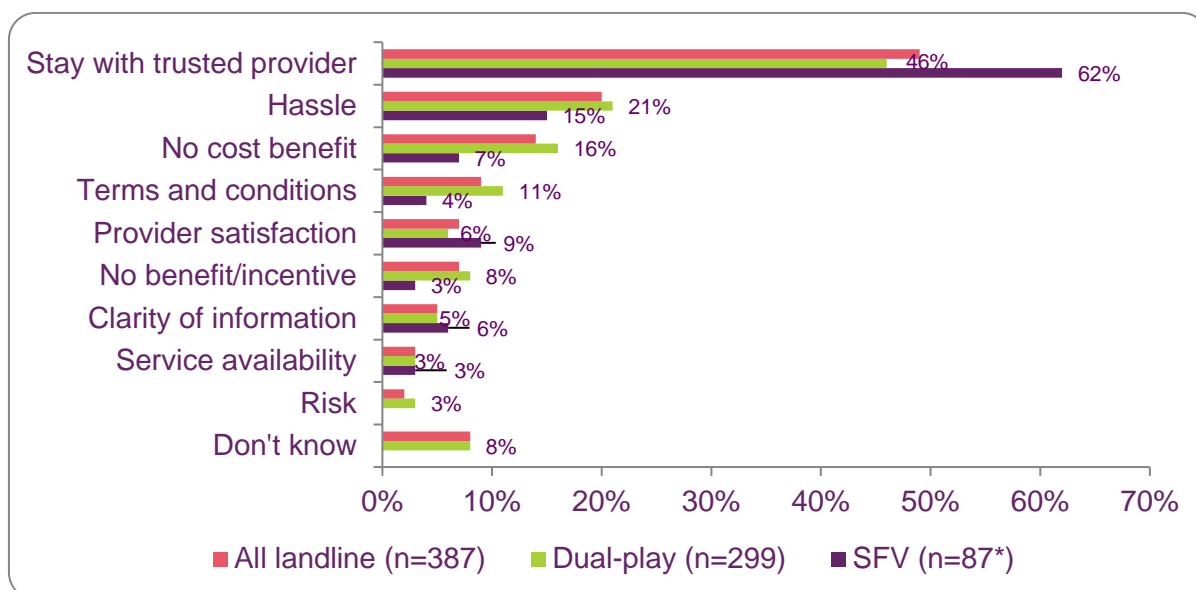


Source: Ofcom, Switching Tracker, July to August 2016.

Notes: \*Caution: base under 100

**Reasons for not being interested in switching**

A8.167 Figure A8.59 describes the reported reasons for being interested in switching their provider. The main reason for not considering changing provider amongst SFV customers is that they prefer to stay with a trusted provider. 62%\* of SFV customers state this as a reason for not being interested in changing providers, compared to 46% of dual-play customers. Other reasons stated by SFV customers were hassle (15%\*), no cost benefit (7%\*) and provider satisfaction (9%\*). The 2015 Jigsaw survey shows 30% of BT voice-only customers cited “Trusted brand” compared to only 6% for non-BT as the reasons for choosing their current supplier. In addition, 42% of BT voice-only customers cited ‘Always been my landline provider’ as the reason compared to 8% for non-BT.

**Figure A8.59: Reasons why not interested in changing provider**

Source: Ofcom, *Switching Tracker, July to August 2016*.

Notes: \*Caution: base under 100. Base too low for split-supplier segment. Voice-only responses are not plotted, since they are equivalent to standalone voice. The voice-only segment is not included, since this is virtually the same as SFV, given the low base of split-supplier customers. The base is of those who have not switched or considered switching; not looking for a new provider; do not agree their landline provider is the best.

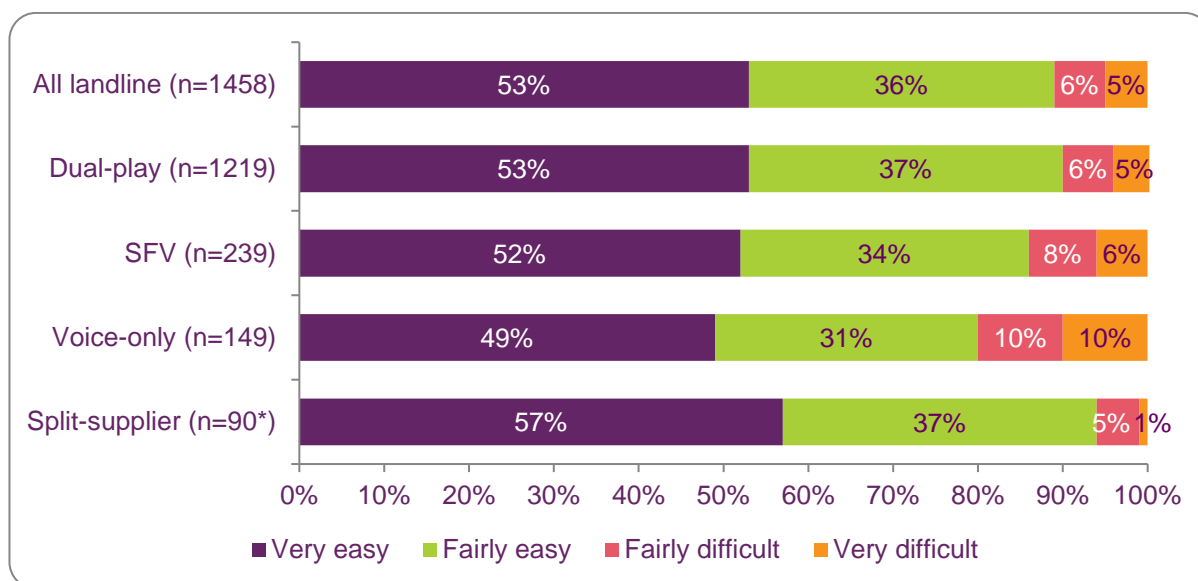
### Perceptions of switching

A8.168 Figure A8.60 below indicates that 14% of SFV customers found or perceived the switching process to be very difficult (6%) or fairly difficult (8%). 20% of voice-only customers found or perceived the switching process to be very difficult (10%) or fairly difficult (10%), compared to 6%\* of split-supplier customers.

A8.169 A similar proportion of SFV customers (14%) found or perceived the switching process to be very difficult or fairly difficult compared to dual-play customers. In total, 11% of dual-play customers found or perceived the switching process to be very difficult (5%) or fairly difficult (6%).<sup>203</sup>

<sup>203</sup> The difference between these two groups is not statistically significant (at the 95% confidence level).



**Figure A8.60: Ease of switching providers**

Source: Ofcom, *Switching Tracker*, July to August 2016.

Notes: \*Caution: base under 100

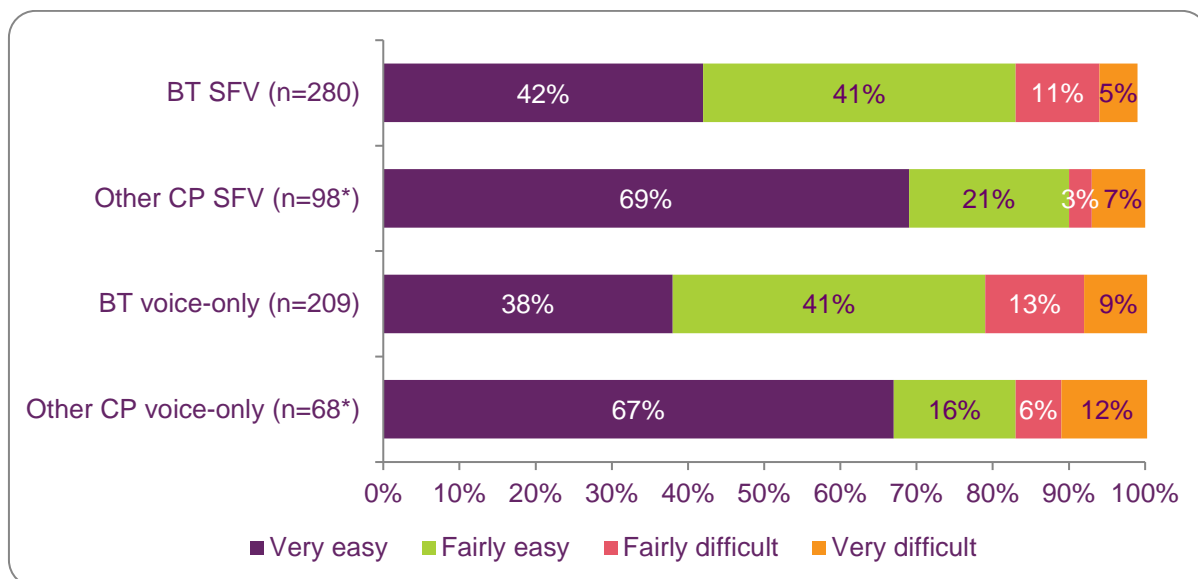
A8.170 Figure A8.61 below indicates that a similar proportion of BT SFV and voice-only customers found or perceived the switching process to be difficult, compared to customers with other CPs. In total, 16% of BT SFV customers found or perceived the switching process to be very difficult or fairly difficult compared to 10%\* of SFV customers with other CPs.<sup>204</sup> We do not have a sufficient base to present figures for split-supplier customers with BT and other CPs.

A8.171 The same comparisons appear also to apply to BT voice-only customers and other CP voice only customers. In total, a similar proportion of BT voice-only customers (22%) found or perceived the switching process to be fairly or very difficult, compared to other CP voice-only customers (18%\*<sup>205</sup>).

<sup>204</sup> This difference is not statistically significant (at the 95% confidence level).

<sup>205</sup> This difference is not statistically significant (at the 95% confidence level).

**Figure A8.61: Ease of switching providers: BT versus other CPs**



Source: Ofcom, Switching Tracker, July to August 2016.

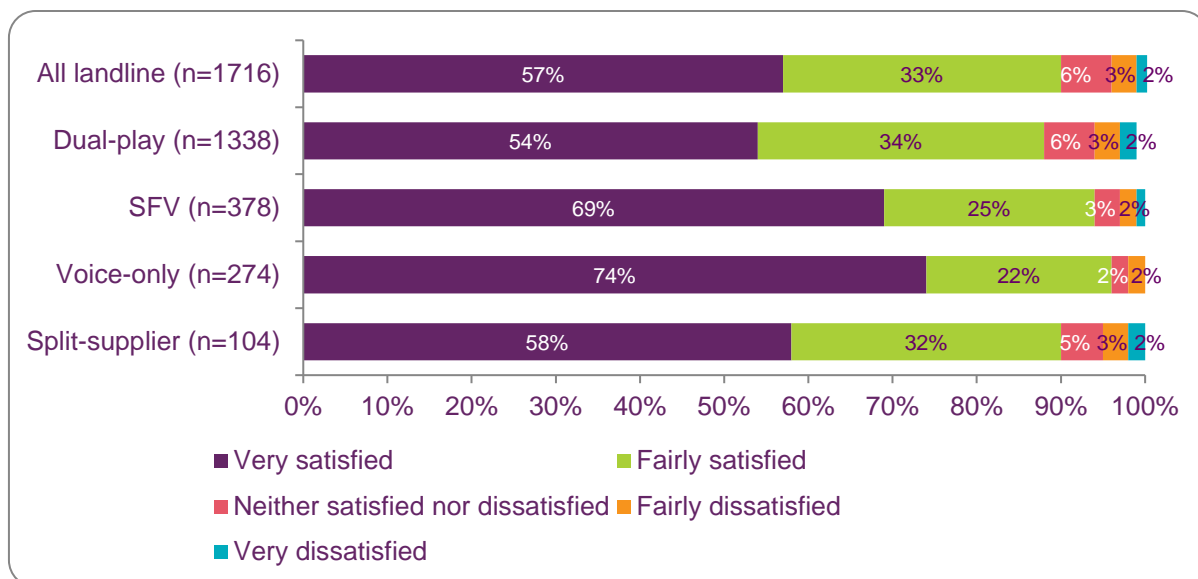
Notes: \*Caution: base under 100

**Satisfaction**

A8.172 Figure A8.62 below shows that 69% of SFV customers are very satisfied with the service provided by their landline provider. 74% of voice-only customers are very satisfied, compared to a lower proportion (58%) of split-supplier customers.

A8.173 A higher proportion of SFV customers (69%) are very satisfied with the overall service provided by their landline provider, compared to 54% of dual-play customers.

**Figure A8.62: Satisfaction with overall service provided by landline provider**

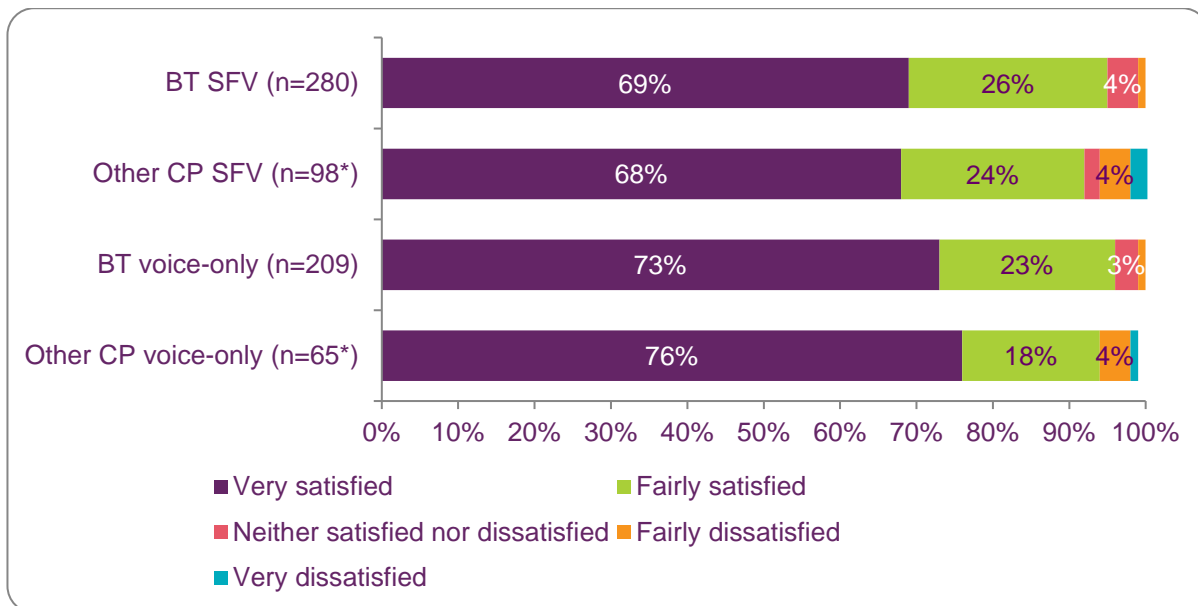


Source: Ofcom, Switching Tracker, July to August 2016.

Notes: \*Caution: base under 100

A8.174 Figure A8.63 indicates that there is no material difference in terms of satisfaction with service between BT and other CP customers within the SFV market. In addition, satisfaction levels are similar within the voice-only segment.<sup>206</sup> We do not have a sufficient base to present figures for split-supplier customers with BT and other CPs.

**Figure A8.63: Satisfaction with overall service provided by landline provider: BT versus other CPs**



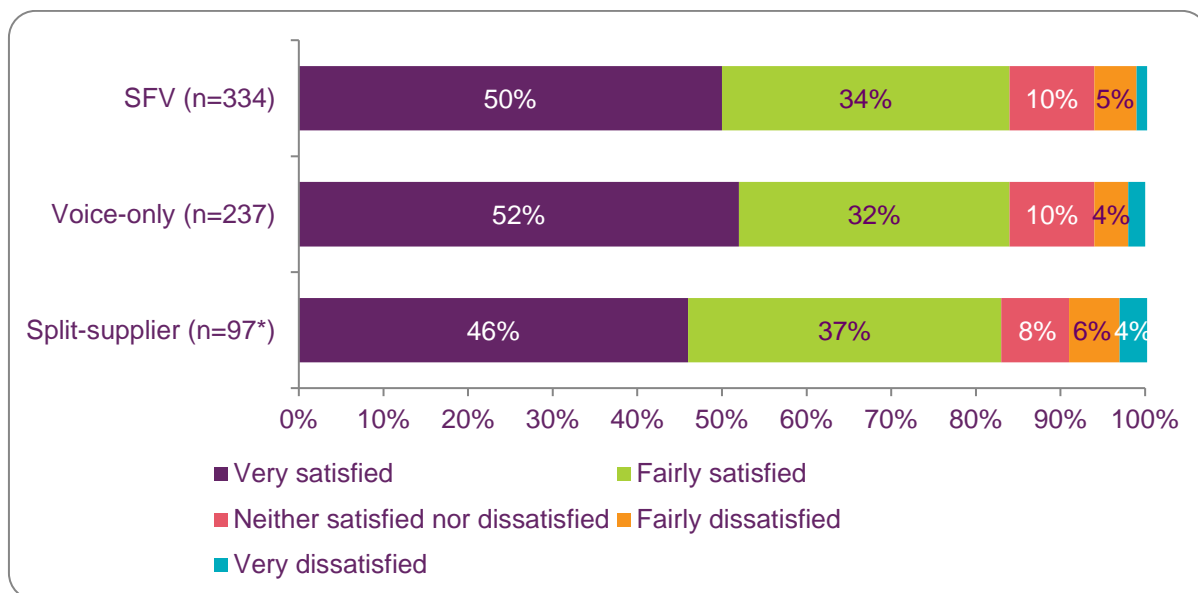
Source: Ofcom switching tracker, July – August 2016

A8.175 Figure A8.64 below shows that 50% of SFV customers reported that they were very satisfied with value for money provided by their landline provider. A further 34% of SFV customers reported they were fairly satisfied with the value for money provided by their landline provider. Voice-only customers are broadly similar to split-supplier customers, with 52% reporting that they were very satisfied compared to 46%\* of split-supplier customers.<sup>207</sup>

<sup>206</sup> Differences are not statistically significant (at 95% confidence level).

<sup>207</sup> This difference is not statistically significant (at the 95% confidence level).

**Figure A8.64: Satisfaction with value for money provided by landline provider**

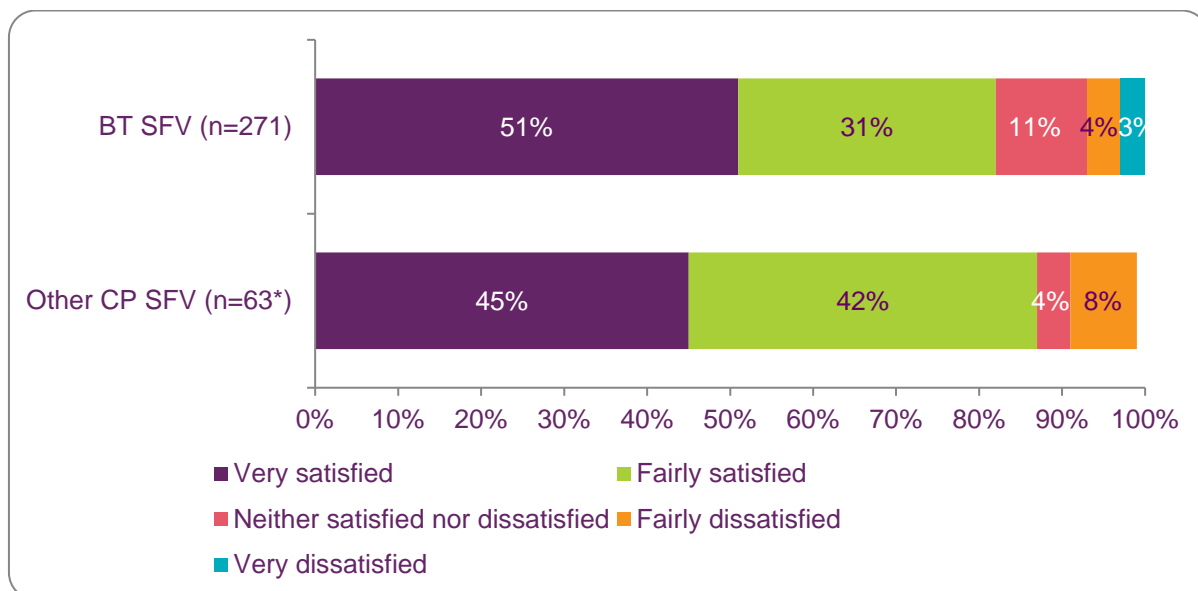


Source: Ofcom, Switching Tracker, July to August 2016.

Notes: \*Caution: base under 100. This question was only asked to SFV customers.

A8.176 Figure A8.65 shows that a similar proportion of BT SFV customers (52%) and SFV customers with other CPs (45%) reported they were very satisfied with the value for money provided by their current provider.<sup>208</sup> We do not have a sufficient base to present figures for split-supplier and voice-only customers with BT and other CPs.

**Figure A8.65: Satisfaction with value for money provided by landline provider: BT versus other CPs**



Source: Ofcom switching tracker, July – August 2016. This question was only asked to SFV customers.

<sup>208</sup> This difference is not statistically significant (at the 95% confidence level).

## Our estimates of consumer detriment experienced by SFV customers

### Current consumer detriment

- A8.177 In Section 6 we set out our estimate of current consumer detriment of £150 million to £340 million per annum. This reflects the difference between what customers currently pay for SFV services, and our view of what they would pay in a competitive market.
- A8.178 At September 2016, there were 2.9 million SFV lines in total in the UK. When calculating consumer detriment, we adjust for the impact of discounted tariffs,<sup>209</sup> consistent with their potential treatment under the price control as set out in Section 8, paragraph 8.63.
- A8.179 We take £5 - £7 per line per month as a lower-bound estimate of this consumer detriment. As set out in Annex 5, this is our estimate of the reduction in BT's line rental at which rivals could compete for new customers. On this basis, our estimate of the detriment from consumers paying higher prices is £60 - £84 per line per annum. However, if our proposed measures to promote competition are effective, part of their effect should be to lower acquisition costs, and in consequence reduce the price at which other CPs can profitably compete against BT, which could in turn lead to prevailing prices of more than £5 to £7 below current levels.
- A8.180 On this first basis, we estimate a lower-bound for current total market detriment of around £150m-£240m per annum. This estimate includes non-BT SFV lines because we consider that, while the competition problems in the market arise from BT's SMP, the detriment is not limited to BT's customers. We estimate a lower-bound detriment of around £110m-£190m for BT SFV lines alone.
- A8.181 We take £8 - 10 per line per month (including VAT) as an upper-bound estimate of consumer detriment. This is our estimate of the reduction in BT's line rental price at which prices would cover BT's costs, plus a normal return. On this second basis, we estimate the detriment from consumers paying higher prices at £96-120 per line per annum. This equates to an upper-bound for current total market detriment of around £260m-£340m per annum (£200m-£260m for BT SFV lines alone). However, we note this is based on prices which might be too low to be sustainable in a competitive market, if such a market involved higher costs than BT currently faces, such as arising from greater consumer switching.

### Forecast consumer detriment

- A8.182 Since customer numbers have been declining, we recognise that the overall detriment is likely to fall year on year. We have forecast detriment over the potential price control period, based on a projection of total market SFV lines (adjusting for the impact of discounted tariffs, which we also forecast).
- A8.183 We assume that the month on month rate of decline in lines remains constant at the average for the last 12 months of data we hold (1.31% per month for October 2015 – September 2016). On this basis, we estimate total consumer detriment for a three-year price control period across the whole market to be around £250m - £525m, in net present value terms.<sup>210</sup> Applying the same approach only to BT's

<sup>209</sup> Such as Home Phone Saver.

<sup>210</sup> Using the HMT Green Book Social Time Preference Rate of 3.5%.

customer base (using the average rate of decline for BT's SFV lines of 1.54% per month) suggests a detriment of £175m-£350m for BT customers.<sup>211</sup>

A8.184 For the first two years of a price-control period, the corresponding estimates are £200m - £425m across the whole market and £150m-£275m for BT customers.

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<sup>211</sup> If we took an alternative approach of extrapolating the historical decelerating trend in the rate of decline in the market, this would imply an annualised rate of decline of 14% for 2016, 11% for 2017, 8% for 2018, 5% for 2019 and 2% for 2020. This would give an NPV for market-wide detriment of £300m-£625m.

## Annex 9

# Draft legal instruments

## Proposals for SMP services conditions

### NOTIFICATION OF PROPOSALS UNDER SECTIONS 48A AND 80A OF THE COMMUNICATIONS ACT 2003

#### Proposals for identifying markets, making market power determinations and setting SMP services conditions in relation to BT under section 45 of the Communications Act 2003

#### Background

1. On 15 September 2009 Ofcom published a statement entitled “*Fixed Narrowband Retail Services Markets - Identification of markets and determination of market power*”. In that statement Ofcom analysed a number of fixed narrowband markets for the UK and Hull and concluded that, with the exception of Hull, the relevant markets did not warrant *ex ante* regulation.<sup>212</sup>
2. On 1 December 2016, Ofcom launched a new review into residential standalone landline telephone services. This Notification sets out Ofcom’s proposals for this review.
3. In parallel to this review, Ofcom launched a public consultation on the regulation of wholesale narrowband services which underpin landline telephone services. Ofcom’s proposals in this respect were set out in a document entitled “*Narrowband Market Review - Consultation on the proposed markets, market power determinations and remedies for wholesale call termination, wholesale call origination and wholesale narrowband access markets.*”

#### Proposals in relation to the United Kingdom excluding the Hull Area

#### Proposals for market identifications and market power determinations

4. Ofcom is proposing to identify the following markets listed in Column 1 of **Table A** below for the purpose of making a determination that the person specified in the corresponding row in Column 2 of that Table has significant market power in that identified services market.

#### **Table A: Market identifications and market power determinations in the United Kingdom excluding the Hull Area**

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<sup>212</sup> In a Statement entitled “*Review of the fixed narrowband services markets, Statement on the proposed markets, market power determinations and remedies*” dated 26 September 2016, Ofcom removed all remaining *ex ante* regulation in the Hull area.

<b>Column 1: Market identification</b>	<b>Column 2: Market power determination</b>
Residential Standalone Fixed Voice access services	BT
Residential Standalone Fixed Voice call services	BT

### **Proposals to set and apply, modify and revoke SMP services conditions**

- Ofcom is proposing to set, in relation to each of the services markets in which Ofcom is proposing to make the market power determinations as listed in **Table A** above, the SMP conditions as set out in the **Schedule** to this Notification, which SMP conditions shall, unless otherwise is stated in that Schedule, take effect from the date of any notification under sections 48(1) and 79(4) of the Act adopting the proposals set out in this Notification.

### **Ofcom's duties and legal tests**

- The effect of, and Ofcom's reasons for making, the proposals for identifying the markets, making the market power determinations and determinations in relation to SMP conditions referred to in this Notification are set out in the consultation document accompanying this Notification.
- In identifying and analysing the markets referred to in this Notification, and in considering whether to make the corresponding proposals set out in this Notification, Ofcom has, in accordance with section 79 of the Act, taken due account of all applicable guidelines and recommendations which have been issued or made by the European Commission in pursuance of an EU instrument, and which relate to market identification and analysis or the determination of what constitutes SMP. In so doing, pursuant to Article 3(3) of Regulation (EC) No 1211/2009, Ofcom has also taken the utmost account of any relevant opinion, recommendation, guidelines, advice or regulatory practice adopted by the Body of European Regulators for Electronic Communications (BEREC).
- Ofcom considers that the proposed SMP conditions comply with the requirements of sections 45 to 47 and 91 of the Act, as appropriate and relevant to each such SMP condition.
- In making all of the proposals referred to in this Notification, Ofcom has considered and acted in accordance with its general duties set out in section 3 of the Act and the six Community requirements in section 4 of the Act. In accordance with section 4A of the Act, Ofcom has also taken due account of all applicable recommendations issued by the European Commission under Article 19(1) of the Framework Directive.

### **Making representations**

- Representations may be made to Ofcom about any of the proposals set out in this Notification and the accompanying consultation document by no later than 9 May 2017.
- Copies of this Notification and the accompanying consultation document will be sent to the Secretary of State in accordance with sections 48C(1) and 81(1) of the Act.



## Interpretation

12. For the purpose of interpreting this Notification (which for the avoidance of doubt includes the Schedules):

- (a) except in so far as the context otherwise requires, words or expressions have the meaning assigned to them in paragraph 13 below, and otherwise any word or expression has the same meaning as it has in the Act;
- (b) headings and titles shall be disregarded;
- (c) expressions cognate with those referred to in this Notification shall be construed accordingly; and
- (d) the Interpretation Act 1978 (c. 30) shall apply as if this Notification were an Act of Parliament.

13. In this Notification:

- (a) “**BT**” means British Telecommunications plc, whose registered company number is 1800000, and any of its subsidiaries or holding companies, or any subsidiary of such holding companies, all as defined by section 1159 of the Companies Act 2006;
- (b) “**Hull Area**” means the area defined as the 'Licensed Area' in the licence granted on 30 November 1987 by the Secretary of State under section 7 of the Telecommunications Act 1984 to Kingston upon Hull City Council and Kingston Communication (Hull) plc, (now known as KCOM);
- (c) “**Ofcom**” means the Office of Communications as established pursuant to section 1(1) of the Office of Communications Act 2002;
- (d) “**United Kingdom**” has the meaning given to it in the Interpretation Act 1978 (1978 c30).

The Schedules to this Notification shall form part of this Notification.

## Signed



Marina Gibbs  
Director Competition Policy Ofcom

**A person duly authorised in accordance with paragraph 18 of the Schedule to the Office of Communications Act 2002**

28 February 2017

## SCHEDULE: Proposed SMP Conditions (BT)

### Part 1: Interpretation

1. In addition to the definitions set out above in this Notification and in each condition below (where relevant), in this Schedule—
  - i. **Broadband Service** means a service that allows for the transfer of high volumes of data at high speeds;
  - ii. **BT Business Service** means all BT products and/or services that are only available to entities with a company registration number;
  - iii. **Customer** means any natural or legal entity who or which is party to a contract with the Dominant Provider for the provision of:
    - (a) one or more Services where such entity does not receive a Broadband Service over the Exchange Line used for the provision of the Service(s); and
    - (b) one or more Services, where such Service/Services is/are provided over the same Exchange Line as a Broadband Service, insofar as such Broadband Service is provided by the Dominant Provider or a third party under separate contractual arrangements.
  - iv. **Dominant Provider** means BT;
  - v. **Exchange Line** means an access connection between a Customer's premises and a local exchange;
  - vi. **Exchange Line Service** means a service consisting in the provision by the Dominant Provider of an Exchange Line to a Customer, to the exclusion of services provided as part of a BT Business Service;
  - vii. **Service** means any of the products and/or services listed in the Annex to this Schedule, or any future services and/or products offered by the Dominant Provider which have the same features to the ones listed in the Annex to this Schedule.

## Part 2: Conditions

### Condition 1 – Communication Requirements

- 1.1** The Dominant Provider must comply with any Communication Requirement which Ofcom may from time to time direct.
- 1.2A** The Dominant Provider must cooperate with Ofcom in the development and evaluation of Communication Requirements and must provide Ofcom with such information as Ofcom may require for the purposes of evaluating the effectiveness of any Communication Requirement.
- 1.2B** In complying with its obligations under Condition 1.2A, the Dominant Provider must comply with any directions made by Ofcom.
- 1.3** For the purposes of Conditions 1.1 and 1.2A, Communication Requirement means any direction issued by Ofcom which requires the Dominant Provider to produce, provide or distribute information, or make specific communications to, its Customers, in a specified manner and form.
- 1.3A** A Communication Requirement may include, but is not limited to, requirements as to:
- (a) the content of the information or communication;
  - (b) the format of the information or communication;
  - (c) the frequency of the provision of information or the making of communications to Customers;
  - (d) the identity of the sender of the information or communication;
  - (e) the Customer group to which the Communication Requirement applies;
  - (f) the geographic area to which the Communication Requirement applies;
  - (g) the sending of details of prices and services offered by the Dominant Provider or other providers of Electronic Communications Services;
  - (h) the provision of response card or tear-off slips to the Customer; and
  - (i) the provision of addressed envelopes to the Customer.

**Condition 2 – Price Control**

**2.1** The Dominant Provider must ensure that in each Relevant Period the Line Rental Charge does not exceed the Line Rental Charge Ceiling for that Period.

**2.2** The Line Rental Charge Ceiling is:

- (a) [£111.99 – £13.99] for the First Relevant Period;
- (b) for each subsequent Relevant Period, an amount calculated by employing the following formula:

$$CC_t = CC_{t-1} * (1 + CPI_t + 0-2.5\%)$$

Where:

$CC_t$  means the Line Rental Charge Ceiling for the Relevant Period;

$CC_{t-1}$  means the Line Rental Charge Ceiling for the Prior Relevant Period;

$CPI_t$  means the change in the Consumer Prices Index in the year of 12 months ending three months immediately before the beginning of the Relevant Period expressed as a percentage, rounded to two decimal places.

**2.3** The Dominant Provider must ensure that in the First Relevant Period the Line Rental Saver Charge does not exceed [£129.49 – £151.09].

**2.4** Where a Customer has paid a Line Rental Saver Charge for a Line Rental Saver Charge Year which has started, but not ended on, [date of publication of final statement], the Dominant Provider must ensure that the Nominal Line Rental Saver Charge does not exceed the Controlling Line Rental Saver Charge for each full calendar month remaining until the completion of that Line Rental Saver Charge Year, where:

**Line Rental Saver Charge Year** means the 12-month period covered by the Line Rental Saver Charge paid by the Customer;

**Nominal Line Rental Saver Charge** means the Line Rental Saver Charge paid by the Customer, divided by 12;

**Controlling Line Rental Saver Charge** means the Line Rental Saver Charge Ceiling divided by the number of the remaining full calendar months until completion of the Line Rental Saver Charge Year;

**Price Control for Services in Basket**

**2.5** The Dominant Provider must take all reasonable steps to secure that, at the end of each Relevant Period, the Percentage Change,  $C_t$  (determined in accordance with paragraph 2.6A) in the aggregate of charges for all of the Services in the Basket is not more than the Controlling Percentage,  $CP_t$  (as determined in accordance with Condition 2.6B).

**2.6A** For the purposes of complying with Condition 2.5, the Percentage Change,  $C_t$ , shall be specified by employing the following formula:

$$C_t = \frac{\sum_{i=1}^n \left[ R_i \frac{(\bar{p}_{i,t} - \bar{p}_{i,t-1})}{\bar{p}_{i,t-1}} \right]}{\sum_{i=1}^n R_i}$$

$C_t$  is the Percentage Change in the aggregate of charges for the Services in the Basket for Relevant Period  $t$ ;

$n$  is the number of individual Services in the Basket;

$i$  is a number from 1 to  $n$  for each of the  $n$  individual Services in the Basket;

$R_i$  is the Total Revenue accrued during the Prior Period in respect of the individual Service  $i$  that forms part of the Basket;

$t$  refers to the Relevant Period;

$t-1$  refers to the Prior Period;

$\bar{p}_{i,t}$  is the Relevant Period Weighted Average Charge made by the Dominant Provider for the individual Service  $i$  that forms part of the Basket during the Relevant Period, excluding any discounts offered by the Dominant Provider:

Where such Relevant Period Weighted Average Charge shall be calculated by employing the following formula:

$$\bar{p}_{i,t} = \sum_{j=1}^m (w_{i,j,t} p_{i,j,t})$$

Where:

$m$  is the number of time periods for which there are distinct charges during the Relevant Period;

$j$  is a number from 1 to  $m$  for each of the  $m$  time periods during which a distinct charge is in effect;

$w_{i,j,t}$  is the proportion of the Relevant Period in which each charge,  $p_{i,j,t}$  is in effect, calculated by the number of days during which the charge is in effect and dividing by the number of days in each Relevant Period.

$p_{i,j,t}$  is the charge for the specified period,  $j$ , during the Relevant Period  $t$  for the individual Service,  $i$ ;

$\bar{p}_{i,t-1}$  is, for the purposes of calculating the Percentage Change for the First Relevant Period, the Initial Charge for the individual Service  $i$  that forms part of the Basket during the Prior Period, excluding any discounts offered by the Dominant Provider. For the purposes of calculating the Percentage Change for the Second Relevant Period and the Third Relevant Period,  $\bar{p}_{i,t-1}$  is the Prior Period Weighted Average Charge made by the Dominant Provider for the individual Service  $i$  that forms part of the Basket during the Prior Period, excluding any discounts offered by the Dominant Provider;

Where such Prior Period Weighted Average Charge shall be calculated by employing the following formula:

$$\bar{p}_{i,t-1} = \sum_{j=1}^m (w_{i,j,t-1} p_{i,j,t-1})$$

Where:

$m$  is the number of time periods for which there are distinct charges during the Prior Relevant Period;

$j$  is a number from 1 to  $m$  for each of the  $m$  time periods during which a distinct charge is in effect;

$w_{i,j,t-1}$  is the proportion of the Prior Period in which each charge,  $p_{i,j,t-1}$ , is in effect, calculated by the number of days during which the charge is in effect and dividing by the number of days in the Relevant Period;

$p_{i,j,t-1}$  is the charge for the individual period,  $j$ , during the Prior Year,  $t-1$ , for the individual Service,  $i$ .

**2.6B** For the purposes of complying with Condition 2.6, the Controlling Percentage,  $CP_t$ , shall be calculated by employing the following formula:

$$CP_t = CPI_t + 0$$

Where:

$CP_t$  is the Percentage Change in charges for the specific Service in the single charge category in question for the Relevant Period  $t$ ;

$CPI_t$  means the change in the Consumer Prices Index in the year of 12 months ending three months immediately before the beginning of the Relevant Period expressed as a percentage, rounded to two decimal places.

### Provision of information to Ofcom

- 2.7** The Dominant Provider must record, maintain and supply to Ofcom in an electronic format, no later than 3 months after the end of each Relevant Period, the data necessary for Ofcom to monitor compliance of the Dominant Provider with this Condition 2. The data must include, as relevant:
- (a) all charges published by the Dominant Provider from time to time during the Relevant Period as well as the Prior Period, including the dates and time period during which they were in force;
  - (b) the calculated Percentage Changes, pursuant to Condition 2.6A for all Services in the Basket;
  - (c) all relevant data the Dominant Provider used in the calculation of the Percentage Changes for the purpose of Condition 2.6A, including data for each Service in the Basket;

- (d) the Relevant Period Weighted Average Charges and the Prior Period Weighted Average Charges pursuant to Condition 2.6A and calculations thereof, including the relevant data for each Service within the Basket;
- (e) other data necessary for monitoring compliance with this Condition 2; and
- (f) without prejudice to Ofcom’s statutory information gathering powers, such data as Ofcom may from time to time reasonably require.

All relevant revenues in respect of each of the Services are to be provided to at least the nearest £1,000.

**2.7A** The Dominant Provider shall publish such information provided to Ofcom pursuant to Condition 2.7 as Ofcom may from time to time direct.

## Definitions

**2.8** In this Condition 2:

- i. **Basket** means:
  - (a) in relation to the First Relevant Period together all Services listed in Part 1 of the Annex to this Schedule;
  - (b) in relation to the Second Relevant Period and the Third Relevant Period together all Services listed in Part 1 and Part 2 of the Annex to this Schedule;
- ii. **Consumer Prices Index** means the index of consumer prices compiled, from time to time, by an agency or a public body on behalf of Her Majesty’s Government or a governmental department (which is the Office of National Statistics at the time of publication of this notification), in respect of all items;
- iii. **Controlling Percentage** is to be determined in accordance with Condition 2.6B;
- iv. **Home Phone Saver 2019 Charge** means the amount charged by the Dominant Provider for the service marketed as “Home Phone Saver 2019”;
- v. **Initial Charge** means the charge for a Service which is listed in the BT Consumer Price Guide, effective from 2 April 2017;
- vi. **Line Rental Charge** means any amount charged by the Dominant Provider to a Customer on a monthly basis for Exchange Line Services<sup>213</sup>, excluding:
  - (a) any incremental charge made for the provision of Voice-call Services by the Dominant Provider;
  - (b) any Exchange Line installation charges;
  - (c) the Home Saver 2019 Charge and any element thereof; and

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<sup>213</sup> Currently listed as Standard Line Rental or Line Rental in the BT Consumer Price Guide, effective from 10 February 2017.

- (d) the Line Rental Plus Charge and any element thereof;
- vii. **Line Rental Plus Charge** means the amount charged by the Dominant Provider for the service marketed as “Line Rental Plus Charge”;
- viii. **Line Rental Saver Charge** means any amount charged by the Dominant Provider to a Customer for the provision of Exchange Line Services over the period of 12 months (defined in Condition 2.4 as the "**Line Rental Saver Charge Year**"), where such amount is subject to a discount related to the making of an upfront payment for that entire period;
- ix. **Percentage Change** is to be determined in accordance with Condition 2.6A;
- x. **Prior Period** means each of the following three periods:
- (1) In relation to the First Relevant Period, the period beginning on [*12 months before the publication of the statement*] and ending on [*one day before the beginning of the First Relevant Period*];
  - (2) In relation to the Second Relevant Period, the First Relevant Period;
  - (3) In relation to the Third Relevant Period, the Second Relevant Period.
- xi. **Prior Period Weighted Average Charge** is to be determined in accordance with the relevant formula in Condition 2.6A;
- xii. **Relevant Period** means each of the following three periods:
- (1) The [*X*]-month period beginning on [a minimum of 30 days after the publication of the statement] and ending on [*date*] (the “First Relevant Period”);
  - (2) The twelve-month period beginning on [*date*] and ending on [*date*] (the “Second Relevant Period”);
  - (3) The twelve-month period beginning on [*date*] and ending on [*3 years after publication of the final statement*] (the “Third Relevant Period”).
- xiii. **Relevant Period Weighted Average Charge** is to be determined in accordance with the relevant formula in Condition 2.6A;
- xiv. **Voice-call Service** means a service that allows a Customer to make voice calls using an Exchange Line.



## **ANNEX<sup>214</sup>**

### **Part 1**

Unlimited Evening & Weekend Calls (not including Line Rental)

Unlimited Weekend Calls (not including Line Rental)

Unlimited Anytime Calls (not including Line Rental)

Calls to BT Mobile Consumer numbers

Calls to all other UK Mobile numbers

Calls to UK National and Local numbers

Calls to 0845 & 0870 Numbers

Calls to Service Numbers 090, 118 and other 084 & 087

Calls to International numbers

Friends & Family International

International Freedom

Calls to 070/076/055/056 number ranges

Choose to Refuse

Anonymous Call Reject

BT Privacy at Home

BT Privacy with Caller Display

Call Barring

Call Diversion

Call Waiting

### **Part 2**

Standard Line Rental or Line Rental

BT Smart Talk

BT Call Protect

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<sup>214</sup> All listed products/services are as per BT Consumer Price Guide, effective from 10 February 2017.

Permanent Withhold Number

Bar Three Way Calling

Block Ring Back

1471

1470

## Annex 10

## Glossary

2006 Retail Price Control Statement	Ofcom, <i>Retail Price Controls</i> , July 2006. <a href="https://www.ofcom.org.uk/_data/assets/pdf_file/0012/42114/rpcstatement.pdf">https://www.ofcom.org.uk/_data/assets/pdf_file/0012/42114/rpcstatement.pdf</a>
2007 EC Recommendation	European Commission Recommendation (2007/879/EC) of 17 December 2007 on relevant product and service markets within the electronic communications sector susceptible to ex ante regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services. Published in the Official Journal of the European Union, 28.12.2007, L 344, pages 65-69 at <a href="http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32007H0879">http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32007H0879</a>
2009 Retail Narrowband Statement	Ofcom, <i>Fixed Narrowband Retail Services Markets - Identification of markets and determination of market power</i> , September 2009. <a href="http://webarchive.nationalarchives.gov.uk/20160702162827/http://stakeholders.ofcom.org.uk/consultations/retail_markets/?a=0">http://webarchive.nationalarchives.gov.uk/20160702162827/http://stakeholders.ofcom.org.uk/consultations/retail_markets/?a=0</a>
2013 Narrowband Market Review Statement	Ofcom, <i>Review of the fixed narrowband services markets</i> , September 2013. <a href="https://www.ofcom.org.uk/_data/assets/pdf_file/0014/50720/final_statement.pdf">https://www.ofcom.org.uk/_data/assets/pdf_file/0014/50720/final_statement.pdf</a>
2014 EC Recommendation	European Commission Recommendation (2014/7174/EC) of 9 October 2014 on relevant product and service markets within the electronic communications sector susceptible to ex ante regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communications networks and services. <a href="http://eur-lex.europa.eu/JOHtml.do?uri=OJ:L:2014:295:SOM:EN:HTML">http://eur-lex.europa.eu/JOHtml.do?uri=OJ:L:2014:295:SOM:EN:HTML</a>
2014 FAMR Statement	Ofcom, <i>Fixed access market review: wholesale local access, wholesale fixed analogue exchange lines, ISDN1 and ISDN30</i> , June 2014. <a href="https://www.ofcom.org.uk/_data/assets/pdf_file/0032/78836/volume2.pdf">https://www.ofcom.org.uk/_data/assets/pdf_file/0032/78836/volume2.pdf</a>
2016 NMR Consultation	Ofcom, <i>Narrowband market review – Consultation</i> , December 2016. <a href="https://www.ofcom.org.uk/_data/assets/pdf_file/0016/95011/Narrowband-Market-Review.pdf">https://www.ofcom.org.uk/_data/assets/pdf_file/0016/95011/Narrowband-Market-Review.pdf</a>
The Act	Communications Act 2003
ASA	Advertising Standards Authority
BEREC	Body of European Regulators for Electronic Communications, a body of the European Union.
BT	British Telecommunications plc.
BT Basic	BT Basic is a social telephony scheme sold by BT for customers who are recipients of specific means-tested Government benefits. See <a href="http://btplc.com/inclusion/ProductsAndServices/BTBasic/index.htm">http://btplc.com/inclusion/ProductsAndServices/BTBasic/index.htm</a>
BT retail divisions	Those BT business units that directly serve residential and/or business customers.
Bundle	A bundle refers to the purchase of landline services in addition to other services such as broadband, pay-TV, etc.
Call plan	An add-on to a line rental services which allow customers to make calls to a specified set of number types (UK geographic numbers, or UK mobile etc.) within a given period (weekend, evening, anytime etc.) for a fixed price. They may or may not come with time limitations or fair use policies.
Care Level 1/Care Level 2	Service maintenance levels provided by BT. Care Level 1 provides a target fix time by 23.59 day after next, Monday to Friday, excluding Public and Bank Holidays. For example, report Tuesday, clear Thursday. Care Level 2 provides a target fix time by 23.59 next day, Monday to Saturday, excluding Public and Bank Holidays. For example, report Tuesday, clear Wednesday.
CP (or Communications Provider)	A person who provides an electronic communications network or an electronic communications service.
Consumer Price Index (CPI)	The official measure of inflation of consumer prices in the UK.

Countervailing buyer power	The balancing of the market power of one party or group selling a service by that of another party or group that purchases the service.
Cost-based charge control	A charge control based on a model of the input cost of providing a service including a regulated return.
DCR	Digital Communications Review 2016. See <a href="https://www.ofcom.org.uk/_data/assets/pdf_file/0016/50416/dcr-statement.pdf">https://www.ofcom.org.uk/_data/assets/pdf_file/0016/50416/dcr-statement.pdf</a>
Dual-play	Where CP offers two services as part of a package of services, for example fixed voice and fixed broadband services.
EBIT	Earnings before interest and tax.
EC	European Commission.
EE	Everything Everywhere Limited, now part of BT plc.
EIA	Equality impact assessment.
Home Phone Saver	Home Phone Saver is a BT telephone only line rental package which provides a number of additional services. The service cannot be taken with another service such as broadband. <a href="http://bt.custhelp.com/app/answers/detail/a_id/49402/~home-phone-saver-2017">http://bt.custhelp.com/app/answers/detail/a_id/49402/~home-phone-saver-2017</a>
Hull Area	The area defined as the 'Licensed Area' in the licence granted on 30 November 1987 by the Secretary of State under Section 7 of the Telecommunications Act 1984 to Kingston upon Hull City Council and Kingston Communications (Hull) plc (KCOM).
Inclusive call allowance	The allowance of calls that apply free of charge within a Call plan.
Local Loop Unbundling (LLU)	A process by which a dominant provider's local loops are physically disconnected from its network and connected to a competing provider's networks, enabling other providers to use the local loop to provide services.
Metallic Path Facility (MPF)	The provision of access to the copper wires from the customer premises to a BT MDF that covers the full available frequency range, including both narrowband and broadband channels, allowing a competing provider to provide the customer with both voice and/or data services using the dominant provider's local loop.
NMR	Narrowband Market Review.
National Regulatory Authority (NRA)	The relevant communications regulatory body for each country in the EU. Ofcom is the NRA for the United Kingdom.
Ofcom	The Office of Communications.
Out-of-plan call	A call which is not included free of charge as part of a Call plan.
Plusnet	Plusnet plc.
Post Office	Post Office Limited.
Price freeze	A situation where the prevailing market price or any other price is then held constant, either in nominal or real terms.
RAB	Regulatory Asset Base.
ROCE	Return on Capital Employed.
ROS	Return on Sales.
S135	Section 135 of the Communications Act.
Shared Metallic Path Facility (SMPF)	The provision of access to the copper wires from the customer's premises to a BT MDF that allows a competing provider to provide the customer with broadband services, while BT continues to provide the customer with conventional narrowband communications.
Significant Market Power (SMP)	A test set out in European Directives used by NRAs, such as Ofcom, to identify those CPs which must meet additional obligations under the relevant Directives.
Sky	British Sky Broadcasting Ltd.
SMP Guidelines	EC guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications networks and services (2002/C165/03).
Split purchaser	A customer that buys both a standalone fixed voice service and a standalone fixed broadband service, either from the same supplier or different suppliers, i.e. all split-service and split-supplier customers.
Split-service customer	A customer that buys both a standalone fixed voice service and a standalone fixed broadband service from the same supplier, but each service is bought separately (not in a bundle).

Split-supplier customer	A customer that buys both a standalone fixed voice service and a standalone fixed broadband service from two different suppliers.
SSE	SSE Energy Supply Limited.
SSNIP	Small but Significant Non-Transitory Increase in Price.
Standalone fixed broadband service	Fixed broadband services that are not sold as part of a bundle with any other services.
Standalone fixed voice (SFV) call	Voice call made by a customer using a standalone fixed voice service.
Standalone fixed voice (SFV) customers	Customers that buy a fixed voice service from a CP but do not also buy a fixed broadband service from the same CP as part of a bundle.
Standalone Fixed Voice (SFV) services	Landline services that are not sold as part of a bundle with non-voice service. This includes access (i.e. line rental) and calls.
TalkTalk	TalkTalk Telecoms Group plc.
The Phone Co-op	The Phone Co-op Limited.
UK	United Kingdom – when referring to the United Kingdom this excludes Hull except when referring to United Kingdom wide data.
UK Regulators Network (UKRN)	A member organisation formed of 13 of the UK's sectoral regulators: The Civil Aviation Authority (CAA), The Financial Conduct Authority (FCA), the Payment Systems Regulator (PSR), Office of Communications (Ofcom), Office of Gas and Electricity Markets (Ofgem), Water Services Regulation Authority (Ofwat), Office of Rail and Road (ORR), Northern Ireland Authority for Utility Regulation (Utility Regulator), Single Source Regulations Office (SSRO), Financial Reporting Council (FRC), NHS Improvements, Water Industry Commission for Scotland (WICS) and Legal Services Board (LSB).
Universal Service Directive	Directive 2002/22/EC of the European Parliament and of the Council of 7 March 2002 on a common regulatory framework for electronic communications networks and services (Framework Directive) as amended by Directive 2009/136/EC 21140 and Regulation 544/2009.
Virgin Media Limited	Virgin Media plc.
Voice-only customer	A customer that buys a standalone fixed voice service, but do not also buy a fixed broadband service from any CP.
Voice Over Internet Protocol (VoIP)	The traffic method of carrying voice calls on fixed and mobile networks by packetizing speech and carrying it using IP
WCO	Wholesale fixed geographic call origination services
WCT	Wholesale fixed geographic call termination services
Wholesale Fixed Analogue Exchange Lines (WFAEL)	A narrowband analogue access connection between a customer's premises and a local exchange.
Wholesale Line Rental (WLR)	The service offered by BT to other United Kingdom communications providers to enable them to offer retail line rental services in competition with BT's own retail services. Line rental is offered along with calls (and other service elements, such as broadband) to retail customers.
Wholesale Local Access (WLA)	Wholesale local access – covers fixed telecommunications infrastructure, specifically the physical connection between end users' premises and a local exchange.
White label access product	A wholesale product bought from another CP (who is buying WLR from Openreach) and rebranded.

## Formal S.135 Requests

Communications Provider	A10.1 Formal Information Request	A10.2 Summary of information requested
BT	Section 135 notice dated 3 November 2016	Request market research reports and specific data relating to SFV customers, services and lines from Nov 2014 to September 2016, together with information on profitability.
BT	Section 135 notice dated 9 November 2016	For Residential Analogue Voice-only Retail Lines the number of customers supplied, lines to customers and volume of calls on those lines. The number of customer acquisition and losses over a period together with information about revenues and costs.
BT	Section 135 notice dated 4 January 2017	Clarification of information provided in subsequent information requests relating to estimates on size of relevant customer base and customer numbers on specific BT products.
The Phone Co-op	Section 135 notice dated 18 November 2016	Request market research reports and specific data relating to SFV customers, services and lines from Nov 2014 to September 2016, together with information on profitability.
The Phone Co-op	Section 135 notice dated 29 November 2016	For Residential Analogue Voice-only Retail Lines the number of customers supplied, lines to customers and volume of calls on those lines. The number of customer acquisition and losses over a period.
Post Office	Section 135 notice dated 15 November 2016	Request market research reports and specific data relating to SFV customers, services and lines from Nov 2014 to September 2016, together with information on profitability.
Post Office	Section 135 notice dated 29 November 2016	For Residential Analogue Voice-only Retail Lines the number of customers supplied, lines to customers and volume of calls on those lines. The number of customer acquisition and losses over a period.
Sky	Section 135 notice dated 21 November 2016	Request market research reports and specific data relating to SFV customers, services and lines from Nov 2014 to September 2016, together with information on profitability.
SSE	Section 135 notice dated 12 December 2016	Request market research reports and specific data relating to SFV customers, services and lines from Nov 2014 to September 2016, together with information on profitability.
TalkTalk	Section 135 notice dated 22 November 2016	Request market research reports and specific data relating to SFV customers, services and lines from Nov 2014 to September 2016, together with information on profitability.

Virgin Media Ltd	Section 135 notice dated 25 November 2016	Request market research reports and specific data relating to SFV customers, services and lines from Nov 2014 to September 2016, together with information on profitability.
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**ANNEX 7**

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Case Number: [ ]

**IN THE COMPETITION APPEAL TRIBUNAL  
BETWEEN**

**JUSTIN LE PATOUREL**

**Applicant**

**and**

**BT GROUP PLC**

**Respondent**

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**[draft] COLLECTIVE PROCEEDINGS ORDER**

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**UPON** the application of the Applicant for a collective proceedings order (the “**CPO Application**”) pursuant to section 47B of the Competition Act 1998 (“**section 47B**”) and Rule 75 of the Competition Appeal Tribunal Rules 2015 (S.I. 2015 No. 1648) (the “**Tribunal Rules**”)

**AND UPON** receipt of a collective proceedings claim form on [15] January 2021

**AND UPON** hearing Counsel for the parties on [ ]

**AND UPON** the Tribunal having given judgment on the CPO Application on [ ]

**IT IS ORDERED THAT:**

**Forum**

1. Pursuant to Rules 18, 52 and 74 of the Tribunal Rules, the proceedings be treated as proceedings in England and Wales.

**Authorisation of Class Representative**

2. Pursuant to section 47B and Rules 77 and 80 of the Tribunal Rules, Mr Justin Le Patourel is authorised to act as the Class Representative to continue collective proceedings on an opt-out basis claiming damages for loss suffered by the Class (as defined below).
3. The remedy sought is an award of aggregate damages for the Class (as defined below) pursuant to section 47C(2) of the Competition Act 1998 together with interest, costs and any further or other relief as the Tribunal may think fit.

4. The Applicant’s address for service is Mishcon de Reya LLP, Africa House, 70 Kingsway, Holborn, London WC2B 6AH (for the attention of Rob Murray and Natasha Pearman).

### **Class definition**

5. The Class shall be defined as: “all persons domiciled in the United Kingdom (except in the **Hull Area**) who, during the **Claim Period**, bought a **BT Standalone Fixed Voice Service** except for the **Excluded Services** (referred to below as “**the Class Members**”)”, whereby:
  - a. **BT Standalone Fixed Voice Service** means any residential landline calling plan service provided by BT, except for the Excluded Services, which (i) includes landline line rental and (ii) has not been sold as part of a bundle with broadband. For these purposes, a bundle refers to a contract, or two or more closely related, linked or interdependent contracts which, individually or together, include and require the purchase of broadband as well as the landline calling plan service.
  - b. **Excluded Services** means BT Basic and BT Home Phone Saver.
  - c. **Hull Area** means the area defined as the Licence Area in the licence granted on 30 November 1987 by the Secretary of State under Section 7 of the Telecommunications Act 1984 to Kingston upon Hull City Council and Kingston Communications (Hull) plc.
  - d. The **Claim Period** means:
    - i. for residential BT Voice Only Customers, between 1 October 2015 and 1 April 2018 inclusive;
    - ii. for business BT Voice Only Customers, between 1 October 2015 and the date of the Tribunal’s final determination of the Claims made by the Sub-class of BT Voice Only Customers or their earlier settlement (or settlement of any part thereof); and
    - iii. for BT Split Purchase Customers, between 1 October 2015 and the date of the Tribunal’s final determination of the Claims made by the Sub-class of BT Split Purchase Customer or their earlier settlement (or settlement of any part thereof).
6. The following categories of persons (as constituted from time to time) shall be excluded from the class and accordingly not be Class Members:
  - a. officers, directors or employees of the Respondent;
  - b. officers, directors or employees of any entities in which the Respondent has a controlling interest;
  - c. all members of the Respondent’s legal team;
  - d. all experts instructed on behalf of the Respondent;
  - e. all members of the Applicant’s legal team;
  - f. all experts instructed on behalf of the Applicant;

- g. all employees of [the claims administrator] engaged in advising and assisting the Applicant and any other professional adviser who may be engaged by the Applicant for the purposes of these proceedings; and
  - h. all members of the Tribunal panel assigned to these proceedings.
7. The following categories of Class Members shall be designated as Sub-classes in the Collective Proceedings:
- i. **BT Voice Only Customers:** Class Members who, during the applicable Claim Period as defined above, have bought a BT Standalone Fixed Voice Service but did not, at the same time, buy a broadband service, either from BT or any other provider.
  - j. **BT Split Purchase Customers:** Class Members who, during the applicable Claim Period as defined above, have bought at the same time both (i) a BT Standalone Fixed Voice Service; and (ii) a broadband service, either from BT or any other provider.

### **Notification**

8. The Class Representative shall publish a Notice of the Collective Proceedings in the form appended to this Order in accordance with Rule 81 of the Tribunal’s Rules.

### **Opting-out and opting-in**

9. Every Class Member who is domiciled in the United Kingdom on [ ] (“**the Domicile Date**”) shall be included in these collective proceedings subject to paragraphs 10 - 11 below.
10. Any Class Member who is domiciled in the United Kingdom on the Domicile Date may opt-out of the Collective Proceedings by giving the Class Representative notice in writing of their decision to opt out by [ ].
11. Any Class Member who is not domiciled in the United Kingdom on the Domicile Date may opt-in to the Collective Proceedings by giving the Class Representative notice in writing of their decision to opt in by [ ].
12. Any notice to be given under paragraphs 10 or 11 above, and any other document to be served on the Class Representative, shall be sent to: [ ].

### **General**

13. There be liberty to apply.

### **DATED:**

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**ANNEX 8**

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*NOTICE OF THE COLLECTIVE PROCEEDINGS ORDER:*

*This is a legal notice that has been issued at the direction of the Competition Appeal Tribunal  
In Case No 0000/o/o/21*

**If you had a residential landline ('home phone') service from BT any time from October 2015 to date, your rights may be affected by a collective action.**

- This notice contains information about the collective action that may affect you.
- The collective action has been filed on behalf of certain people who had a residential landline service from BT in the UK between October 2015 and now, who may have a claim against BT for compensation.
- At this stage, it is important that you understand your legal rights related to this claim. Your legal rights may be affected by this action whether you act or you don't act, so please read this notice carefully for information about your rights and the deadlines to act.
- This notice explains what the collective action is about, who might be eligible to receive a payment, your rights as an affected customer of BT, what action you need to take (if any), and the deadlines that apply.
- To read the Competition Appeal Tribunal's full Collective Proceedings Order which allows the collective action to go ahead, visit [www.callclaim.co.uk](http://www.callclaim.co.uk).

For more information, call 0333 212 1617, or visit [www.callclaim.co.uk](http://www.callclaim.co.uk)

## Summary of Notice

This notice contains information about a court case that may affect you. Your legal rights may be affected whether you act or you don't act, so please read this notice carefully.

The Competition Appeal Tribunal (the "Tribunal") has made a collective proceedings order authorising Mr Justin Le Patourel, to proceed with a collective action against BT Group Plc ("BT"). The terms of the collective proceedings order are set out later in this notice. In a collective action, a claim is brought by a representative (called a class representative) on behalf of a large number of individuals who group together to seek compensation for their losses. Together the group of people make up a class.

In these collective proceedings, Mr Le Patourel has been appointed to act as the class representative for certain people who had a residential landline ('home phone') service from BT in the UK at any time between October 2015 and now (please see paragraph 7 of the General Information section of this notice for further details), who may have a claim against BT for compensation.

If you are one of these people, and you lived in the UK on [insert date], then you are a class member and will be bound by the Tribunal's judgment deciding the outcome of the case, unless you opt out. If you are one of these people but did not live in the UK on that date, then you will only become a class member and be bound by the outcome if you choose to opt in.

This collective action has been brought on the basis that BT has abused a position of dominance and charged its customers excessive prices for the landline services, in breach of the Competition Act 1998. The action brought by Mr Le Patourel is about seeking compensation for BT customers who were overcharged for their landline services as a result of BT's breach of the law.

If the case results in a judgment against BT or a settlement, members of the class may be eligible to receive compensation. If compensation becomes available, details on how to get it and how it will be calculated will be provided at that time. Whatever the outcome of the case, class members will not have to pay anything.

It will be for the Tribunal to decide whether BT has overcharged class members and if so, by how much. Unless you opt out, if the Tribunal makes a judgment on these issues you will be bound by it and the amount of compensation that you are entitled to will be limited to what the Tribunal decides, and no more. If the Tribunal decides that class members are not entitled to any compensation, and you have not chosen to opt out, then you will not be able to seek compensation from BT by any other route.

Therefore, you may want to opt out if you would prefer to bring a separate claim against BT to seek compensation for the overcharges.

For more information, call 0333 212 1617, or visit [www.callclaim.co.uk](http://www.callclaim.co.uk)

## A Summary of Your Rights and Choices:

*Please read this notice carefully.*

*Your legal rights may be affected whether you act or you don't act.*

YOU MAY:	YOUR LEGAL RIGHTS AND CHOICES EXPLAINED	DEADLINE:
<p><b><i>Do nothing and remain in the collective action</i></b></p>	<p>You do not need to do anything if you were living in the UK on [domicile date] and you:</p> <p>Had a BT landline service at any time between October 2015 and April 2018*, but did not receive a broadband service (from BT or any other provider) - <b>Landline-Only Customers</b><sup>1</sup></p> <p style="text-align: center;">or</p> <p>Had a BT landline service and also a broadband service (from BT or any other provider), at any time between October 2015 and today, but these services were not packaged together as part of a landline/broadband bundle – <b>Unbundled Customers</b><sup>2</sup></p> <p>*Note: different dates apply if you are a Landline-Only Customer who used your landline for business purposes. Please see below FAQs for further information.</p> <p>You are excluded if you are a:</p> <ul style="list-style-type: none"> <li>BT customer who took a landline service aimed at business users</li> <li>BT Basic or BT Home Phone Saver customer</li> <li>Any individual living in the Hull area as this area is supplied by KCOM Group Limited and not BT</li> </ul> <p>By doing nothing at this time, you will be included in the collective action and may benefit from any eventual money/compensation which results from this collective action.</p> <p>You will not be liable for any costs.</p>	<p><b><i>None</i></b></p>

<sup>1</sup> Also known as “Voice Only Customers”

<sup>2</sup> Also known as “Split Purchase Customers”

For more information, call 0333 212 1617, or visit [www.callclaim.co.uk](http://www.callclaim.co.uk)

	<p>However, you will also give up the right to make your own claim against BT in respect of the legal claims in this collective action and you agree to be bound by judgments issued by the Tribunal in this case.</p> <p>Although you do not need to contact us to be included in the action, we recommend that you get in touch to provide your contact details so that we can keep you informed about the progress of the case.</p>	
<p><b><i>Opt Out of the collective action</i></b></p>	<p>If you were living in the UK on [domicile date] and you:</p> <p>Had a BT landline service at any time between October 2015 and April 2018*, but did not receive a broadband service (from BT or any other provider) - <b>Landline-Only Customers</b></p> <p style="text-align: center;">or</p> <p>Had a BT landline service and also a broadband service (from BT or any other provider), at any time between October 2015 and today, but these services were not packaged together as part of a landline/broadband bundle - <b>Unbundled Customers</b></p> <p>*Note: different dates apply if you are a Landline-Only Customer who used your landline for business purposes. Please see below FAQs for further information.</p> <p>You are excluded if you are a:</p> <p style="padding-left: 40px;">BT customer who took a landline service aimed at business users BT Basic or BT Home Phone Saver customer Any individual living in the Hull area as this area is supplied by KCOM Group Limited and not BT</p> <p>Then you have the right to request to be excluded from the claim (to decide to “opt out”). By opting out you keep the right to make your own separate claim against BT, but you will not be able to claim a share of any money that becomes available as a result of this collective action.</p> <p>Requests to optout must be received by [insert date].</p>	<p>[Date]</p>

For more information, call 0333 212 1617, or visit [www.callclaim.co.uk](http://www.callclaim.co.uk)



<p><b><i>Opt Into the Claim</i></b></p>	<p>If you were living <b>outside of the UK</b> on [domicile date] and you:</p> <p>Had a BT landline service at any time between October 2015 and April 2018*, but did not receive a broadband service (from BT or any other provider) - <b>Landline-Only Customers</b></p> <p>OR</p> <p>Had a BT landline service and also a broadband service (from BT or any other provider), at any time between October 2015 and today, but these services were not packaged together as part of a landline/broadband bundle - <b>Unbundled Customers</b></p> <p>*Note: different dates apply if you are a Landline-Only Customer who used your landline for business purposes. Please see below FAQs for further information.</p> <p>You are excluded if you are a:</p> <ul style="list-style-type: none"> <li>BT customer who took a landline service aimed at business users</li> <li>BT Basic or BT Home Phone Saver customer</li> <li>Any individual living in the Hull area as this area is supplied by KCOM Group Limited and not BT</li> </ul> <p>Then you must take steps if you want to be included in the claim (i.e. elect to “opt in”). You are NOT automatically included. You can complete an Opt-In Form by visiting <a href="http://www.callclaim.co.uk">www.callclaim.co.uk</a> or by calling the freephone number 0333 212 1617 to receive more information.</p> <p>Requests to opt in must be received by [insert date].</p> <p>If you opt in then you will be in the same position as those class members who live in the UK and are part of the class.</p>	<p>[Date]</p>
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Details on how to sign up for updates, opt in or opt out are available at [www.callclaim.co.uk](http://www.callclaim.co.uk). You may also call the freephone number 0333 212 1617 to receive more information.

For more information, call 0333 212 1617, or visit [www.callclaim.co.uk](http://www.callclaim.co.uk)

## GENERAL INFORMATION

### 1. Why has this Notice been issued?

The Competition Appeal Tribunal has directed that this notice be issued by the class representative (Mr Justin Le Patourel) following a Collective Proceedings Order made on [date]. The Order allows this claim to proceed as a collective action on behalf of eligible BT customers. To read the full Order, visit [www.callclaim.co.uk](http://www.callclaim.co.uk).

The purpose of this notice is to inform you of important legal rights you have related to this collective action. Exercising these rights could affect your ability to get a payment in the future if the case is won and money becomes available. This notice explains what the claim is about, who might be eligible to receive a payment, your rights, what action you need to take (if any) and the deadlines that apply.

Please read this notice carefully as your decisions about this claim will have legal consequences.

### 2. What is a Collective Action?

A law called the Consumer Rights Act 2015 allows for a class representative to bring a collective claim on behalf of a group of individuals who are alleged to have suffered a common loss. Individuals within the group are known as “class members”. Class members do not each need to bring an individual claim to obtain compensation for their loss. Instead, they may all receive compensation through a single collective claim brought on their behalf by the class representative.

The class representative's duty is to act fairly and adequately in the interests of all of the consumers who are part of the class of affected people.

### 3. Who is the Collective Action against?

This Claim is against BT Group Plc (“BT”).

### 4. What is this Collective Action about?

CALL is the Collective Action on Land Lines. CALL is led by the class representative, Mr Justin Le Patourel. CALL is seeking compensation from BT on behalf of 2.3 million residential landline (‘home phone’) customers who were overcharged between October 2015 and now.

### 5. Why has this Claim been brought?

The claim has been brought by Justin Le Patourel, a former Ofcom employee, who the Tribunal has authorised to act as the “Class Representative”, having been satisfied that he will act in the best interests of the group of affected customers and has the relevant skills, experience and financial capability to do so.

Mr Le Patourel applied for this collective action following a review in 2017 by Ofcom, the UK's telecom's regulator, which found that BT had overcharged residential customers who purchased

For more information, call 0333 212 1617, or visit [www.callclaim.co.uk](http://www.callclaim.co.uk)

a BT landline service and either did not also take a broadband service (Landline-Only Customers) or did take broadband, but did not 'bundle' this with their landline in a single, discounted package (Unbundled Customers). This overcharging had gone on since at least 2009.

Ofcom believed BT was able to overcharge in this way because it had a position of power in the telecoms market. In addition, BT knew that few of its Landline-Only Customers and Unbundled Customers, many of whom are older and/or vulnerable, were likely to switch away.

As a result, Ofcom said BT should reduce its charges for its Landline-Only Customers. In April 2018, BT reduced these charges by £7 per month (£84 per year). Ofcom is currently running a consultation regarding its intention to continue to limit the prices BT can charge its Landline-Only Customers for their landlines.

Importantly however, BT did not offer to compensate either:

1. Landline-Only Customers for the excessive prices they had paid from 2009 to April 2018; or
2. Unbundled Customers (and certain Landline-Only Customers that use their landline for business purposes), who we believe are still being overcharged today.

The role of CALL – led by Justin Le Patourel - is to seek compensation for all consumers who were overcharged by BT (except those who opt out). Justin will instruct the lawyers and experts, make decisions on the conduct of the claim and, in particular, will decide whether to present any offer of settlement to the Tribunal for its approval.

Throughout the claim, CALL – on behalf of Justin Le Patourel - is responsible for communicating with affected consumers and for issuing formal notices, such as this notice. CALL will post updates about the claim on the website [www.callclaim.co.uk](http://www.callclaim.co.uk).

## 6. Who is the Class Representative?

The class representative is Mr Justin Le Patourel. During his career, Justin has worked to help consumers get good deals from their telecoms providers and make it easier for them to switch provider when they're unhappy or want to take advantage of a better deal elsewhere.

As class representative, Mr Le Patourel's job is to lead the collective action and act fairly and adequately in the interest of the class members.

Justin is supported by his legal team which is led by Mishcon de Reya. Mishcon de Reya is one of the UK's leading law firms with significant experience of bringing group actions and complex competition law litigation. You will not be charged for any legal (or other) fees.

## 7. Who is “the class” in this Claim and the exceptions?

Who?	Which telecoms service did I take?	When?	Exceptions
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For more information, call 0333 212 1617, or visit [www.callclaim.co.uk](http://www.callclaim.co.uk)

BT residential customers	<b>1. Landline-Only Customers</b> Customers who had a BT landline service but did not receive a broadband service (from BT or any other provider)	Any time between Oct 2015 - Apr 2018  (Oct 2015 – today for certain business customers)	<ul style="list-style-type: none"> <li>• Certain BT business customers (see “What if I used my landline for my business?’ below)</li> <li>• BT Basic or BT Home Phone Saver customers</li> <li>• Customers in the Hull area</li> </ul>
	<b>2. ‘Unbundled Customers</b> Customers who had a BT landline service and also a broadband service (from BT or any other provider), but where those services were not packaged together as part of a landline/broadband bundle	Any time between Oct 2015 - today	

## 8. What if I used my landline for my business?

If at any time from October 2015 to today you used a BT landline service aimed at residential users for business purposes, you are still included in the claim. However, if you used a BT landline service aimed at business users, unfortunately you are excluded from our claim.

If you used a BT landline service aimed at residential users for business purposes, **and** you are a Landline-Only Customer, then the period in which you need to have been a subscriber is extended. Customers in this category are in the class if they were a subscriber at any time between October 2105 and now.

If you are not sure what type of service you have or had, we suggest that you call BT on 0800 800 150 (or +44 150 174 7714 from outside the UK) for confirmation.

## 9. What is an opt-out proceeding? What is the “domicile date”?

The claim is proceeding as an opt-out case. In simple terms, if you were living in the UK on [domicile date] (which is known as the “domicile date”) and you satisfy the class definition, you are included in the class. You do not need to do anything unless you wish to be excluded from the class. This is called ‘opting out’ of the class.

If you were not living in the UK on [domicile date], you satisfy the class definition and you want to participate in this claim, then you must ‘opt into’ the class (see section 16 below on how to do this).

All class members who stay in the class or opt into the class will be bound by any Tribunal judgment. As a class member, you will not be able to bring an individual claim against BT raising the same issues included in this claim.

For more information, call 0333 212 1617, or visit [www.callclaim.co.uk](http://www.callclaim.co.uk)

This notice explains how to opt out or opt into the class.

### **10. How do I get a payment?**

No money is available now and there is no guarantee that money will be available in the future. The case will have to be won in the Tribunal unless a settlement can be agreed with BT before it gets to a hearing. This process can take time, so please be patient. We recommend that you sign up for updates on the progress of the case on our website, [www.callclaim.co.uk](http://www.callclaim.co.uk). If, and when, money becomes available, class members will be notified about how to obtain a payment.

### **11. When will the Tribunal hear the case?**

The date has not yet been decided. Please sign up to receive updates about the case and you will be notified of any significant developments such as hearings. Details of how to receive updates are set out below. You should also regularly check the case website at: [www.callclaim.co.uk](http://www.callclaim.co.uk) for updates.

### **12. What is the Competition Appeal Tribunal?**

The Competition Appeal Tribunal is a specialist court based in London that covers the whole of the UK and hears disputes such as these. The Tribunal publishes its Rules and Guidance, together with information about what it does, on its website [www.catribunal.org.uk](http://www.catribunal.org.uk). A summary of this claim can be found on the Tribunal's website.

## **WHO IS IN THE CLASS?**

### **13. What does it mean to be a class member?**

As a class member, if money becomes available, you will be eligible to receive a payment to compensate you for your loss. You will also be legally bound by all Tribunal judgments with respect to this claim. If a payment becomes available, details on how to receive it and how the amount will be calculated will be provided at that time. These details will not be known and are not known until that time.

You will not be liable for any costs of the claim.

Whether Justin Le Patourel wins money for the class or not, unless you opt out, you will never be able to make your own claim against BT in respect of the claims included in this case.

### **14. How do I know if I'm a class member?**

If you were a Landline-Only Customer or an Unbundled Customer (see definition at question 7) during the relevant periods and none of the exceptions listed apply to you, then in legal terms you are known as a 'Class Member'. Justin Le Patourel is seeking compensation for Class Members.

If you are not sure what type of account or service you have or had, we suggest that you call BT on 0800 800 150 (or +44 150 174 7714 from outside the UK) for confirmation.

For more information, call 0333 212 1617, or visit [www.callclaim.co.uk](http://www.callclaim.co.uk)

Remember, our claim does not include:

- a. Customers who used a BT landline service aimed at business users.
- b. Customers who took BT Basic or BT Home Phone Saver (as BT priced these products separately).
- c. Individuals living in the Hull area (as BT does not provide telecom services here).
- d. BT's overcharging prior to October 2015 (as the legal process in the UK does not allow for claims prior to this date)

Members of different sub-classes may be entitled to different amounts of compensation if the claim succeeds.

## HOW TO OPT OUT OR OPT IN

### 15. I am an affected consumer and I want to come out of the class

If you are an affected consumer and you were living in the UK on [domicile date] and you want to come out of the class, you must take steps to opt out.

Visit [www.callclaim.co.uk](http://www.callclaim.co.uk) and complete the Opt-Out Form on the website. On the Opt-Out Form you will be asked to confirm the following statement “**I want to opt out of the collective claim against BT Group Plc, Case No. 0000/0/0/21**” and provide your full name, postal address, email address and telephone number.

If you prefer, you may also opt out by post by sending a letter with the information listed in the previous paragraph. To assist you in submitting an Opt-Out by post, a sample Opt-Out Letter is available at [www.callclaim.co.uk](http://www.callclaim.co.uk). If you would like to be sent a stamped addressed envelope (“SAE”) to submit your Opt-Out, please send an email with your postal address to [SAE@callclaim.co.uk](mailto:SAE@callclaim.co.uk). Please send your letter to:

CALL Claim Opt-Outs  
PO Box XXX  
LONDON  
XXX XXX

To be considered, your Opt-Out Request must be received or postmarked by [date]. Once your Opt-Out Request is received and processed, we will send you an acknowledgment by email if you have provided an email address, or by post if not.

By opting out, you will not be able to receive a payment from this claim if money becomes available. However, you may be able to bring your own separate claim against BT for the same issues.

**IMPORTANT CONSIDERATION:** Please note, if you opt out and then wish to bring a claim on your own against BT, you must do so within six months of the date on which you opt out. If you

For more information, call 0333 212 1617, or visit [www.callclaim.co.uk](http://www.callclaim.co.uk)

do not file an individual claim against BT within this timeframe, your claim will be time barred (meaning the time permitted for you to bring an individual claim will have passed).

**16. I am an affected consumer not living in the UK on [date] and I want to join the class**

We believe there may be small proportion of affected consumers not living in the UK on [date] (even if they were before). If you are one of those, you must take steps to opt into the class if you want to be a part of the claim and be eligible to receive a payment in the future.

Visit [www.callclaim.co.uk](http://www.callclaim.co.uk) and complete the Opt-In Form on the website. On the Opt-In Form, you will be asked to provide your full name, postal address, email address and telephone number. You will also be asked to provide information about when you were living in the UK.

If you prefer, you may also opt in by post by sending a letter with the information listed in the previous paragraph. To assist you in submitting an Opt-In by post, a sample Opt-In Letter is available at [www.callclaim.co.uk](http://www.callclaim.co.uk). If you would like to be sent a stamped addressed envelope (“SAE”) to submit your Opt-In, please send an email with your postal address to [SAE@callclaim.co.uk](mailto:SAE@callclaim.co.uk). Please send your letter to:

CALL Claim Opt-Ins  
PO Box XXX  
LONDON  
XXX XXX

To be considered, your Opt-In Request must be received or postmarked by [date]. Once your Opt-In Request is received and processed, we will send you an acknowledgement by email if you have provided an email address, or by post if not.

**IMPORTANT CONSIDERATION:** Please note, if you are an affected consumer not living in the UK on [date] and you decide not to opt in and then subsequently wish to bring a claim on your own, you must do so within six months of [date] or your claim will be time barred (meaning the time permitted for you to bring an individual claim will have passed).

**17. What happens if I am an affected consumer not living in the UK on [date] and I don't opt in by [date]**

Under the rules of the Tribunal, if you are an affected consumer not living in the UK on [date], you are required to submit an Opt-In Request by [date] to be part of the class (*see* previous question). If you do not opt in by [date] and money later becomes available, the only way for you to be eligible to receive a payment is for the Tribunal to give you permission to opt in at a later date. There is no guarantee this permission will be given so you should opt in by [date] if you want to be eligible to get a payment.

**WOULD LIKE MORE INFORMATION?**

For more information, call 0333 212 1617, or visit [www.callclaim.co.uk](http://www.callclaim.co.uk)

### **18. How can I stay updated on the progress of the claim?**

There are a number of ways that you can receive updates:

You can visit [www.callclaim.co.uk](http://www.callclaim.co.uk) and register

You can call 0333 212 1617 and provide your contact details

You can follow our social media channels [insert details]

If, and when, money becomes available, you will be contacted with information on how to claim your share if you have registered for updates.

### **19. How can I get more information?**

This notice summarises the Collective Proceedings Order. To read the full Order and see other information about the claim, visit [www.callclaim.co.uk](http://www.callclaim.co.uk).

For more information, call 0333 212 1617, or visit [www.callclaim.co.uk](http://www.callclaim.co.uk)



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**ANNEX 9**

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- [Landline prices review to protect elderly and vulnerable](#)

## Landline prices review to protect elderly and vulnerable



01 December 2016

- **Ofcom concerned about cost of line rental for landline-only customers**
- **Review will ensure customers are protected and get value for money**

**Ofcom has today announced a [review of the retail market \(https://www.ofcom.org.uk/consultations-and-statements/category-1/narrowband-market-review\)](https://www.ofcom.org.uk/consultations-and-statements/category-1/narrowband-market-review) for standalone landline telephone services, to ensure that customers receive value for money.**

Overall competition in the telecommunications sector remains strong, with consumers getting better value for money in recent years (see chart 1). But Ofcom is concerned that people who buy landline services on their own are not being served well by the market.

Our analysis shows that all major landline providers have increased their line rental charges significantly in recent years – by between 28% and 41% in real terms. This is despite providers benefitting from around a 25% fall in the underlying wholesale cost of providing a landline service (see chart 2).

Price increases are felt most acutely by ‘standalone’ landline customers – those who do not have broadband or a pay-TV service. They do not benefit from strong competition in the market for ‘bundled’ communications – where landline, broadband and sometimes pay-TV services are packaged together.

Ofcom’s analysis also shows that elderly and vulnerable people, who make up a significant proportion of standalone landline customers in the UK, are particularly affected by price rises (see chart 3). They are often very reliant on their landline, and more likely than most to have stayed with the same phone company all their life.

Ofcom’s review will establish whether measures are needed to protect this group of customers. We are now analysing the market in detail and, depending on our findings, we expect to publish a consultation in early 2017.

Jonathan Oxley, Ofcom’s Competition Group Director, said: “Our evidence shows that landline providers have been raising the price of line rental, even as their costs have been coming down.

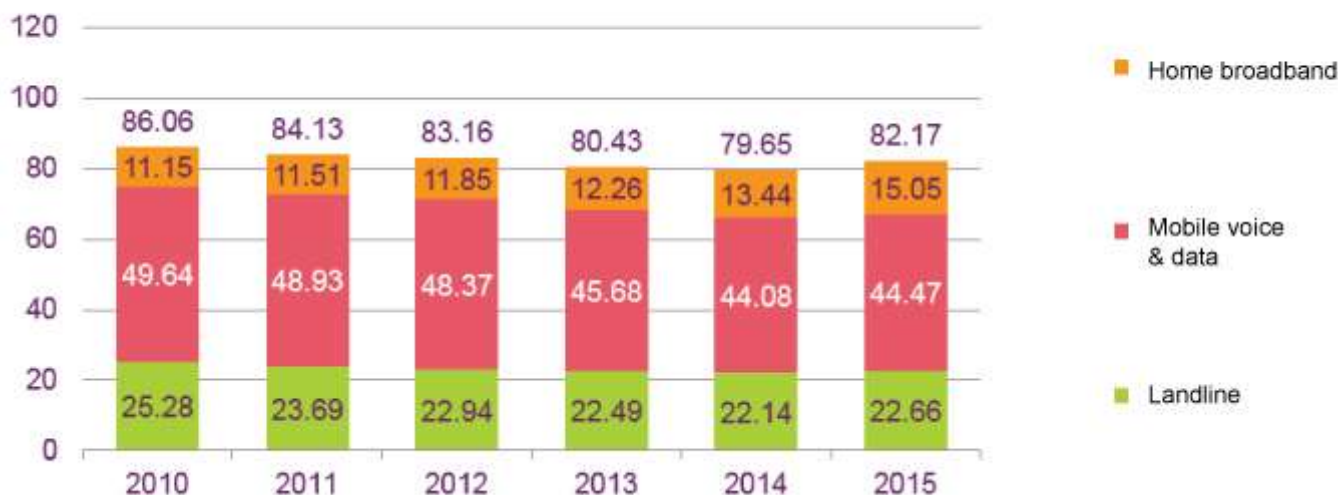
“We’re particularly concerned for older and vulnerable customers, who rely on their landline and are less likely to change provider. So we’re reviewing this market to ensure these customers are protected and getting value for money.”

In January this year, Ofcom published research ([https://www.ofcom.org.uk/data/assets/pdf\\_file/0031/98077/Ofcom-Fixed-BB-Advertising-of-prices-Report-2015.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0031/98077/Ofcom-Fixed-BB-Advertising-of-prices-Report-2015.pdf)) it carried out with the Advertising Standards Authority on consumers’ understanding of how broadband prices were advertised, including the separation of line rental charges.

Following this work, the ASA introduced new rules (<https://www.asa.org.uk/news/tougher-approach-to-broadband-price-claims-in-ads.html>) in October, which we welcome, requiring broadband prices to be clearer and inclusive of line rental. This may benefit customers taking bundles, and reduce incentives to increase line rental charges. However, it is unlikely to benefit landline-only customers – another reason that Ofcom is reviewing this market.

**Chart one:**

**Average household spending on telecoms services**  
(£ per month, 2015 prices)

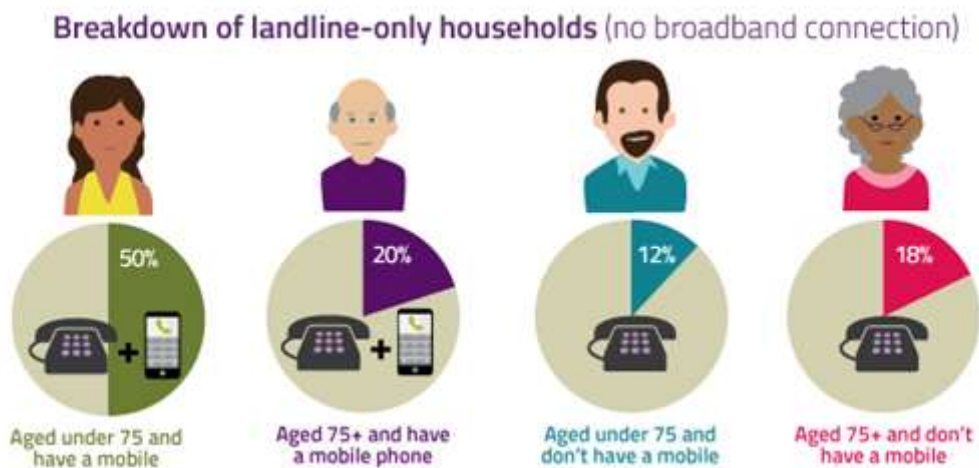


*Landline spending reflects reduced use of landlines, and lower cost of making calls*

**Chart two:**



**Chart three:**



## Wholesale market review

Today's announcement is made within a consultation covering Ofcom's separate [review of the wholesale markets](https://www.ofcom.org.uk/consultations-and-statements/category-1/narrowband-market-review) (<https://www.ofcom.org.uk/consultations-and-statements/category-1/narrowband-market-review>) that underpin fixed voice services in the UK.(1)

The consultation relates to wholesale prices that BT can charge other telecoms providers to offer homes and businesses a telephone service over its copper network. Regulation resulting from the review will apply from 1 October 2017 to 30 September 2020.

The wholesale review looks at the following markets:

- Wholesale exchange lines – the traditional lines used by residential and business consumers;
- ISDN (Integrated Services Digital Network) – digital lines primarily used by larger businesses with multiple lines or sites, for example call centres;
- Call origination – a service that enables people to make calls over these lines; and
- Call termination – the service used by a telecoms provider to connect their customers' incoming calls.

Today's consultation closes on 28 February 2017.

## NOTES TO EDITORS

1. Ofcom is reviewing these wholesale markets under the Electronic Communications Framework. This Framework applies to all transmission networks and services (including access) for electronic communications including telecommunications (fixed and mobile), e-mail and access to the internet. Ofcom may impose appropriate remedies in retail markets in which there is significant market power where wholesale remedies would not achieve its statutory objectives.

Source for Chart 1: Ofcom Communications Market Report (Figure 4.34). Ofcom / operators / ONS. Between 2011 and 2015 the average home broadband data use per month increased from 17 GB to 82GB.

Source for Chart 2: Ofcom/Pure Pricing UK Broadband Updates

Source for Chart 3: 2015 Jigsaw residential survey (wave 1).

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- Contact Ofcom (<https://www.ofcom.org.uk/about-ofcom/contact-us>)

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## See also...

Half of homes could boost their broadband (<https://www.ofcom.org.uk/about-ofcom/latest/media/media-releases/2018/half-of-homes-could-boost-their-broadband>)

14 December 2018

Half of British households could switch to faster broadband today, Ofcom has found, as it announces a range of action to protect loyal broadband customers and help people get a better deal.

Helping people to shop around and secure the right deal (<https://www.ofcom.org.uk/about-ofcom/latest/media/media-releases/2017/helping-people-to-shop-around-and-secure-the-right-dea>)

We've announced an initiative to help consumers engage with communications markets. We want more people to shop around with confidence and take full advantage of the wide choice on offer.

Ofcom confirms priorities for 2017/18 (<https://www.ofcom.org.uk/about-ofcom/latest/media/media-releases/2017/ofcom-confirms-priorities-for-201718>)

30 March 2017

Ofcom has published its 2017/18 Annual Plan, outlining its priorities for the next financial year.

BT's landline-only customers set for cheaper bills (<https://www.ofcom.org.uk/about-ofcom/latest/media/media-releases/2017/bts-landline-only-customers-set-for-cheaper-bills>)

28 February 2017

More than two million people who buy only a landline telephone service from BT would see their monthly bills cut by at least £5 per month, under plans announced by Ofcom today.

See all results (</search?query=Landline prices review to protect elderly and vulnerable>)

## Advice for Businesses

A starter pack for businesses (<https://www.ofcom.org.uk/advice-for-businesses/inexperienced-digital-users>)

Knowing your rights (<https://www.ofcom.org.uk/advice-for-businesses/knowning-your-rights>)

Disabled business customers (<https://www.ofcom.org.uk/advice-for-businesses/help-for-disabled-business-customers>)

Read all our advice for businesses (<https://www.ofcom.org.uk/advice-for-businesses>)

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**ANNEX 10**

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# Protecting voice-only landline telephone customers

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[Protecting voice-only landline telephone customers](#) – Welsh overview

Redacted [✂]

## **CONSULTATION:**

**Publication Date:** 10 December 2020

**Closing Date for Responses:** 21 January 2021

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# 1. Overview

The Covid-19 pandemic has demonstrated that telecoms services have never been more important. While many people and businesses now rely on online communications such as email, instant messaging apps and video calls, the traditional fixed-line phone remains vital for customers who choose to take a landline service. In 2019, there were still 1.2m voice-only customers, representing approximately 5% of total residential customers.<sup>1</sup> The overwhelming majority of voice-only landline customers take their service from BT, which has a share of over 75% of such customers.

The prices those customers pay for their voice-only service have been protected since 1 April 2018 through BT's voluntary commitments, which we accepted in 2017. As well as an initial price cut of £7 to line rental, BT also capped increases to line rental and call charges at the rate of inflation (CPI) for three years. These voluntary commitments expire on 31 March 2021. BT has now made another offer of further voluntary commitments, which we propose to accept, in lieu of imposing formal regulation on BT, to ensure continued protections for voice-only customers.

## What we are proposing

The commitments BT has offered, which we propose to accept, are:

- **Continue with an inflation-linked control (CPI+0%) on the basket of line rental and call charges for voice-only products.** We believe a continuation of prices which remain flat in real terms is a proportionate, clear and timely way to continue to protect consumers. BT has also committed to an annual CPI+0% limit on prices for its Home Phone Saver product and a safeguard cap of CPI+2.5% for its line rental product
- **Commitment duration of five years.** This will provide certainty for customers for the next five years and allow us to reassess the right protections once the Public Switched Telephone Network (PSTN) switch-off has taken place, which is scheduled to be completed by December 2025
- **Commitments apply to all voice-only products and services taken by customers, regardless of the technology used to deliver the service.** This will ensure that customers are protected, irrespective of the technology used to deliver the service. We think this is particularly important as customers are migrated to different technologies – such as ‘voice over internet protocol’ (VoIP) – as a result of PSTN switch-off
- **Commitments also apply to any new products or services introduced throughout the 5-year commitment period** that are offered on a voice-only basis
- **BT to provide information to Ofcom on its compliance with the commitments on an annual basis.** Compliance is an important part of monitoring voluntary commitments. BT will provide Ofcom with an externally-audited annual compliance statement. It will also publish an annual compliance statement on its website.

<sup>1</sup> "Voice-only" refers to voice-only landline products which feature a call service to and from a fixed connection, the majority of which are currently delivered via the analogue public switched telephone network (PSTN), but which may also increasingly be delivered over digital internet-based (IP) technologies.

### Protecting voice-only landline customers

The overall number of customers taking voice-only products has reduced from 1.5 million customers in early 2017 to 1.2 million in late 2019 - a decline of almost 20%. While BT's volumes are declining, we have seen its total share of customers increasing to over 75% (from just over two-thirds in 2017).

As new and alternative products continue to be developed, we are seeing some wholesale cost uncertainty for providers who currently use copper-based services, which are currently used to deliver the majority of voice-only products, and which we plan to deregulate over the coming years. So, while there are still a limited number of retail providers in addition to BT serving voice-only customers, we expect that over the next few years, the choice of providers will become even more limited. This is because PSTN switch-off will drive providers towards offering IP-based packages, which are more likely to include broadband.

Levels of switching among voice-only customers are low, particularly for BT customers. Voice-only customers also tend to be older, from lower socioeconomic grades, not working, and more financially vulnerable.

We continue to believe that price protection for voice-only customers remains necessary to address our previous concerns from our last review in 2017, which included lack of competition in the market and poor value for money for this group of customers. We welcome the further voluntary commitments BT has offered, which build on the foundations of the previous protections. We have carefully considered these commitments and our provisional view is that they would offer sufficient protections for these customers, reflecting current market conditions.

These voluntary commitments would not prevent us from reviewing the market or considering regulatory intervention at a later date, if we were to consider it appropriate to do so. If we decide to accept BT's commitments following our assessment of responses to this consultation, we still intend to continue to monitor this market.

### Next steps

In this document, we set out our proposed approach to ensuring continued protections for voice-only customers. We ask for stakeholders to respond to this consultation by 21 January 2021. Once we have considered representations, we expect to issue a statement of our decision in March, ahead of the expiry of the existing commitments.

## 2. Introduction

- 2.1 For a small but significant number of customers who choose to take a voice-only service, the traditional fixed line phone remains vital.<sup>2</sup> In 2019, there were still 1.2 million voice-only customers, approximately 5% of total residential voice-only customers. The overwhelming majority of these customers take their service from BT, which has a share of over 75%.<sup>3</sup>
- 2.2 The prices which those customers pay for the voice-only service have been protected since 1 April 2018 through BT's offer of a voluntary commitment, which we accepted in 2017 following a review of the market.<sup>4</sup>
- 2.3 In this section we explain the circumstances leading to the introduction of the existing commitments, together with information showing BT's compliance with them. We also explain our concerns arising from the 2017 review, which remain relevant in considering whether we should accept BT's proposed new commitments in lieu of imposing formal regulation on BT. We also explain our role in the protection of voice-only customers.

### Existing voluntary commitments on voice-only services

#### Our February 2017 consultation made proposals to impose regulation

- 2.4 In 2016-17, we reviewed the market for standalone voice-only telephone services because we were concerned that customers buying these services on a standalone basis could be missing out on the benefits of competition. At the time of that review, retail prices were rising, despite wholesale prices falling in real terms - as shown in Figure 1 below.<sup>5</sup> We were also concerned about levels of consumer engagement, which were low.

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<sup>2</sup> "Voice-only" refers to voice-only landline products which feature a call service to and from a fixed connection, the majority of which are currently delivered via the analogue public switched telephone network (PSTN), but which may also increasingly be delivered over digital internet-based (IP) technologies.

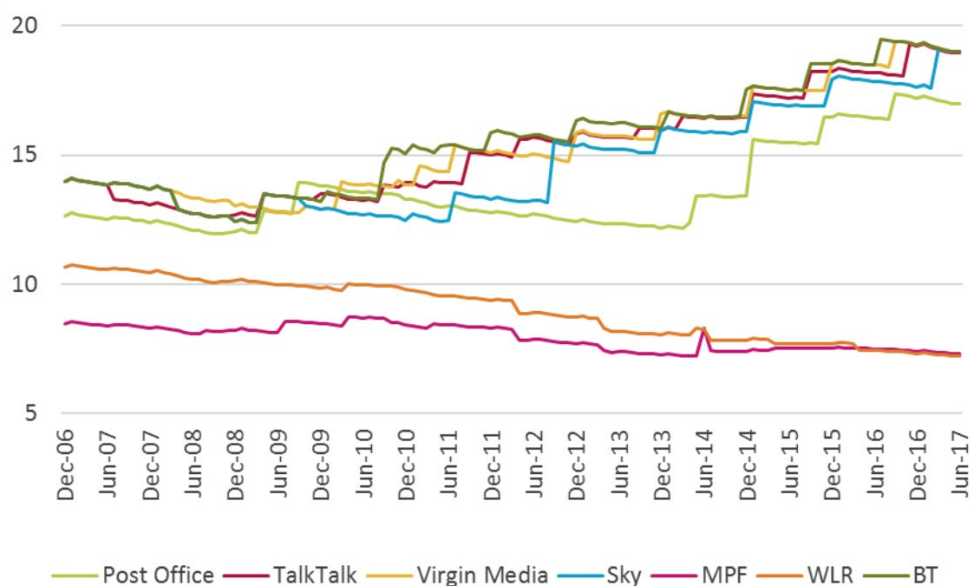
<sup>3</sup> BT s135 response dated 17 November 2020.

<sup>4</sup> [https://www.ofcom.org.uk/data/assets/pdf\\_file/0015/107322/standalone-voice-only-statement.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0015/107322/standalone-voice-only-statement.pdf)

<sup>5</sup> From 2009 to the time of the review, voice-only customers had been exposed to increasing line rental prices, despite wholesale charges for Wholesale Line Rental (WLR - the underlying technology which supports the majority of voice-only services) falling by up to 27% in real terms.

## Protecting voice-only landline customers

Figure 1: Wholesale and retail line rental price movements (£/month at June 2017 prices)



Source: February 2017 consultation

- 2.5 We found evidence that competition was not benefiting this group of customers and price increases were generally not justified given declining wholesale costs. We considered that customers buying voice-only services on a standalone basis were receiving poor value for money.
- 2.6 In February 2017, we published a consultation on our proposals for dealing with those issues (the 'February 2017 consultation').<sup>6</sup> In particular, we provisionally identified a market for standalone fixed voice access and a market for standalone fixed voice calls, both of which were UK-wide (excluding the Hull area). We proposed that BT held significant market power (SMP) in both markets.<sup>7</sup> To address the consumer detriment we identified, and which we considered arose from a lack of competition in the markets, we proposed several options for regulation, including a one-off price cut on BT's retail line rental price, and further consumer engagement remedies.

<sup>6</sup> Consultation: [Review of the market for standalone landline telephone services \(February 2017\)](#)

<sup>7</sup> The concept of 'SMP' is, in this context, defined under legislation as being equivalent to the competition law concept of 'dominance', namely a firm is particularly deemed to have SMP if, either individually or jointly with others, it 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.

## Our October 2017 statement concluded that consumers were worse off because of insufficient competition

- 2.7 In October 2017, we published our statement setting out our conclusions in light of the further market assessment we made following the February 2017 consultation (the ‘October 2017 statement’).<sup>8</sup>
- 2.8 In our market assessment we concluded, in particular, that:
- BT’s position in the markets for the purchase of voice-only access and calls was consistent with the position we set out in the February 2017 consultation for standalone fixed voice services more generally;
  - BT was the dominant provider of standalone fixed voice services with around 70% market shares;
  - we considered that insufficient competition in these markets had led to customers being materially worse off.
- 2.9 In relation to the consumer detriment, we explained our concerns about voice-only customers stemmed from the fact that line rental prices had been increasing in real terms since 2010, despite falling wholesale charges for products used to provide line rental. We also identified a concern that the provision of standalone fixed voice services was not competitive.
- 2.10 We concluded that a price cut was essential to address our concerns. In addition, we also considered low consumer engagement was another factor which contributed to cementing BT’s market position, and therefore we considered it important this should be addressed. However, given our concerns were addressed by BT’s proposed voluntary commitments (which we discuss below), we decided not to proceed with the imposition of regulatory remedies. We also did not consider it necessary to reach a formal determination of significant market power (SMP) in the markets for voice-only access and calls.
- 2.11 In our February 2017 consultation, we had proposed that voice-only and split purchase customers should be considered part of the same market because we understood that it was not technically possible for providers to differentiate between these customers.<sup>9</sup> However, in our October 2017 statement, after further assessing the position, we noted that it was in fact possible for providers to differentiate between voice-only and split purchase customers, and that they could choose to set different prices (or other terms and conditions) between these two customer groups if they wished.
- 2.12 In our October 2017 statement, we noted that split purchasers are typically younger and more technologically literate than voice-only customers, and, by definition, have internet access which allows them to access alternative offers more easily. Unlike voice-only customers, split purchasers have a wide range of choices available to them, such as dual-

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<sup>8</sup> Statement: [Review of the market for standalone landline telephone services \(October 2017\)](#)

<sup>9</sup> Split purchases customers take a voice-only service from one provider and a broadband service from a different provider.

**Protecting voice-only landline customers**

play (telephone and broadband) bundles. We therefore focused our intervention on voice-only customers.

**BT offered voluntary commitments for retail voice-only customers which met our requirements**

- 2.13 In response to our February 2017 consultation proposals, BT proposed a set of voluntary commitments to address the concerns we had identified. BT committed to:
- a) a one-off, line rental price reduction of £7 per month (including VAT) and limiting subsequent increases to CPI+2.5%;
  - b) raise the prices of a basket of call and line rental products by no more than inflation (CPI+0%) each year;
  - c) not increase the charges for Home Phone Saver<sup>10</sup> before 1 April 2021;
  - d) report information to allow Ofcom to monitor BT's compliance with the voluntary commitments; and
  - e) a commitment to work to improve the information available, to ensure that both voice-only customers and split purchasers were aware of possible savings.
- 2.14 We considered the commitments would bring certainty and benefits for customers more quickly than a formal intervention. We noted that the proposals would bring prices closer to cost and so mitigate the immediate consumer detriment, while also supporting the development of information remedies to encourage consumers to shop around for the best deal and promote increased competition.
- 2.15 BT committed to those voluntary commitments for a period of three years, beginning on 1 April 2018 and ending 31 March 2021.

**Compliance with the voluntary commitments****BT commitment to limit line rental price increases to CPI+2.5%**

- 2.16 Following the initial £7 reduction in the monthly price of line rental to £11.99 on 1 April 2018, BT subsequently increased the price by 1.25% to £12.14 on 31 March 2020. This was below the 4.8% increase for 2019/20 permitted under the voluntary commitments.<sup>11</sup>
- 2.17 To date, BT has not increased the line rental price in 2020/21, but the voluntary commitments would allow a price increase of up to 4% (i.e. up to £12.63).<sup>12</sup>

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<sup>10</sup> The Home Phone Saver product bundles line rental, calls and features into a package. See BT's website: [Learn about Home Phone Saver](#).

<sup>11</sup> CPI of 2.3% (November 2018) + 2.5% = 4.8%.

<sup>12</sup> CPI of 1.5% (November 2019) + 2.5% = 4.0%.



## Protecting voice-only landline customers

**BT's commitment to limit the basket of line rental and call products price increases to CPI+0%**

- 2.18 BT has provided us with information showing how rental and call price changes compared to the voluntary commitments for the financial periods 2018/19, 2019/20 and 2020/21.<sup>13</sup> Although the information for 2020/21 is provisional as the financial year is not yet complete, it provides a good estimate of prices changes. BT has told us it expects to increase prices on 31 March 2021 (the last day of the current voluntary commitments) by CPI+3.9%, however this is unlikely to impact the average price change for 2020/21, and therefore compliance with the commitments.<sup>14</sup>
- 2.19 Figure 2 below shows the price changes relating to the basket of line rental and call products allowed under the voluntary commitments, compared to the actual price changes which BT made.

**Figure 2: Basket of line rental and calls: price changes**

	2018/19	2019/20	2020/21	3 Year Total
Allowed price change (CPI)	3.16%	2.29%	1.50%	7.11%
Actual price change	3.98%	0.34%	-0.65%*	3.65%*

\*The price change for 2020/21 (and hence the 3 year total) is provisional and likely overestimates the annual price change as BT has assumed all rental and call prices will increase by CPI+3.9% on 31 March 2021. Source: BT response dated 17 November 2020 to question 3 of the s135 notice dated 2 November 2020

- 2.20 We note that BT did not meet its voluntary commitments in 2018/19 as a result of a modelling error. BT made a charitable donation of £142k to recognise the impact of this error.
- 2.21 Figure 2 also shows that, over the three-year period, BT is expected to have increased basket prices by less than allowed under its voluntary commitments, with basket prices increasing by 3.65% compared to the 7.11% permitted under the commitments. The basket price reduction in 2020/21 was mostly due to BT capping the monthly price of some out of bundle calls at £5 in response to Covid.<sup>15</sup>

**BT conducted voluntary trials to test customer information remedies****Voice-only customers**

- 2.22 As part of the voluntary commitments, BT agreed to trial remedies to improve the information available to voice-only customers to encourage them to engage and help them to decide if they were on the best deal. In 2018, BT conducted a randomised control trial

<sup>13</sup> Spreadsheet provided in BT response dated 17 November 2020 to question 3 of the s135 notice dated 2 November 2020.

<sup>14</sup> BT s135 response dated 17 November 2020. The price increase is consistent with BT's announcement '[annual price changes and CPI](#)'.

<sup>15</sup> See BT website: [Keeping us all connected at a critical time](#) [accessed 20 November 2020]

**Protecting voice-only landline customers**

(RCT) of different types of information sent by letter aimed at improving engagement amongst BT's voice-only customers. The trials tested the effectiveness of sending these customers different types of information, via letter, about the deals available to them. There were six groups of customers, in addition to a control group, and each was sent a letter that included different types of information, such as information on average speed, voice-only offers and the option to take up a broadband service.

## 2.23 Key findings included:

- A general letter, which didn't include much detailed information, did not have a significant impact on levels of engagement, and actually led to increased contact and complaints to BT without encouraging shopping around;
- Sending a detailed voice-only offer, or information on average spend, in the letter led to a statistically significant increase in engagement, although this was relatively small in absolute terms; and
- Adding information about broadband services generally reduced the level of engagement, suggesting that the inclusion of information which many of these customers might see as irrelevant weakened the other messages in the letter.<sup>16</sup>

2.24 In February 2020, we introduced new requirements on providers to notify their residential and business customers when their minimum contract period is coming to an end (end-of-contract notifications, or ECNs), and to tell residential customers about the best tariffs available from their provider (annual best tariff notifications, or ABTNs). BT noted its view that ECNs and ABTNs seek to achieve broadly the same outcomes as the behavioural commitments communications which we had previously accepted, and that to send both would be disproportionate and potentially confusing.<sup>17</sup>

2.25 We agreed that requiring BT to send separate information as part of its commitments for voice-only customers, in addition to the ECN and ABTN which it would now also be sending, could cause confusion. But we also considered it important to incorporate any insights gained from the randomised control trial and accompanying survey into BT's communications. In light of the findings, BT therefore formulated revised text to be used in ECN and ABTN communications sent out to these customers.

**Split purchase customers**

2.26 The voluntary arrangement on information remedies also included a commitment to send an annual statement to split purchase customers, to help them take advantage of the deals on offer in the market by explaining that they could get a better deal if they purchased services as part of a bundle. BT issued split purchaser annual statements until ECNs and ABTNs came into effect, at which point it incorporated these statements into the new annual communications.

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<sup>16</sup> [Consultation document: Trialling consumer remedies \(September 2019\)](#)

<sup>17</sup> [Statement: Helping consumers get better deals - statement on end-of-contract notifications and annual best tariff information \(May 2019\), Section 6 pp. 67 - 68](#)

## Our role in protecting voice-only customers

- 2.27 We have noted that BT has now offered new voluntary commitments (which we assess in Section 4) upon the expiry of the existing commitments on 31 March 2021. Whilst we are minded to accept those commitments in lieu of imposing formal regulation on BT such as, for example, a price cap (which is what we proposed in the 2017 February consultation), we will explain our role in protecting voice-only customers, given our continuing concerns.
- 2.28 The legal framework relevant to our consideration of the issues considered in this consultation is set out in Part 2 of the Communications Act 2003 (the “2003 Act”). Specifically, one type of regulation we may impose on communications providers (such as BT) is significant market power (SMP) conditions.
- 2.29 In light of BT’s proposed new commitments, we are not setting out in this consultation any formal proposals for defining relevant markets, SMP designation and SMP conditions. However, our analysis in this consultation builds on our considerations under the market review process conducted in 2017.
- 2.30 Our proposals in this consultation focus instead on addressing the concerns we continue to have in protecting voice-only customers. In that regard, our proposals are seeking, in particular, to secure or further the performance of our general duties under section 3 of the 2003 Act in furthering the interests of citizens and of consumers, where appropriate, by promoting competition. In so doing, we have had regard to various factors including:
- the desirability of promoting and facilitating the development and use of effective forms of self-regulation;
  - the needs of persons with disabilities, of the elderly and of those on low incomes;
  - the different interests of persons in the different parts of the United Kingdom, of the different ethnic communities within the United Kingdom and of persons living in rural and in urban areas; and
  - the interests of those consumers in respect of choice, price, quality of service and value for money.
- 2.31 In performing our general duties in this context, we have also had regard to the principles under which our regulatory activities should be transparent, accountable, proportionate, consistent, and targeted only at cases in which action is needed, including by reference to Ofcom’s general regulatory principles. Additionally, our proposals seek to secure that we do not impose on BT any unnecessary regulatory burdens in light of its proposed new commitments.

## Impact assessment

- 2.32 The analysis presented in the whole of this consultation represents an impact assessment, as defined in section 7 of the 2003 Act.
- 2.33 Impact assessments provide a valuable way of assessing different options for regulation and showing why the preferred option was chosen. They form part of best practice policy-

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making. This is reflected in section 7 of the 2003 Act, which means that generally Ofcom has to carry out impact assessments where its proposals would be likely to have a significant effect on businesses or the general public, or when there is a major change in Ofcom’s activities. However, as a matter of policy Ofcom is committed to carrying out and publishing impact assessments in relation to the great majority of its policy decisions. For further information about Ofcom’s approach to impact assessments, see our guidelines, ‘Better policy-making: Ofcom’s approach to impact assessment’.<sup>18</sup>

- 2.34 Specifically, pursuant to section 7, an impact assessment must set out how, in our opinion, the performance of our general duties (within the meaning of section 3 of the 2003 Act) is secured or furthered by or in relation to what we propose.

**Equality impact assessment**

- 2.35 Section 149 of the Equality Act 2010 (the “EA 2010”) imposes a duty on Ofcom, when carrying out its functions, to have due regard to the need to eliminate discrimination, harassment, victimisation and other prohibited conduct related to the following protected characteristics: age; disability; gender reassignment; marriage and civil partnership; pregnancy and maternity; race; religion or belief; sex and sexual orientation. The EA 2010 also requires Ofcom to have due regard to the need to advance equality of opportunity and foster good relations between persons who share specified protected characteristics and persons who do not.
- 2.36 Section 75 of the Northern Ireland Act 1998 (the “NI 1998”) also imposes a duty on Ofcom, when carrying out its functions relating to Northern Ireland, to have due regard to the need to promote equality of opportunity and regard to the desirability of promoting good relations across a range of categories outlined in the NI 1998. Ofcom’s Revised Northern Ireland Equality Scheme explains how we comply with our statutory duties under the NI 1998.<sup>19</sup>
- 2.37 To help us comply with our duties under the EA 2010 and the NI 1998, we assess the impact of our proposals on persons sharing protected characteristics and in particular whether they may discriminate against such persons or impact on equality of opportunity or good relations.
- 2.38 We do not consider that our proposals have equality implications under the EA 2010 or the NI 1998.

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<sup>18</sup> See Ofcom’s website, <http://www.ofcom.org.uk/about/policies-and-guidelines/better-policy-makingofcoms-approach-to-impact-assessment/>.

<sup>19</sup> Ofcom, 2014. *Revised Northern Ireland Equality Scheme for Ofcom*, January 2014 (updated December 2019). [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0023/123737/Revised-NI-Equality-Scheme.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0023/123737/Revised-NI-Equality-Scheme.pdf)

### 3. Market developments since our last review

- 3.1 In this section, we discuss market developments that have taken place since the introduction of the existing voluntary commitments. We will also explain the reasons why we consider we need continued protections for voice-only customers.
- 3.2 Our analysis of market developments in this section is particularly based on information requested and received from the main providers. We have requested data on volumes of customers and pricing of voice-only services, and asked about providers' plans for future provision and promotion of voice-only services. We received responses from BT, Post Office, Virgin Media, OVO (previously part of SSE Retail), TalkTalk and Sky.

#### The number of voice-only customers continues to decline with BT serving the majority of customers

- 3.3 The data we collected indicates that the total number of voice-only lines decreased from 1.5m in 2017 to 1.2m in 2019. This is a decline of almost 20% over this period. While some of these voice-only customers have switched over to dual play options, the providers reported that the largest source of ceased voice-only services relates to the death of the bill payer.
- 3.4 BT continues to hold by far the majority share of customers, serving over 75% of total voice-only customers in 2019 (an increase from 69% in 2017). Post Office holds the second largest share, although its volumes have declined since 2017. Post Office, together with the other four providers, collectively hold less than 25% of voice-only customers in 2019.<sup>20</sup>
- 3.5 We also observe that, while providers continue to serve a declining legacy base of voice-only customers, and that there is some active marketing of voice-only products to new customers, this is limited in scale. These marketing efforts appear to be focused on trying to convert voice-only customers to either dual-play or triple-play packages:
- BT does not actively market fixed voice-only packages - its website only advertises voice-only packages for customers who also take a broadband service at the same time. Offers for fixed voice-only customers who only want to take a voice service without any broadband (for example, the discounted line rental) are only available through the telephone contact centre.
  - Post Office promotes its voice-only service through its website and in its branches. It has also run a range of voice-only promotions (for example, free weekend calls). However, its focus is on promoting broadband and fibre products, as well as informing existing voice-only customers about opportunities to upgrade to broadband.<sup>21</sup>
  - Virgin Media advertises its voice-only products on its website but focuses on pursuing cross-selling opportunities (with broadband and television).<sup>22</sup>

<sup>20</sup> Shares estimated from information collected from providers under our formal investigation powers

<sup>21</sup> Post Office s135 response dated 10 November 2020

<sup>22</sup> Virgin Media s135 response dated 12 November 2020

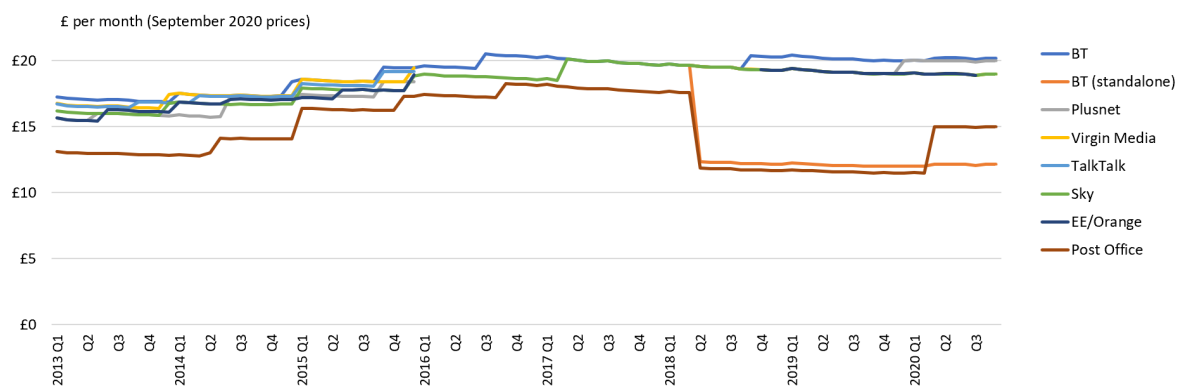
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- Sky withdrew its voice-only services to new customers in 2019 but continues to serve its legacy base of voice-only customers.<sup>23</sup>
- TalkTalk no longer sells voice-only products to new customers.

### Price trends suggest the majority of voice-only customers benefited from the implementation of the line rental price reduction and that there is little competition in the market for this group of customers

3.6 Our analysis indicates that, very shortly following the initial reduction in the line rental price by BT, Post Office introduced a similar price reduction. Given that the two largest providers reduced their line rental prices, most voice-only customers benefited from lower line rental prices from April 2018. Post Office has since increased its monthly line rental price to £15 (although this is still below the price it charged prior to April 2018).<sup>24</sup>

Figure 3: Residential monthly line rental prices<sup>25</sup>



Source: Ofcom/ Pure Pricing UK Broadband updates Note: Adjusted for CPI, excludes line rental saver pre-payment tariffs

3.7 For the other providers, we observe that a variety of voice-only products are on offer at various price points:

- OVO<sup>26</sup> and Sky offer monthly line rental packages for [£] and £18.99 respectively. However, these are not proactively marketed to new customers and Sky has stopped offering services to new voice-only customers.<sup>27</sup>
- TalkTalk stopped selling voice-only products but offers legacy products at monthly prices ranging from [£], depending on the call package and features.<sup>28</sup>
- Virgin Media offers a range of products to new customers as a voice-only offering. It also offers a Talk Protected product for eligible customers (which includes customers

<sup>23</sup> Sky s135 response dated 24 November 2020

<sup>24</sup> Free calls to Post Office numbers is included as part of the line rental deal.

<sup>25</sup> Prices are those available to new customers and are sourced from information published on the providers' websites, meaning they will exclude offers that are only available through other channels. Some providers no longer offer standalone voice-only services and do not specify a line rental price on their website.

<sup>26</sup> OVO s135 response dated 6 November 2020

<sup>27</sup> Sky s135 response dated 24 November 2020

<sup>28</sup> TalkTalk s135 response dated 12 November 2020

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aged 65 and over or with disabilities). Qualifying customers pay £17.99 per month for the line rental and receive a £5 discount on the call package.<sup>29</sup>

- 3.8 Pricing trends information suggests that only Post Office followed the price reduction for the line rental component. This is largely consistent with the limited marketing efforts described above. This suggests that, apart from Post Office, there has been limited overall effort by competitors to compete for new voice-only customers.

### **Levels of switching and engagement amongst voice-only customers continue to be low**

- 3.9 Switching for this segment of customers is very low, particularly for BT customers. As shown in Figure 4 below, the proportion of BT voice-only customers without bundled broadband that have never switched was 87% in 2019.<sup>30</sup> In comparison, only 33% of customers who purchase broadband with voice-only services from the same supplier have never switched.

**Figure 4: Switching rates for voice-only customers for 2019:**

	Voice-only and broadband with the same supplier	Voice-only without broadband bundled	BT voice-only without broadband bundled
Switched less than 3 years ago	29%	7%	2%
Switched more than 3 years ago	38%	20%	11%
Never switched	33%	73%	87%

Source: Ofcom Switching Tracker 2019

- 3.10 Switching Tracker data also indicates that consumer engagement remains low, with only 4% of respondents to the switching tracker who had a BT voice-only service saying that they were “active” or “browsers”. In contrast, 48% of all customers who purchase broadband with voice services are classified as “active” or “browsers”.<sup>31</sup> Customers who take a voice-only service are less likely to switch providers or engage with their existing provider.

<sup>29</sup> Virgin Media s135 response dated 12 November 2020

<sup>30</sup> This represents a modest increase from 2016 where the comparable figure is 84%

<sup>31</sup> Ofcom’s Engagement Index takes a selection of behavioural and attitudinal factors into account to classify consumers into different segments. “Browsers” are consumers who are currently looking, or planning to look, for a new deal, have initiated some supplier contact, and / or have conducted some competitor evaluation. “Active” consumers are those who have switched supplier in the last year (unless moving home), and / or are undertaking at least two of the following: currently or planning to look for a new deal, initiated some supplier contact, and / or have conducted some competitor evaluation.

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**Voice-only customers tend to be more dependent on their voice-only service, and to be disproportionately older, from lower socioeconomic grades, not working, and more financially vulnerable**

- 3.11 Customers who take a voice-only product are more likely to be dependent on their voice-only service than customers more generally. The Ofcom 2018 Technology Tracker data reveals that 73% of voice-only customers say that they use their voice-only service as their main service to make calls when at home.<sup>32</sup> This statistic has remained relatively consistent over the period since 2015. In contrast, only 29% of all adults say that they use their voice-only service as their main method for making and receiving calls.
- 3.12 Voice-only customers also tend to be disproportionately older, from lower socioeconomic grades, not working, and more financially vulnerable. Our 2019 Technology Tracker survey found that 49% of customers with a voice-only service and no fixed broadband are from a DE socioeconomic grade and over 40% are 75 years or older.<sup>33</sup> Of these customers, 57% are considered to be the most financially vulnerable consumers.<sup>34</sup>
- 3.13 While the overall volumes for voice-only services are declining, in the short to medium term there is still likely to be a significant volume of consumers, many of whom will be in vulnerable circumstances.

**Changes in underlying technology point to some wholesale cost uncertainty for voice-only services**

- 3.14 Over the next five to ten years, with the migration to VOIP and ensuing copper switch-off, we expect to see substantial changes to the underlying technology which supports voice-only services. These changes introduce a degree of uncertainty over the costs of providing voice-only services.
- 3.15 Wholesale Line Rental (WLR) and Metallic Path Facility (MPF) are the main products used to deliver voice-only services. The charge control on Openreach's WLR product, which is used to deliver PSTN services, was removed in 2018. Until 2021, WLR is still subject to a condition which requires Openreach's pricing to be on fair and reasonable terms.
- 3.16 Beyond 2021, we propose to completely deregulate WLR. However, Openreach has made a voluntary commitment to support the existing WLR and ISDN2/30 customer base (including

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<sup>32</sup> Ofcom Technology Tracker 2018 (note that this question was not asked in the 2019 Technology Tracker survey and therefore an updated figure is not available). Ofcom Technology Tracker 2018 data can be found at <https://www.ofcom.org.uk/research-and-data/data/statistics/stats18>.

<sup>33</sup> DE socio-economic groups, defined by NRS and maintained by the Market Research Society, include semi-skilled and unskilled manual workers, state pensioners, casual and lowest grade workers, and people who are unemployed with state benefits only

<sup>34</sup> In contrast, for all voice-only customers in general, the Technology Tracker shows that 22% are classified as DE socioeconomic grade, only 10% are 75 years or older and 26% are considered to be the most financially vulnerable consumers.



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any new circuits provided up to December 2023) on a reasonable basis until December 2025.<sup>35</sup>

- 3.17 Openreach has stated that the PSTN will be switched off by December 2025, and that it will issue a full "stop-sell" of new supply WLR from September 2023.<sup>36</sup> Ofcom has recently consulted on the conditions under which copper regulation could be withdrawn in ultrafast exchanges.<sup>37</sup> PSTN switch-off and withdrawal of copper-based services will result in consumers needing to take IP-based packages to stay connected, which are more likely to include broadband and less likely to offer a voice-only service. We note that at least one major provider does not intend to offer fixed voice-only services.
- 3.18 As we noted in our wholesale fixed telecoms market review consultation<sup>38</sup>, Openreach has introduced a low bandwidth broadband product of 0.5Mbit/s, priced in line with current WLR basic line rental, to support existing voice-only and similar low bandwidth applications within its FTTC and FTTP footprint after PSTN switch-off.<sup>39</sup> However, some providers may choose to develop products which use mobile or fixed wireless access technologies to provide voice-only services. For example, BT is considering alternative ways to serve these customers through wireless technologies.

## **We need to ensure continued price protection for customers of voice-only services**

- 3.19 Our analysis indicates that customers who take a voice-only service are disproportionately more likely to be in vulnerable circumstances and that these customers are much less likely to switch provider or engage with the market to shop around for a better deal. While the overall number of fixed voice-only customers is reducing, BT's share of customers has increased over the current commitment period, and is likely to continue to increase as some providers which have previously offered a voice-only service stop supplying the product. We expect this to result in decreased competition and choice for consumers. In this context, it is likely that prices could rise disproportionately for this group of customers. We therefore continue to believe that we need price protection for customers of voice-only services.

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<sup>35</sup> [Consultation: Promoting competition and investment in fibre networks: Wholesale Fixed Telecoms Market Review 2021-26, Volume 2: Market assessment \(January 2020\), Section 1 pp.9-10](#)

<sup>36</sup> See Openreach website: <https://www.openreach.co.uk/orpg/home/products/wlrwithdrawal/wlrwithdrawal.do>

<sup>37</sup> [Consultation: Consultation: Copper retirement – conditions under which copper regulation could be completely withdrawn in ultrafast exchanges, Supplementary consultation to the Wholesale Fixed Telecoms Market Review \(October 2020\)](#)

<sup>38</sup> [Consultation: Promoting competition and investment in fibre networks: Wholesale Fixed Telecoms Market Review 2021-26 \(January 2020\)](#)

<sup>39</sup> See Openreach website: <https://www.openreach.co.uk/orpg/home/updates/briefings/super-fastfibreaccessbriefings/super-fastfibreaccessbriefingsarticles/nga00920.do>

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- 3.20 BT has proposed a further set of voluntary commitments which we consider will provide appropriate price protection and certainty for the vast majority of voice-only customers, particularly during this period of technological change.
- 3.21 We discuss in Section 4 that we propose to accept these new commitments, which would come into force on 1 April 2021.

## 4. Proposed protections for customers of voice-only services

- 4.1 The prices which customers pay for their voice-only service have been protected since 1 April 2018. The existing voluntary commitments expire on 31 March 2021 and BT has made an offer of further voluntary commitments which we have carefully considered.
- 4.2 In this section, we explain the further commitments BT has offered and our reasons for proposing to accept these commitments. We will continue to monitor market developments and will review whether BT's proposed commitments continue to meet the needs of voice-only customers.

### Commitments offered by BT

- 4.3 The commitments BT has offered are:
- a) **Continue with a CPI+0% control on a basket of rental and call products consumed by voice-only customers.** In line with existing commitments, we consider a limit of prices increasing in real terms as a proportionate, clear and timely way to continue to protect consumers. BT has also committed to an annual CPI+0% limit on prices for its Home Phone Saver product and a safeguard cap of CPI+2.5% for its line rental product
  - b) **Commitment duration of five years.** We consider five years is an appropriate period of time for the duration of these commitments. This will provide certainty for customers for the next five years and allow us to reassess the right protections once the Public Switched Telephone Network (PSTN) switch-off has taken place, which is scheduled to be completed by December 2025
  - c) **Commitments apply to all products and services taken by voice-only customers, regardless of the technology used to deliver the service.** This will ensure that consumers are protected at the retail level, irrespective of the technology used to deliver the service. We consider this to be particularly important as consumers are migrated to different technologies as a result of PSTN switch-off
  - d) **Commitments also apply to any products or services introduced throughout the duration of the agreement.** This will ensure these commitments extend to any new service that is introduced and offered to voice-only customers during the commitment period
  - e) **BT to provide information to Ofcom on its compliance with the commitments on an annual basis.** Compliance is an important part of monitoring voluntary commitments. BT will provide Ofcom with an externally audited annual compliance statement. It will also publish an annual compliance statement on its website.

## Our assessment of the commitments offered by BT

### BT will continue with CPI+0% control on a basket of rental and call products, a commitment of a CPI+0% control on its Home Phone Saver product and a safeguard cap of 2.5% of the price of line rental

- 4.4 As a result of BT's current commitments, voice-only customers have benefited from an initial £7 price reduction in their monthly line rental and have enjoyed below inflation pricing of their fixed telephony services.
- 4.5 We believe a new commitment to cap price rises for BT's voice-only products to CPI+0%, and a safeguard cap of 2.5% of the price of line rental, will continue to ensure that voice-only customers, many of whom may be vulnerable, do not face disproportionate price increases as the market enters a period of uncertainty and change.
- 4.6 We also consider that customers who take the Home Phone Saver product, which is a voice-only service, should continue to be protected. BT has also committed to a further annual CPI+0% control on its Home Phone Saver product.
- 4.7 We have sought to illustrate the potential value to consumers from the proposed commitments.<sup>40</sup> We do this by comparing permitted prices under the new commitments to what may happen absent the new commitments (the counterfactual).<sup>41</sup> We present two scenarios for the counterfactual to provide an indicative range for customer benefits:
- **A gradual above inflation scenario.** Absent the commitments, it seems likely that BT's prices would increase in real terms. Prior to the 2017 consultation, BT's line rental charges increased by around 4% per annum in real terms.<sup>42</sup> Moreover, for its mass-market offerings (including voice-only services), BT has stated that each year it will adjust the amount customers pay by CPI plus 3.9%.<sup>43</sup> For the first counterfactual scenario, we therefore assume that prices increase by 4% per annum in real terms.
  - **A steeper above inflation scenario.** In this scenario, we assume a reversal of the line rental reduction customers have benefitted from. Line rental prices were reduced by £7/month in April 2018 and we consider it is possible that prices could eventually rise to the level preceding that reduction, absent new commitments. If this were to happen, the line rental price for voice-only customers could rise to the same level that

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<sup>40</sup> The indicative estimations cover Home Phone Saver customers as well as voice-only customers who purchase the discounted line rental.

<sup>41</sup> As a simplifying assumption, the estimations do not explicitly calculate the value for call products. However, broadly speaking, if call prices were to rise by more than inflation, line rental would not because of the CPI+0% basket cap. Conversely, if call prices rise by less than inflation, line rental could rise by more than inflation but by no more than CPI+2.5% because of the sub-cap on line rental.

<sup>42</sup> Calculated over the period 2013 to 2017, although line rental had been increasing above inflation from around 2010

<sup>43</sup> See BT website at <https://www.bt.com/help/broadband/annual-price-changes-and-cpi>

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BT currently charges to other customers (around £20).<sup>44</sup> We assume this happens over the next five years (the commitment period).<sup>45</sup>

- 4.8 We apply these counterfactual scenarios to BT's customer base over the commitment period.<sup>46</sup> On this basis, an indicative range for the estimated benefit for customers would be around £6m to £14m in the first year and benefits would increase each year of the commitment period. On average over the five year period, customer benefits in these scenarios could be between £17m to £34m on an annualised basis.<sup>47</sup>
- 4.9 The indicative range for customer benefits reflects the estimated benefits to BT's customers. In so far as the commitments act to limit how far other providers might change their own prices, customers of other providers may also benefit.

**BT has offered commitments for a duration of five years**

- 4.10 We will review these commitments in five years' time, by March 2026. This duration will provide voice-only customers price certainty for the next five years, but it will also allow us to reassess the right protections going forward as we get closer to PSTN switch-off. At this point, there will be more clarity over technology, on-going wholesale costs and the providers that continue to serve these customers.

**The commitments will be technology neutral and apply to any products or services introduced throughout the duration of the agreement**

- 4.11 BT has offered for the commitments to be technology neutral and apply to any existing or new voice-service taken by voice-only customers, regardless of the underlying technology used to deliver that service.
- 4.12 In Section 3, we explained the likely wholesale cost uncertainty as the industry moves from WLR and copper-based products. The retirement of legacy products and migration of consumers to new products might introduce further price complexity for providers. Price protection at the retail level for voice-only customers will be particularly important as providers migrate customers to different technologies as a result of PSTN switch-off.

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<sup>44</sup> BT currently charges its pay-as-you-go customers £20.20 a month for the line rental, whereas voice-only customers currently pay £12.14 a month.

<sup>45</sup> This increase is only applied to the customers who use the discounted line offering. For Home Phone Saver customers, who did not receive a price reduction, the assumption is that there would be a 4% per annum real increase for these customers under both counterfactuals.

<sup>46</sup> This also requires assumptions to be made regarding customer numbers in future years. In both scenarios, we assume that volumes decrease by [3%] per annum for line rental customers and by [3%] for Home Phone Saver customers. These assumptions are informed by BT's own forecasts and our own judgment based on recent trends because BT's forecasts didn't cover the whole period in question or the entire customer base.

<sup>47</sup> The average is calculated on an annualised basis which recognises that a future £1 of benefit is worth less than £1 of benefit today, by applying the social discount rate of 3.5% (real). This is the Social Rate of Time Preference as specified in the HM Treasury [Green Book \(Central Government Guidance on Appraisal and Evaluation\)](#)

## **BT has offered to provide annual audited information to Ofcom on its compliance with the commitments and to publish a statement on its website**

- 4.13 The provision of regular information allows us to monitor compliance and we consider that it is an integral part of accepting this new set of voluntary commitments from BT. External review will provide further assurance but we will consider whether an external review remains appropriate and proportionate three years into the new commitment period.
- 4.14 We also welcome BT's offer to improve transparency to stakeholders on how it is meeting the terms of its commitments by publishing an annual compliance statement on its website. If we were to identify any concerns with compliance, we would consider the most appropriate course of action. Accepting these voluntary commitments would not prevent us from reviewing the market or considering regulatory intervention at a later date.

## **We propose to accept the commitments offered by BT**

- 4.15 In light of our assessment, we propose to accept the commitments offered by BT. In our view, they would be sufficient to address our concerns, whilst providing price certainty, and effective and proportionate protections for voice-only customers. Whilst the commitments would only apply to BT, its large share of the voice-only customer market means these protections will apply to the majority of voice-only customers. We also consider that the commitments represent the least burdensome regulatory intervention

Q1. Do you agree with our overall approach to accept BT's offer of further commitments to ensure on-going protection of the prices paid by voice-only customers?

# A1. Responding to this consultation

## How to respond

- A1.1 Ofcom would like to receive views and comments on the issues raised in this document, by 5pm on 21 January 2021.
- A1.2 You can download a response form from <https://www.ofcom.org.uk/consultations-and-statements/category-2/protecting-voice-only-landline-customers>. You can return this by email to the address provided in the response form.
- A1.3 If your response is a large file, or has supporting charts, tables or other data, please email it to [voiceonly2021@ofcom.org.uk](mailto:voiceonly2021@ofcom.org.uk), as an attachment in Microsoft Word format, together with the [cover sheet](#). This email address is for this consultation only, and will not be valid after 21 January 2021.
- A1.4 Responses may alternatively be posted to the address below, marked with the title of the consultation:
- Retail Voice-only Customers Consultation Team c/o Cat Kelly  
Ofcom  
Riverside House  
2A Southwark Bridge Road  
London SE1 9HA
- A1.5 We welcome responses in formats other than print, for example an audio recording or a British Sign Language video. To respond in BSL:
- Send us a recording of you signing your response. This should be no longer than 5 minutes. Suitable file formats are DVDs, wmv or QuickTime files. Or
  - Upload a video of you signing your response directly to YouTube (or another hosting site) and send us the link.
- A1.6 We will publish a transcript of any audio or video responses we receive (unless your response is confidential).
- A1.7 We do not need a paper copy of your response as well as an electronic version. We will acknowledge receipt if your response is submitted via the online web form, but not otherwise.
- A1.8 You do not have to answer all the questions in the consultation if you do not have a view; a short response on just one point is fine. We also welcome joint responses.
- A1.9 It would be helpful if your response could include direct answers to the questions asked in the consultation document. The questions are listed at Annex 4. It would also help if you could explain why you hold your views, and what you think the effect of Ofcom's proposals would be.

## Protecting voice-only landline customers

- A1.10 If you want to discuss the issues and questions raised in this consultation, please contact [voiceonly2021@ofcom.org.uk](mailto:voiceonly2021@ofcom.org.uk).

## Confidentiality

- A1.11 Consultations are more effective if we publish the responses before the consultation period closes. In particular, this can help people and organisations with limited resources or familiarity with the issues to respond in a more informed way. So, in the interests of transparency and good regulatory practice, and because we believe it is important that everyone who is interested in an issue can see other respondents' views, we usually publish all responses on [the Ofcom website](#) as soon as we receive them.
- A1.12 If you think your response should be kept confidential, please specify which part(s) this applies to, and explain why. Please send any confidential sections as a separate annex. If you want your name, address, other contact details or job title to remain confidential, please provide them only in the cover sheet, so that we don't have to edit your response.
- A1.13 If someone asks us to keep part or all of a response confidential, we will treat this request seriously and try to respect it. But sometimes we will need to publish all responses, including those that are marked as confidential, in order to meet legal obligations.
- A1.14 Please also note that copyright and all other intellectual property in responses will be assumed to be licensed to Ofcom to use. Ofcom's intellectual property rights are explained further in our [Terms of Use](#).

## Next steps

- A1.15 Following this consultation period, Ofcom plans to publish a statement in March 2021.
- A1.16 If you wish, you can [register to receive mail updates](#) alerting you to new Ofcom publications.



## Ofcom's consultation processes

- A1.17 Ofcom aims to make responding to a consultation as easy as possible. For more information, please see our consultation principles in Annex 3.
- A1.18 If you have any comments or suggestions on how we manage our consultations, please email us at [consult@ofcom.org.uk](mailto:consult@ofcom.org.uk). We particularly welcome ideas on how Ofcom could more effectively seek the views of groups or individuals, such as small businesses and residential consumers, who are less likely to give their opinions through a formal consultation.
- A1.19 If you would like to discuss these issues, or Ofcom's consultation processes more generally, please contact the corporation secretary:

Corporation Secretary  
Ofcom  
Riverside House  
2a Southwark Bridge Road  
London SE1 9HA  
Email: [corporationsecretary@ofcom.org.uk](mailto:corporationsecretary@ofcom.org.uk)

## A2. Ofcom's consultation principles

### Ofcom has seven principles that it follows for every public written consultation:

#### Before the consultation

- A2.1 Wherever possible, we will hold informal talks with people and organisations before announcing a big consultation, to find out whether we are thinking along the right lines. If we do not have enough time to do this, we will hold an open meeting to explain our proposals, shortly after announcing the consultation.

#### During the consultation

- A2.2 We will be clear about whom we are consulting, why, on what questions and for how long.
- A2.3 We will make the consultation document as short and simple as possible, with a summary of no more than two pages. We will try to make it as easy as possible for people to give us a written response. If the consultation is complicated, we may provide a short Plain English / Cymraeg Clir guide, to help smaller organisations or individuals who would not otherwise be able to spare the time to share their views.
- A2.4 We will consult for up to ten weeks, depending on the potential impact of our proposals.
- A2.5 A person within Ofcom will be in charge of making sure we follow our own guidelines and aim to reach the largest possible number of people and organisations who may be interested in the outcome of our decisions. Ofcom's Consultation Champion is the main person to contact if you have views on the way we run our consultations.
- A2.6 If we are not able to follow any of these seven principles, we will explain why.

#### After the consultation

- A2.7 We think it is important that everyone who is interested in an issue can see other people's views, so we usually publish all the responses on our website as soon as we receive them. After the consultation we will make our decisions and publish a statement explaining what we are going to do, and why, showing how respondents' views helped to shape these decisions.

Protecting voice-only landline customers

## A3. Consultation coversheet

### BASIC DETAILS

Consultation title:

To (Ofcom contact):

Name of respondent:

Representing (self or organisation/s):

Address (if not received by email):

### CONFIDENTIALITY

Please tick below what part of your response you consider is confidential, giving your reasons why

Nothing

Name/contact details/job title

Whole response

Organisation

Part of the response

If there is no separate annex, which parts? \_\_\_\_\_

If you want part of your response, your name or your organisation not to be published, can Ofcom still publish a reference to the contents of your response (including, for any confidential parts, a general summary that does not disclose the specific information or enable you to be identified)?

### DECLARATION

I confirm that the correspondence supplied with this cover sheet is a formal consultation response that Ofcom can publish. However, in supplying this response, I understand that Ofcom may need to publish all responses, including those which are marked as confidential, in order to meet legal obligations. If I have sent my response by email, Ofcom can disregard any standard e-mail text about not disclosing email contents and attachments.

Ofcom seeks to publish responses on receipt. If your response is non-confidential (in whole or in part), and you would prefer us to publish your response only once the consultation has ended, please tick here.

Name

Signed (if hard copy)

## A4. Consultation questions

A4.1 Ofcom proposes to accept voluntary commitments offered by BT to protect fixed voice-only customers.

Q1. Do you agree with our overall approach to accept BT's offer of further commitments to ensure on-going protection of the prices paid by voice-only customers?

## A5. Commitments offered by BT

A5.1 Full details of the commitments that BT has offered are set out at [Annex 5](#)



Cristina Luna-Esteban  
Ofcom  
Riverside House  
2a Southwark Bridge Road  
London SE1 9HA

7 December 2020

By email only

Dear Cristina

**Standalone landline customers: BT's ongoing Commitments**

Following recent discussions between BT and Ofcom, the attached document sets out the details of BT's voluntary commitment to cap future price increases for voice-only customers' basket of services (line rental and calls) at CPI, for a period of five years from when the current Commitments expire in March 2021.

BT is committed to assisting voice-only customers in relation to both fair pricing and digital inclusion. We will continue to work with Ofcom on measures to improve our customers' engagement with the market.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Dee Cheek', with a horizontal line underneath.

Dee Cheek

**Principal, Regulatory Affairs**

**BT Group**

Annex: Standalone fixed voice: BT's voluntary commitments**WHEREAS:**

(A) BT voluntarily provides to Ofcom the commitments set out below; in particular, the commitment not to increase prices for its voice-only customers above the basket cap of CPI+0%.

(B) These commitments relate to residential line rental and calls products provided under the BT brand (they do not apply to EE, Plusnet, nor to BT's business products and/or services).

**NOW THEREFORE:****1. General Provisions**

1.1 BT plc gives Ofcom the commitments below (BT's Commitments).

1.2 The Annex to these Commitments shall form part of these Commitments.

1.3 These Commitments shall apply in respect of the whole of the United Kingdom, for a period of five years from 1 April 2021.

**2. BT's Price Commitments:**

2.1 As agreed with Ofcom, BT will:

2.1.1 Apply on 1 April 2021, a CPI + 0% basket cap to line rental and calls products for voice-only customers, as well as a separate CPI+0% cap on the price of the Home Phone Saver product;

2.1.2 Apply on 1 April 2021 an additional "safeguard" cap of CPI + 2.5% to the price of line rental for voice-only customers;

2.1.3 For these purposes, use the change in the CPI in the 12 months ending in the December prior to each Commitment year, expressed as a percentage;

2.1.4 Apply the Commitments to all line rental products and services for voice-only customers, including Home Phone Saver, regardless of the technology used to deliver the service, for a 5-year period from 1 April 2021; with the initial price of any products based on new technology being the same as that for existing line rental products at the time;

2.1.5 Employ the use of a simple compliance model in order to demonstrate that customer charges have adhered to these Commitments.

**3. BT's reporting Commitments**

3.1 BT will complete and provide to Ofcom a compliance statement (compliance summary, compliance detail) annually, within four months of the end of BT's financial year. These will be published alongside other regulatory financial compliance statements on BT's website.

3.2 BT will work with Ofcom and KPMG, or other external auditor, in accordance with an agreed audit procedure.

3.3 The requirement for an external audit is to be reviewed by Ofcom and BT after the first three years to consider whether it is still a necessary and proportionate requirement.

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**ANNEX 11**

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# Fixed Narrowband Retail Services Markets

Identification of markets and  
determination of market power

Statement

Publication date: 15 September 2009

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## Section 1

# Summary

## Introduction

- 1.1 On 19 March 2009, we published a consultation document setting out the initial findings of our review of the state of competition in the retail narrowband telephony markets, which cover analogue and digital (ISDN) telephone lines, and calls for consumers<sup>1</sup> and businesses (the “March Consultation”).<sup>2</sup>
- 1.2 We have now completed our review. Our conclusions are that most of the UK retail markets, with the exception of Hull, are now effectively competitive and, specifically, BT no longer has significant market power (“SMP”) in the provision of retail fixed narrowband analogue access and retail calls markets in either the residential or business sectors. While we consider that BT still has SMP in the retail ISDN2 market, we consider that it is appropriate to rely solely on wholesale remedies in this market as the existing retail remedies no longer offer additional benefits to the downstream competitive process. We have decided that we need to undertake a further review of the ISDN30 market before we conclude on whether or not this remains an appropriately defined market and, if so, whether it is effectively competitive.
- 1.3 These decisions represent the next stage in a process of deregulation at the retail level, which has been supported by changes to the regulation of BT’s wholesale services. In 2006, we lifted retail price controls, given the improvement in competition in the market.
- 1.4 We consider that this deregulation will lead to a further increase in competition in these retail markets. BT will be able to more freely compete in the supply of bundles of services which include fixed telephony together with other telecommunications service such as mobile communications, broadband and television. This should ensure that competition will continue to lead to enhancement in services and greater value for money for consumers.
- 1.5 Our decisions do not, however, affect BT’s continued universal service obligations under the Universal Service Order (“USO”) to provide basic telephony services (including access) . Equally, Ofcom will continue to regulate the retail activities of BT, on an equal basis with other Communications Providers, through other sector regulations<sup>3</sup>. We will continue to monitor consumers’ experience of these services and will intervene, if appropriate.

## Background

- 1.6 When we last reviewed these market in 2003<sup>4</sup>, we found that BT had SMP in almost all the fixed narrowband markets in the UK (excluding Hull)), while Kingston Communications had SMP in all the fixed narrowband retail services markets in the Hull area<sup>5</sup>. We decided that SMP remedies were essential to ensure that BT and Kingston could not use their SMP to the disadvantage of other Communications Providers,

<sup>1</sup> Throughout the document we will normally use consumers to refer to residential consumers

<sup>2</sup> [http://www.ofcom.org.uk/consult/condocs/retail\\_markets/fnrsm\\_condoc.pdf](http://www.ofcom.org.uk/consult/condocs/retail_markets/fnrsm_condoc.pdf)

<sup>3</sup> Communications Act general conditions and general consumer protection legislation / regulations,

<sup>4</sup> Fixed Narrowband Retail Services Market

([http://www.ofcom.org.uk/static/archive/oftel/publications/eu\\_directives/2003/fix\\_narrow\\_retail0803.pdf](http://www.ofcom.org.uk/static/archive/oftel/publications/eu_directives/2003/fix_narrow_retail0803.pdf))

<sup>5</sup> The exception was BT was not found to have SMP for international business calls

consumers or both. As a result, we set retail controls for BT and Kingston (now KCOM)<sup>6</sup>.

- 1.7 Since the 2003 review, Ofcom has instigated a number of measures to enhance competition in the retail markets. The aim has been to encourage real competition for the benefit of consumers and businesses; and a reduction in BT and KCOM's market power in retail and wholesale services. This has included:
- the development of a set of appropriately priced wholesale narrowband services;
  - agreement with BT of a set of Undertakings<sup>7</sup> which included the creation of Openreach (the functional separate organisation within BT providing wholesale access services); and
  - the development of equivalence of inputs for the wholesales services for both BT and other Communications Providers, supporting the delivery of services to households and businesses.
- 1.8 As a result of these developments and the improved state of competition they supported, we decided to remove the retail price controls on BT in 2006<sup>8</sup>. The following year, we relaxed retail access remedies for businesses with telecoms spend over £1M pa on the basis other Communications Providers could compete with BT on an equal footing using wholesale line rental ("WLR").<sup>9</sup>

### **Lack of SMP for BT in the retail analogue access and calls markets**

- 1.9 Several of BT's competitors argued against our proposals. In summary, they argued BT continued to have SMP for the following reasons:
- BT maintains high market shares in these markets;
  - BT's competitors face continued barriers to entry and growth;
  - BT's profitability suggests continued significant market power;
  - switching activity has slowed;
  - BT has introduced new automatic roll-over contract terms for their residential customers that could inhibit consumer switching<sup>10</sup> going forward; and
  - potential changes to migration processes currently being discussed could inhibit switching.
- 1.10 We are fully aware of the importance of these matters. Our proposals in the March Consultation took them into account and we have closely looked at them again in light of the responses received. However, we still consider that the empirical evidence demonstrates that ease of competitive entry, lack of barriers to growth, access to wholesale services and customer awareness of choice has substantially changed the nature of retail competition in these markets in the last few years.
- 1.11 Our overall analysis of the economic characteristics of these retail markets is therefore that BT no longer has SMP in any of them. Accordingly, we have concluded that these

<sup>6</sup> Kingston Communications is now operating as KCOM Ltd, though trades in Hull as Kingston Communications.

<sup>7</sup> Strategic Review of Telecommunications ([http://www.ofcom.org.uk/consult/condocs/statement\\_tsr/](http://www.ofcom.org.uk/consult/condocs/statement_tsr/))

<sup>8</sup> Retail Price Control (<http://www.ofcom.org.uk/consult/condocs/retail/prc.pdf>)

<sup>9</sup> Wholesale line rental ("WLR") is a regulated wholesale service provided by BT which allows other communications providers to offer telephone line access.

<sup>10</sup> BT have had automatic roll-over contracts for businesses for some time.

markets are effectively competitive already at this stage. In carrying out our regulatory task for these market analyses prospectively, we also consider that on a forward looking basis BT's position in these markets will be further affected by the increased competition that we anticipate will take place, with the result of its market power continuing to decline to a material degree.

- 1.12 We are required under the EU regulatory framework to carry out regulatory tasks, such as market analysis, to achieve the policy objectives set out in Article 8 of the Framework Directive, such as to promote competition. We note that, in addition to an overall assessment of the above-mentioned factors (economically, factually and legally), there is evidence that continued regulation provides little benefit to consumers and may now be constraining competition. BT's competitors may have so far benefited from apparent restrictions in BT's ability to compete in retail markets.
- 1.13 For residential customers these restrictions have stopped BT from being able to freely price product bundles which include both SMP and non SMP services.
- 1.14 For business customers, these restrictions did not allow the development of tailored service packages.
- 1.15 With most<sup>11</sup> of these restrictions now removed, competition for customers should intensify.

### Competition in Hull

- 1.16 We have concluded that KCOM still has SMP in all the narrowband retail markets in Hull. However, we consider that there are grounds for future further review of the application of the remedies we have imposed on KCOM, for both the residential and business markets.
- 1.17 With respect to the residential markets we are concerned that, in the absence of competition, residents of Hull will not have access to emerging trends in bundled services, allowing both savings through the purchase of multiple products and future innovation in service offerings.
- 1.18 We propose to discuss with KCOM options for the development of new bundled services, subject to controls commensurate with the SMP KCOM continues to hold.
- 1.19 With respect to the business markets, we accept that there is some evidence that the access of larger businesses to narrowband services provided through leased lines may mean that KCOM has market power in this segment of the market has reduced. We propose to undertake further examination of this market segment to determine whether it is appropriate to modify or suspend the application of some of KCOM SMP conditions for a sub-group of their business customers.

### Impact assessment

- 1.20 We have undertaken impact and equality assessments in our review, the results of which we set out in the March Consultation. In light of our market power determinations that BT no longer has SMP in most retail markets, we have no option but to withdraw all regulatory SMP obligations applying to BT in those markets. As pointed out in the March Consultation, there should be a net benefit to consumers as a result of the changes we

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<sup>11</sup> BT will still be subject to universal service obligations and some of the wholesale provision by necessity impact on the retail environment.

are implementing. The only significant risk identified is that BT will discriminate against its less active customers. However, we consider BT would find it difficult to substantially exploit this customer group as such customers are not confined to one specific social, economic or demographic grouping.

- 1.21 Also, changes to BT's SMP status and to the SMP remedies in these markets have no impact on BT's universal service obligations, which ensure universal access and the protection of vulnerable consumers.<sup>12</sup>
- 1.22 As regards to BT's SMP in the retail ISDN2 market and KCOM's SMP in its retail markets, we refer to our impact assessment set out in the March Consultation and updated section 7 of this Statement that takes into account the relevant consultation responses.

### Summary of conclusions

- 1.23 We conclude that BT (in the UK (excluding Hull)) no longer has SMP in the supply of:
- retail fixed narrowband analogue telephone lines for businesses and consumers;
  - retail fixed narrowband calls for business and consumers.
- 1.24 We have concluded that BT still has SMP in the supply of ISDN2 lines. However, we consider that the current retail remedies are no longer effective and are potentially counterproductive to the development of downstream competition. We have concluded, therefore, that it is appropriate to rely solely on the wholesale remedies for this market.
- 1.25 We have reviewed the retail markets in Hull and concluded that KCOM retains SMP in all retail narrowband markets and that the existing retail remedies should be retained, that is:
- No undue discrimination in the pricing and provision of services;
  - Price publication for all services.
- 1.26 However, the application of these remedies in Hull may be subject to further review.
- 1.27 We have not included our final determination on the ISDN30 market within this statement as we are still reviewing evidence provided on market definition and the competition for both the retail and wholesale markets. We will be consulting further on both the ISDN30 retail and wholesale markets later this year.

### Structure of this document

- 1.28 This Statement should be read in conjunction with the March Consultation for the full reasoning of Ofcom's final decisions on the market definitions, market power determinations and the setting of SMP conditions. This is because our conclusions in this Statement are drawn from the analysis and reasons given in the March Consultation and the further consideration we have afforded to each issue after carefully considering each and every response we received to our consultation. This Statement does not therefore repeat all our reasoning, together with related evidence, data and other

---

<sup>12</sup> We will shortly reviewing of the current USO. We intend to consider whether changes to it are required. We will include an assessment of the extent to which the USO results in a significant net burden upon BT and KCOM, the universal service providers, and the case for alternative funding and procurement models to ensure that USO provision is both effective and proportionate.

information, but instead focuses on issues arising following the consultation and, where appropriate, it presents updated (or revised) data.

1.29 The rest of the document is structured as follows:

- Section 2 explains the purpose of this market review and its relationship with the related wholesale review and other projects; it also introduces the regulatory framework for undertaking this review;
- Section 3 discusses the market and regulatory developments;
- Section 4 sets out our conclusions on the definition of the relevant markets;
- Section 5 sets out our conclusions on the market power analysis for access markets;
- Section 6 sets out our conclusions on the market power analysis for calls markets;
- Section 7 sets out our conclusions and comments on regulatory remedies and the impact assessment raised by stakeholders in their consultation responses; and
- Section 8 summarises our conclusions on market definitions, market power determinations and remedies in light of our duties and the legal tests.

## Section 2

# Purpose of the review

## Introduction

- 2.1 This review forms part of another round of market reviews to consider the state of competition in narrowband retail markets. The objective of this review has been to:
- define and analyse competition in the retail narrowband markets;
  - assess whether any individual company or, if appropriate, set of companies, hold SMP in any of those markets; and if SMP is found
  - determine what *ex ante* remedies are appropriate to address the market power, enhance competition in the markets and protect consumers from the exploitation of market power.
- 2.2 In particular, this review has reconsidered the set of retail markets defined in the first round of market reviews in 2003 and the impact of changes to the remedies that have been imposed on BT and KCOM since that review.
- 2.3 We were required to undertake this market review as part of our commitment to a regular programme of such reviews. However, several other factors supported undertaking the review at this time:
- changes to the EC recommendations have removed the retail fixed calls market from the list of markets suitable for *ex ante* regulation, calling into question our continued determination in this market. (However, we are required by the Communication Communications Act 2003 (“the Communications Act”) to re-review any market in which we have previously found SMP.);
  - changes to wholesale regulations undertaken in response to the Telecommunications Strategic Review (“TSR”);
  - indications of increased retail competition to fixed networks from mobile networks; and
  - changes to the nature of competition between fixed providers: e.g., a large number of new market entrants some of which are competing on the basis of new sales strategies such as bundling fixed narrowband services with other products and services.

## Relationship with the Fixed Narrowband Wholesale Service Market Review and other Related Projects

- 2.4 There is a clear relationship between any analysis of retail markets and the corresponding wholesale markets. Wholesale markets are defined in terms of the retail markets. However, of equal importance is the fact that forward looking analysis of competition in retail markets depends on assumptions regarding the wholesale remedies available to support competition at the retail level.



## Fixed Narrowband Retail Services Market Review

- 2.5 In recognition of this relationship, we have simultaneously undertaken reviews of the state of competition in the fixed narrowband retail and wholesale services markets. In forming our proposals and conclusions, each review was informed by the proposals and conclusions of the other. In the case of this retail review, we assumed that the wholesale recommendations, ensuring the continued provision of appropriate wholesale access and call origination remedies, are in place. The review also assumed all other existing regulations from other related markets (for example, the Wholesale Local Access market review and the associated local loop unbundling (“LLU”) remedies) remain in place.
- 2.6 The Fixed Narrowband Wholesale Services Market Review considered:
- wholesale narrowband access;
  - call origination and termination; and
  - conveyance and transit markets.
- 2.7 Other related projects include:
- The Network Charge Control: This considers the charge control remedies - for network conveyance and transit, call origination, and call termination – imposed by the Fixed Narrowband Wholesale Services Market Review. We are publishing our conclusions on this review simultaneously with this Statement.
  - Wholesale Line Rental (“WLR”) Charge Control: This considers the charge controls for WLR and related services and its conclusion is expected to be published in the near future.

### The Regulatory Framework

- 2.8 The regulatory framework that applies to the issues covered in this document is set out in detail in the March Consultation. However, in summary, the framework is based upon five EU Communication Directives, four of which were implemented into UK law by the Communications Act.
- 2.9 The Communications Act sets out, at section 3, general duties of Ofcom where we must, in carrying our functions, further the interests of citizens in relation to communications matters and the interests of consumers in relevant markets, where appropriate by promoting competition.
- 2.10 Section 4 of the Communications Act sets out duties of Ofcom for the purpose of fulfilling Community obligations.
- 2.11 Sections 3 and 4 apply across our decision making in this document as we carry out the function of undertaking a market review.
- 2.12 The framework, as implemented by the Communications Act, sets out the procedure to be followed when undertaking market reviews. In particular section 84 of the Communications Act requires us to carry out further analyses of identified markets at appropriate intervals. For reasons summarised at paragraph 2.3 above, we have considered it appropriate to conduct a review of narrowband retail services at this time.
- 2.13 A market review normally has three stages:
- market definition, i.e. the definition of relevant markets;

- market analysis, i.e. the assessment of competition in each market; in particular whether any undertaking has SMP in a given market; and
- remedies, i.e. the assessment of appropriate regulatory obligations where there has been a finding of SMP.

### *Market Definition*

- 2.14 The legal process set out in the legislation on the market definition stage is considered in detail in Annex 7 to the March Consultation. In considering market definitions, we have had regard to the Commission's 2007 review and revision of its Recommendation on relevant product and service markets (the "Recommendation"). The Recommendation identifies markets that may be susceptible to ex ante regulation. In the last review of the Recommendation in 2007, the Commission identified only one market at the retail level as being susceptible to ex ante regulation: access to the public telephone network at a fixed location. Although the Commission has identified that single retail market in its Recommendation, this does not mean that NRAs are not in a position, after analysis of relevant markets, to impose regulatory remedies on those markets where SMP has been found should national circumstances justify it. Equally, if on analysis of the identified market in the Recommendation, an NRA finds that the market is competitive, based upon national circumstances, it would not be appropriate to impose regulatory remedies.
- 2.15 The Recommendation was discussed in Annex 7 to our March Consultation and, in particular, the use of the "three criteria test" is considered. Where a market outside of the list identified by the Commission is considered by an NRA, the Recommendation states that the three criteria test should be applied cumulatively to determine if the market is susceptible to ex ante regulation. The three criteria are:
- Barriers to entry and the development of competition;
  - Dynamic aspects - no tendency toward competition; and
  - Relative efficiency of competition law and complementary *ex ante* regulation.
- 2.16 We have taken the Recommendation into account when identifying markets in this review.

### *Market Analysis: the criteria for assessing SMP*

- 2.17 The legal process set out in the legislation on the market analysis stage was considered in detail in Annex 7 of the March Consultation. In considering market analysis we have taken into account both the Commission Guidelines (Guidelines for market analysis and the assessment of SMP), and guidance produced by Oftel in relation to the criteria to assess effective competition.
- 2.18 The SMP guidelines require NRAs to assess whether the competition in a market is effective (i.e. no operator is found individually or jointly dominant). This is undertaken through a forward looking evaluation of the market, determining whether the market is prospectively competitive, taking account of foreseeable developments.
- 2.19 It is stressed in the Guidelines that the existence of a dominant position cannot be established on the sole basis of market shares, and that a thorough overall analysis is required before coming to a conclusion on the existence of SMP. Non-exhaustive criteria are suggested to measure the degree of market power held by an undertaking.

## Fixed Narrowband Retail Services Market Review

- 2.20 Where a market is found to be competitive then no SMP conditions can be imposed. Section 84(4) of the Communications Act requires that any SMP condition in that market, applying to a person by reference to a market power determination made on the basis of an earlier analysis, must be revoked.

*Remedies*

- 2.21 The legal process set out in the legislation on the remedies stage was considered in detail in Annex 1 of the March Consultation.
- 2.22 Before considering remedies it is also important to consider whether competition law remedies are sufficient to address the identified problems.
- 2.23 Where remedies are proposed they have to comply with section 47(2) of the Communications Act, in that they have to be objectively justifiable, not unduly discriminatory, proportionate and transparent.
- 2.24 In addition section 91(2) requires that SMP conditions being considered at the retail level may only be imposed where conditions at the wholesale level do not allow us to fully perform our section 4 duties in the relevant market.
- 2.25 When considering appropriate remedies we have also taken account of guidance produced by the European Regulators Group (ERG) remedies; “The Common Position on Remedies”.

## Section 3

# Market and regulatory developments

## Introduction

- 3.1 This Section summarizes the developments, since 2003, in the retail and wholesale markets that underpin the analysis and conclusions set out in the later sections. In particular, we consider the impact of the Telecommunications Strategic Review, the improvement in wholesale services and equality of input (“EOI”)<sup>13</sup>, the changes to the market from bundling<sup>14</sup> and increased mobile use. This Section provides a broad introduction to these trends which will be considered in more detail in later sections.
- 3.2 We also summarise the conclusions of our review of the impact of the removal of retail price controls (“RPCs”) in 2006 which was set out in the March Consultation.

## Background – Previous reviews and strategic framework

### 2003 Market Review

- 3.3 In 2003 Oftel completed the first round of market reviews linked to the new European Commission directives. This included our reviews on fixed retail narrowband markets potentially subject to ex ante regulation<sup>15</sup>.
- 3.4 The outcome of the latter review was a series of SMP determinations for BT and KCOM, in which SMP was found for:
- Nine out of 10 identified retail calls markets (with the exception of business international calls for BT); and
  - All narrowband retail access markets (residential and business analogue markets, ISDN2 residential and business and ISDN30 business)
- 3.5 This determination in turn led to remedies which included (initially):
- The remedies of no undue discrimination and price publication on all SMP services;
  - RPCs with a proposed review in 2006; and
  - The requirement to produce regulatory account on the services covered by the RPCs.

### Telecommunications Strategic Review (“TSR”) and withdrawal of the RPCs

- 3.6 In the TSR, Ofcom set out seven principles for the regulation of telecoms markets, including that Ofcom should:
- focus regulation on the deepest levels of infrastructure where competition will be effective and sustainable;

<sup>13</sup> Equality of Input is a requirement on BT to provide certain wholesale services on an equal basis to both itself and other Communications Providers.

<sup>14</sup> We define bundling in this paper as retail telecommunications service packages which include more than one service type (e.g. narrowband, broadband, television, mobile) at a charge less than the component services would be sold individually.

<sup>15</sup> Fixed Narrowband Retail Services Market ([http://www.ofcom.org.uk/static/archive/oftel/publications/eu\\_directives/2003/fix\\_narrow\\_retail0803.pdf](http://www.ofcom.org.uk/static/archive/oftel/publications/eu_directives/2003/fix_narrow_retail0803.pdf))

## Fixed Narrowband Retail Services Market Review

- ensure equality of access at those levels; and
- as soon as competitive conditions allow, withdraw from regulation at other levels.

3.7 The subsequent Undertakings volunteered by BT led to the creation of Openreach and EOI in respect of services provided by Openreach to Communications Providers and BT's downstream businesses. These initiatives, combined with the creation of a commercially viable and fully fit for purpose WLR product by BT, fundamentally altered the basis of retail competition. As a consequence in 2006 and 2007 we reconsidered the extent of retail regulation in the residential and business markets respectively:

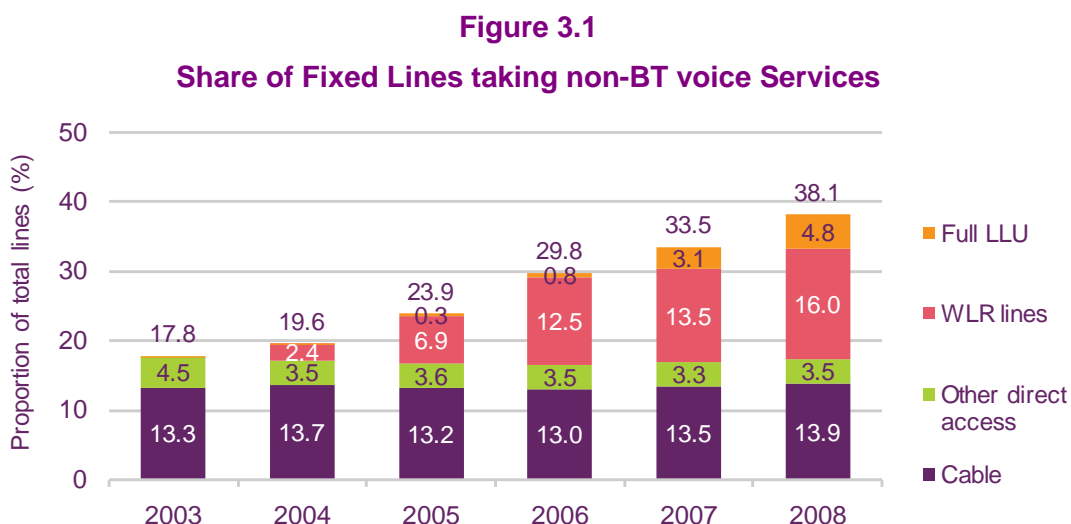
- In 2006 we undertook a review of the RPCs<sup>16</sup>. The RPCs were allowed to lapse on the basis that there was now sufficient retail competition, due to the improvement in the wholesale environment, to ensure prices were set at a competitive level. The removal was accompanied by a commitment by Ofcom to a review of the removal of controls which we undertook and set out in Annex 6 to the March Consultation.
- In 2007 following the a review of the replicability of BT's business exchange lines<sup>17</sup>, we allowed specified exceptions to SMP retail access remedies for larger businesses (telecoms spend over £1M pa) on the basis that the WLR product was fit for purpose and would allow other Communications Providers to compete fully. The stated intention in this review was that the £1M pa limit was a temporary restriction and that, if it were successful, Ofcom could extend this exemption to cover all business customers. We have had no issues raised by Communications Providers or businesses with respect to these changes. If we were not undertaking this market review at this time, it would in any event be appropriate to consider extending the exceptions to smaller businesses and to the calls market.

### Recent market developments

3.8 Since 2003 we have seen a transformation in the competitive environment – for example in the growth in competitive residential and business market retail access providers (using WLR and LLU) – with corresponding impacts on service diversity, price and BT's market share. See Figure 3.1 below.

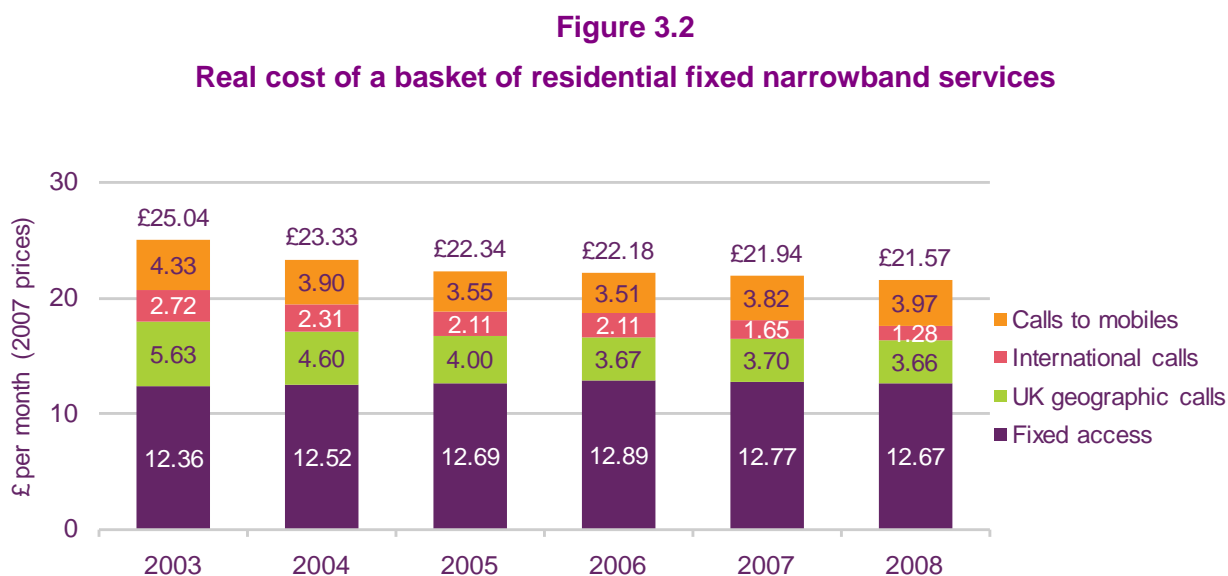
<sup>16</sup> Retail Price Controls (<http://www.ofcom.org.uk/consult/condocs/retail/prc.pdf>)

<sup>17</sup> Consent on business exchange line Replicability, 29 May 2007 (<http://www.ofcom.org.uk/consult/condocs/draftconsent/statement/consent.pdf>)



Source: The Communications Market Report 2009

- 3.9 For example, prior to 2004, Carrier Pre-selection (“CPS”) was the only real competitive narrowband option available outside the areas covered by cable. As Figure 3.1 shows there has been a massive increase in access services provided by Communications Providers other than BT, with the trend towards the provision of a complete access package (WLR + CPS<sup>18</sup> or full LLU).
- 3.10 Competition has also led to real savings for consumers. Despite the removal of the retail price controls (discussed below and in Annex 6 to the March Consultation), we have seen a steady decline in the real cost of narrowband services (see Figure 3.2) on a comparable basis.

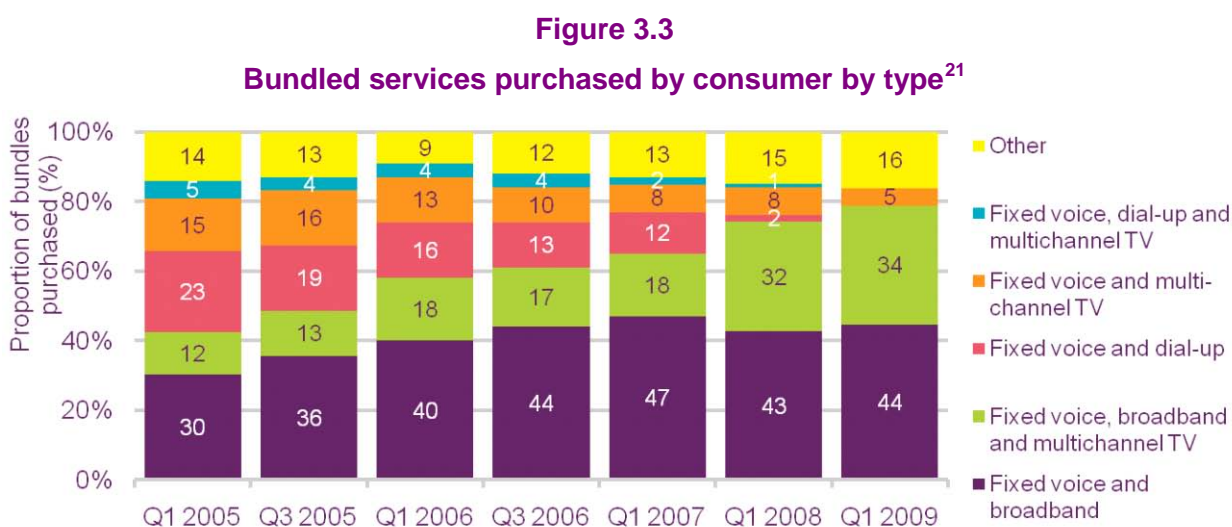


Source: The Communications Market Report 2009

<sup>18</sup> We refer to CPS as a general wholesale service for the provision of calls – in reality Communications Providers can choose between CPS or the alternative BT managed service of BT wholesale calls.

## Fixed Narrowband Retail Services Market Review

- 3.11 We have also seen a trend towards narrowband services being only one component of a bundle of communications services - including telephony, broadband and pay TV services - with both benefits in terms of convenience and often<sup>19</sup> price to consumers. Approximately 46%<sup>20</sup> of individuals now access multiple services from a single supplier, up from 29% in 2005.
- 3.12 As Figure 3.3 shows these single supplier bundles are increasingly being driven by telephony linked to multi-channel TV and/or broadband.
- 3.13 Consumers and businesses are now able to jointly purchase fixed lines and calls services together with broadband access and/or pay television (or even mobile access and calls), at reduced rates (or at times no additional cost). In addition, consumers have seen innovation in packaging of calls and access, with the benefits of predictable monthly budgets and, when chosen appropriately, real cost reductions. We discuss the impact of bundling in more detail in Section 4.



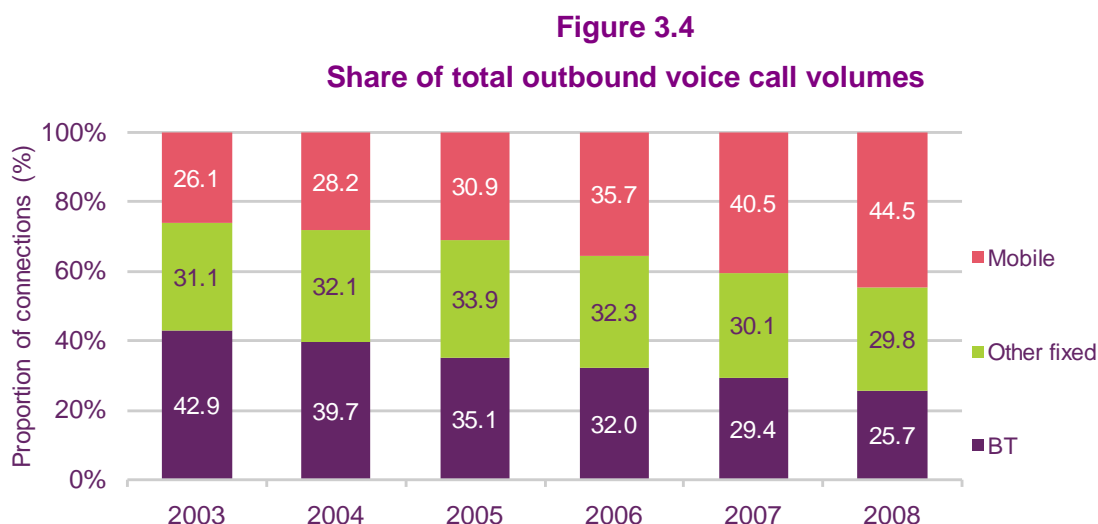
Source: Communications Market Report 2009

- 3.14 We have also seen the continued rise of mobile phone service in terms of mobile's share of call minutes (see Figure 3.4) and, equally, its share of revenue. While we do not yet consider that mobile and fixed narrowband calls are in the same retail market (see Section 4), it is clear that competition from the mobile operators has strongly influenced the nature of the fixed service packages provided.

<sup>19</sup> For the purposes of this discussion bundles refers to situations where a consumer takes two or more services from a single supplier, with or without a price discount. In later sections, we sometimes differentiate bundles which include discounts from those that do not.

<sup>20</sup> Source: Communications Market Report 2009.

<sup>21</sup> In this instance a bundled services is taken to be where a consumer takes two or more services from a single supplier, with or without a price discount.



Source: Communications Market Report 2009

- 3.15 The evidence shows that the narrowband markets have been substantially transformed since the 2003 review. As we will discuss in later Sections, we consider that this transformation has largely eroded BT's market power in the analogue access and calls markets in the UK (excluding Hull).

### Impact of removal of the RPCs

- 3.16 In 2003, following the first retail narrowband market reviews, Oftel confirmed the continuation of RPCs on BT as a remedy for the residential market<sup>22</sup>. RPCs were weighted such that compliance was judged against the expenditure basket of the bottom eight deciles (by expenditure) of residential customers. In expectation that competition in the market would strengthen, the control included an opportunity to review the remedies in 2006 to determine whether its continuation was required.
- 3.17 The 2006 review concluded that the improvements in the competitive environment for retail services (following the introduction and increased use of WLR in particular) allowed us to deregulate the controls on residential charges, and the RPC was allowed to lapse. However, the review did call for a subsequent analysis of the impact of the removal. This analysis was presented in the March Consultation.
- 3.18 At the time that they were discontinued, the RPCs effectively held average real (volume change excluded) increases in retail prices to zero (i.e. RPI+0%) for consumers in the bottom eight deciles of expenditure. The RPCs did not include the charge for payment by means other than direct debit.
- 3.19 Our analysis, as set out in Annex 6 to the March Consultation, showed that in nominal terms BT prices for the bottom eight deciles has fallen by 0.6%, if the additional charge for non-direct debit is excluded, and risen by 2.2% if the non-direct debit charge is included. This is in a period of inflation of around 4% - thus a reduction in real terms.
- 3.20 Further analysis showed that consumers in the bottom three deciles have experienced greater price reductions with a net reduction of 3.5% (nominal), if the non-direct debit charge is excluded, and an increase of 0.2% if the charge is included. This is a reduction of over 7% in real terms, excluding the non-direct debit charges, and around 3.8% if it was included.

<sup>22</sup> This was to be the last in a series of such retail price controls going back to 1984.



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- 3.21 On this basis we concluded that that regulatory change has had no negative impact on the market, and consumer outcomes and may have led to the emergence of more flexible pricing structures.

## Section 4

# Market definitions

## Introduction

- 4.1 In this Section we briefly summarise the proposals we made in the March Consultation and stakeholders' comments on our proposals. We then set out our response to those comments and our final decisions.
- 4.2 Stakeholders made a number of substantive comments about our market definition proposals. The key issues raised were:
- the degree of fixed to mobile substitution in the residential markets;
  - fixed to mobile substitution for businesses in Hull;
  - whether a UK (excluding Hull) national market was appropriate given the limits on the LLU roll out and the market conditions in Northern Ireland; and
  - whether our conclusions on the ISDN2 access markets were sound.
- 4.3 Market definition is an important intermediary step in the assessment of whether a firm has SMP. It allows us to consider the competitive constraints imposed by demand and supply-side substitutes, as well as to determine market shares.
- 4.4 As set out in the March Consultation, in defining the relevant markets we followed our standard approach which fully takes into account the relevant guidelines and recommendations published by the Commission. Under this approach relevant product and geographic markets are identified by using the “hypothetical monopolist test”. A product is considered to constitute a separate economic market if it would be profitable, for a hypothetical monopoly supplier of the product, to impose a “small but significant non-transitory increase in price” (SSNIP) above the competitive level. If a hypothetical price rise would not be profitable then the market definition should be expanded to include substitute (either demand or supply-side) products.
- 4.5 It is important to note that market definition is not an end in itself. We believe that there are risks in putting too much emphasis on an assessment of where the boundaries of the relevant economic market might lie as what matters for an assessment of SMP is not so much whether a service lies just “inside” or just “outside” a market but rather the constraint it imposes on the delivery of services within that market (for example the impact of mobile telephones on the fixed market).
- 4.6 Again as set out in the March Consultation, we have chosen to adopt a cautious approach to market definition to support a robust determination of market power. Specifically, where the evidence of substitutability is conclusive, we have amended our previous market definitions, but where the evidence is ambiguous, we retained our previous market definitions while recognising any increased competitive constraint from greater substitutability in our SMP assessment.

## Summary of defined markets

- 4.7 In the March Consultation, we defined the following fixed narrowband markets for the UK (excluding Hull):

## Fixed Narrowband Retail Services Market Review

- Residential Fixed Narrowband Analogue Access;
- Business Fixed Narrowband Analogue Access;
- Residential Fixed Narrowband Calls;
- Business Fixed Narrowband Calls; and
- ISDN2 Access.

(As noted in Section 1, we will be re-consulting on the ISDN30 market for the UK (excluding Hull), later in the year)

For Hull

4.8 In the March Consultation, we defined the following fixed narrowband markets for the Hull area:

- Residential Fixed Narrowband Analogue Access;
- Business Fixed Narrowband Analogue Access;
- Residential Fixed Narrowband Calls;
- Business Fixed Narrowband Calls;
- ISDN2 Access

(As noted in Section 1, we will be re-consulting on the ISDN30 market for the Hull Area, later in the year)

- 4.9 There are clear indications that there is a greater level of mobile competition for calls, and, in addition, bundles of telecommunications products are increasingly being considered as a single purchase. However, we consider that consumers and businesses still make purchasing choices based around the traditional fixed narrowband services.
- 4.10 Equally, while the competitive environment varies throughout the country, for example in Northern Ireland, the evidence suggests that such variations are insufficient to lead us to conclude that there are distinct regional (or sub-regional) geographic market definitions.

### **The geographic market differentiation**

- 4.11 We proposed in the March Consultation that for each individual market the only geographic differentiation was between a UK market (excluding Hull) and a separate Hull market.
- 4.12 Our view was that all major narrowband operators have national uniform pricing policies and national marketing campaigns, so competition on the supply-side of the market has a clear national dimension<sup>23</sup>. There is clearly the exception of Hull, where the incumbent provider is KCOM and the main UK based retailers, including BT, do not offer directly competing services at the retail level.
- 4.13 We explained that, while there were some differences in the range of choices available to consumers in different parts of the country (for example whether or not a consumer was able to purchase services provided over cable or from LLU based infrastructure) we considered this did not lead to a substantive difference in the quality or price of the narrowband services.

<sup>23</sup> One caveat is the TalkTalk Group which has certain tariffs which offer lower prices to customers who are able to be served within their LLU footprint.

## Consultation responses

- 4.14 One confidential respondent and the Federation of Communications Services (“FCS”) commented on BT’s market share in Northern Ireland and questioned whether it was appropriate to conclude that there was a national market.
- 4.15 FCS noted “the continuing dominance of BT in the retail market in Northern Ireland where BT’s share of, for example, the business market is still over 80%. BT marketing activity in conjunction with the lack of equivalence arising from the decision not to require the introduction of functional separation and specifically the role played by Openreach on mainland UK has led to a curtailment of choice and consequent low levels of customer satisfaction. Ofcom must ensure that this unsatisfactory situation is not compounded by further relaxation of relevant regulation.”
- 4.16 In addition, Sky questioned whether the limitations of the roll out of LLU called into question the existence of a single market.

## Ofcom’s response

### LLU

- 4.17 Communications Providers use LLU to provide either broadband services (using partial LLU, also known as Shared Metallic Path Facility (“SMPF”)) or bundled voice and broadband services (using full LLU, or Metallic Path Facility (“MPF”)). At the present time Communications Providers are using LLU in c.2,000 of BT’s c.5,600 local exchanges (c.36%). Because Communications Providers have generally elected to use LLU in the larger local exchanges, i.e. those local exchanges that serve the most premises, the circa 2,000 local exchanges where LLU is in use actually covers c.85% of UK premises (this is the LLU footprint).
- 4.18 In the Wholesale Broadband Access market review<sup>24</sup> (21 May 2008) we recognised the significant impact LLU roll out has had on broadband competition. However, we consider competition in the narrowband markets does not have the same characteristics as in the broadband markets.
- 4.19 The availability and efficacy of the WLR remedy has been the most significant driver of narrowband competition up to now. It is Communications Providers using WLR who have had the most significant impact on competition in the provision of narrowband services to date. WLR is a national remedy not limited by the technical or financial constraints that apply to LLU.
- 4.20 While we would agree that the addition of LLU and cable supports additional narrowband competition nationally, we do not agree that its absence in some geographic parts of the market means that the characteristics of narrowband competition are fundamentally altered. The characteristics of competition are national – ease of entry, awareness of competition by consumers and common wholesale products.

### Northern Ireland

- 4.21 In response to the comments we received about BT’s market share in Northern Ireland we undertook further research into the market for the provision of exchange lines by Communications Providers active in Northern Ireland from January 2008 to May 2009. This research included issuing further formal information requests to key

<sup>24</sup> Review of the wholesale access broadband markets ([www.ofcom.org.uk/consult/condocs/wbamr07/](http://www.ofcom.org.uk/consult/condocs/wbamr07/))

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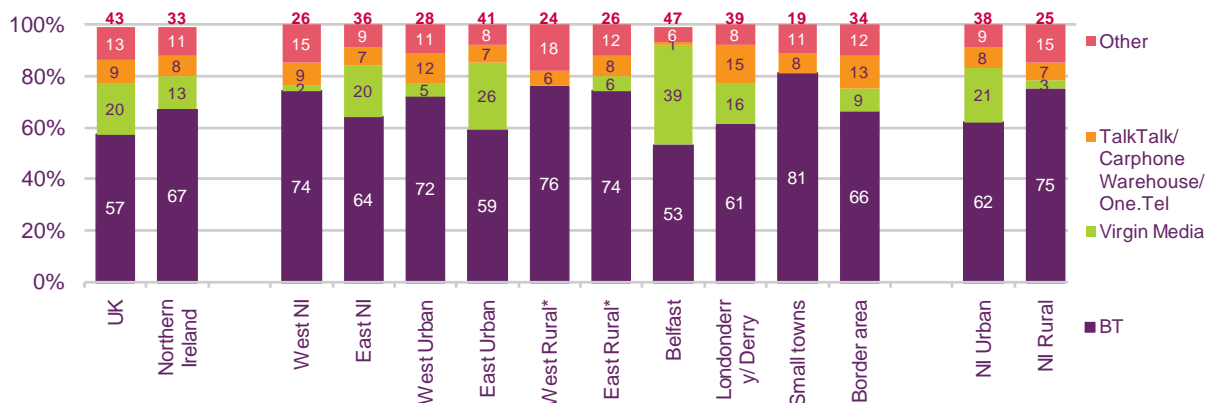
Communications Providers operating in Northern Ireland, information from Openreach on WLR provision in Northern Ireland as well as drawing on market research undertaken for the Communications Market Report 2009<sup>25</sup> (and published in that report).

- 4.22 Our research shows there is some difference between the experience in Northern Ireland and the average for the UK as a whole. This to be expected. As the UK is not perfectly uniform, if we were to examine any part of the UK in isolation it would show some differences from the average for the UK as a whole. Specifically Northern Ireland has a greater proportion of rural consumers than the UK, as a whole, and it has a lower proportion of households that can access cable.

## Residential markets

- 4.23 BT's market share in Northern Ireland is substantially higher than in the UK as a whole. In the survey reported in the 'Communication Market Report: Northern Ireland'<sup>26</sup>, 67% of those with a fixed-line phone in Northern Ireland list BT as their supplier. This is 10% higher than the national average in the same survey of 57%.
- 4.24 However, in the Communication Market Report: Northern Ireland in 2008, this proportion was 75%. We have, therefore seen an 8% decline in the last twelve months.
- 4.25 In addition, as Figure 4.1 below shows BT's market share varies significantly between urban and rural consumers (38% and 25% respectively use suppliers other than BT). This split is not inconsistent with England (44%/32%), Scotland (45%/28%) or Wales (34%/23%). For example, in Belfast only around 53% of households take their fixed line services from BT.

**Figure 4.1**  
**Fixed-line supplier used**



Source: Communications Market Report 2009 (Northern Ireland)

- 4.26 There is also clearly a lag in competing infrastructure roll-out in Northern Ireland. The proportion of homes connected to unbundled exchanges in Northern Ireland was 71% at the end of 2008, compared to the UK average of 84%. However, this was up from 51% at the end of 2007 and the rate of increase is among the highest in the UK.

<sup>25</sup> Communications Market Report 2009 ([www.ofcom.org.uk/research/cm/cmr09/](http://www.ofcom.org.uk/research/cm/cmr09/))

<sup>26</sup> Communications Market Report: Northern Ireland 2009 (<http://www.ofcom.org.uk/research/cm/cmrnr09/ni/cmrnrni.pdf>)

- 4.27 We accept that compared to the UK as a whole BT's market share in Northern Ireland is relatively high. However, over the last year the number of exchange lines provided by other Communications Providers grew by 23%<sup>27</sup> (growth from Q1 2008 to Q1 2009). The direction of change in market share indicates that other Communications Providers are actively competing against, and winning market share from, BT in Northern Ireland.
- 4.28 In addition, the basis of competition (and largely pricing) is the same as the rest of the UK. Virgin, and most other national competitors, price on a national basis as does BT.
- 4.29 Overall, residential competition in Northern Ireland may have developed at a slower rate due to geographical factors (e.g. greater proportion of the population living in rural areas) and a slightly slower rate of infrastructure roll out. However, we see limited evidence which suggests that competition is sufficiently different in structure from the rest of the UK to justify Northern Ireland being designated a separate residential market.

#### Business markets

- 4.30 Our research shows the number of business lines provided by BT in Northern Ireland has fallen, but, up to now, at a slightly lower rate than in the rest of the UK.
- 4.31 The reasons for this appear the same as for residential lines – i.e., differences in the level of urbanisation and slower roll out of infrastructure.
- 4.32 The rate of decline in BT's market share in Northern Ireland is slower than the national average. From January 2008 to May 2009, the number of business exchange lines BT provided in Northern Ireland fell by around 13,000 or 12%, while across the whole of the UK the number of exchange lines provided by BT declined by around 18%. We have information from a sample of Communications Providers who are active in Northern Ireland and the number of exchange lines they provided increased by 17% over the same period.
- 4.33 Based on information from Virgin Media and from BT on external WLR, competing Communications Providers have a market share of 26% at Q1 2009. The direction of change in market share indicates that other Communications Providers are actively competing against, and winning market share from BT in Northern Ireland. Nevertheless it is true that the intensity of competition is somewhat lower than the UK average.
- 4.34 Overall, as with the residential markets, we accept competition in Northern Ireland may have developed at a slower rate due to geographical factors (e.g. greater proportion of the population living in rural areas) and a slightly slower rate of infrastructure roll out. However, again we see only limited evidence which suggests that competition is sufficiently different in structure from the rest of the UK to justify Northern Ireland being designated a separate business market. We also note that other more rural areas of the UK might have witnessed a slower rate of growth for competing Communications Providers.
- 4.35 Given this, we consider it would be inappropriate to undertake a further detailed analysis at a local or regional level in a market characterised by national pricing and national marketing campaigns. Accordingly, with the exception of Hull, we consider that we should define a single geographic market in the UK for all the products in this market review.

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<sup>27</sup> Based on information from BT on MPF, external WLR lines and Virgin Media.

### **Fixed and mobile residential access**

- 4.36 While there was evidence that there was some substitutability between fixed and mobile access, the greater weight of evidence presented in the March Consultation suggested that consumers predominantly view the two types of access as meeting different needs and have a strong preference to purchase both fixed and mobile access.
- 4.37 We considered that demand for landlines was primarily driven by non-price factors. For example when respondents were asked about their attitudes to having a landline, 62% agreed with the statement “never give up landline – feel secure with one”<sup>28</sup>, with 44% agreeing with the statement that there is “too much upheaval to get rid of home phone”, 43% stating that “mobile is not reliable enough to drop the landline” and 26% saying that they “only have a landline for internet”.
- 4.38 Our research set out in the March Consultation showed that 78% of the UK adult population chose to have both fixed and mobile access. This has remained broadly constant since 2003 (when it was 79%).
- 4.39 We, therefore, proposed that fixed and mobile access were in separate markets.

### **Consultation responses**

- 4.40 T-mobile agreed with our conclusions with regards to the substitutability between fixed and mobile access. They noted that “It is correct that they should fall into separate markets. Whilst consumers are able to use either device to make voice calls, there are other different aspects of both services which make them very different. In our experience, consumers consider their mobile phone to fulfil different needs to their fixed phone, and vice versa. This is confirmed by the fact that the majority of people purchase both fixed and mobile access as opposed to instead swapping one for another. We do not think that the extent of fixed-mobile substitution is enough to consider them in the same economic market.”
- 4.41 On the other hand, BT noted that they considered that the growth in mobile call minutes has been largely at the expense of fixed call minutes and with “more in-depth analysis, Ofcom would also have been able to disentangle the access and calls relationship in order to be able to identify a similar pattern of substitution in the access markets.”

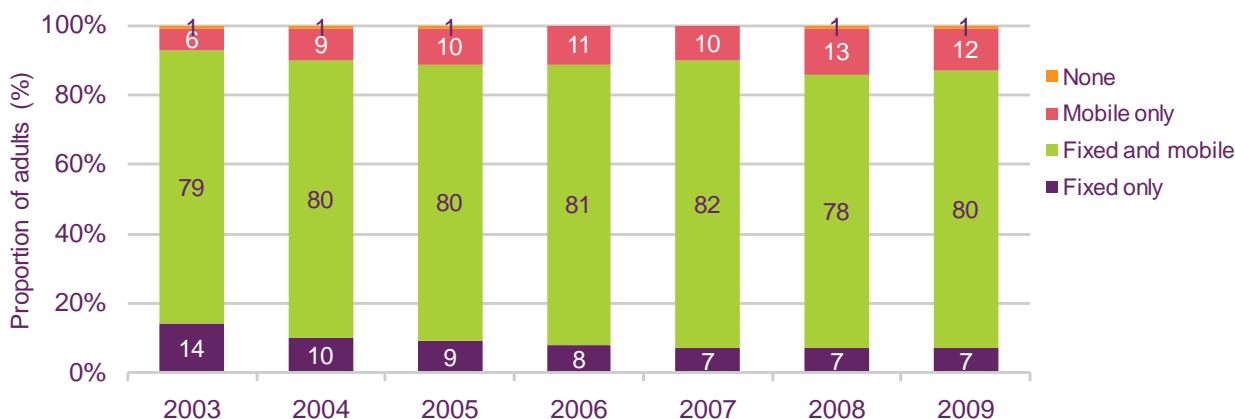
### **Ofcom’s assessment**

- 4.42 We accept, as noted above, that there has been some movement to mobile-only households and that the existence of mobiles does influence the fixed access market.
- 4.43 However, it is clear from our research that consumers currently regard mobile phone and fixed line access as complementary services rather than substitutes. The clearest indicator of this is that the vast majority of consumers buy both fixed and mobile access.
- 4.44 Further evidence that consumers have a preference to purchase both fixed and mobile access can be seen from the fact that the proportion of mobile-only users has experienced a relatively slow rate of growth over the last five years despite a very large fall in the price of mobile services. Between 2003 and 2008 the real price of mobile services declined by an estimated 47% while the price of equivalent fixed line services fell by only 14%. In the same period, mobile-only households grew from around 6% to around 12%, while the proportion of consumers having fixed and mobile access

<sup>28</sup> Ranked the statement at 4 or 5 (where 1 means “does not apply” and 5 means “applies a lot”).

remained steady at around 80%. This is consistent with consumers taking advantage of the falling absolute and relative price of mobile phones by increasingly purchasing both mobile as well as fixed access rather than substituting away from fixed lines.

**Figure 4.2**  
**Fixed and mobile access**



Source: Communications Market Report 2009

4.45 We, therefore, consider that it is appropriate to retain a definition of the residential narrowband access market which excludes mobile access.

### **Mobile and fixed calls markets**

4.46 In the March Consultation, we acknowledged that the assessment leading to the exclusion of mobile services in the markets under consideration was not clear cut. With 79% of UK consumers having both mobile and fixed line access most customers clearly have a degree of choice as to whether to make a call on their fixed line or mobile. Although there will be circumstances where consumers can either only use a mobile or landline or where they have a strong preference for using one over the other, in general mobile and fixed calls are substitutable for each other.

4.47 The situation is made more complex by the different marginal call prices faced by consumers with mobile on the basis of pay-as-you go versus monthly contracts. The latter have far lower marginal costs for calls, within their inclusive bundle, while the former pay-as-you go consumers face quite large marginal costs. In addition, our market research found there was clear differentiation in use of the mobile and fixed lines depending on the call type and the recipient.

4.48 Our assessment was that overall, while there is clear evidence of increasing competition from mobile networks for the provision of calls, on balance we did not believe that such competition is sufficiently strong to prevent a hypothetical monopoly supplier of fixed calls raising prices by 5-10%. We, therefore, proposed that fixed calls were likely to remain a relevant economic market and that the market definition should not be extended to include mobile calls. However, we recognised the growing competitive constraint from mobile calls, and took this into account in our SMP assessment.

### **Consultation responses**

4.49 Both BT and KCOM were concerned that we had underestimated the extent of fixed mobile substitution. BT pointed to evidence that the recent increase in mobile call



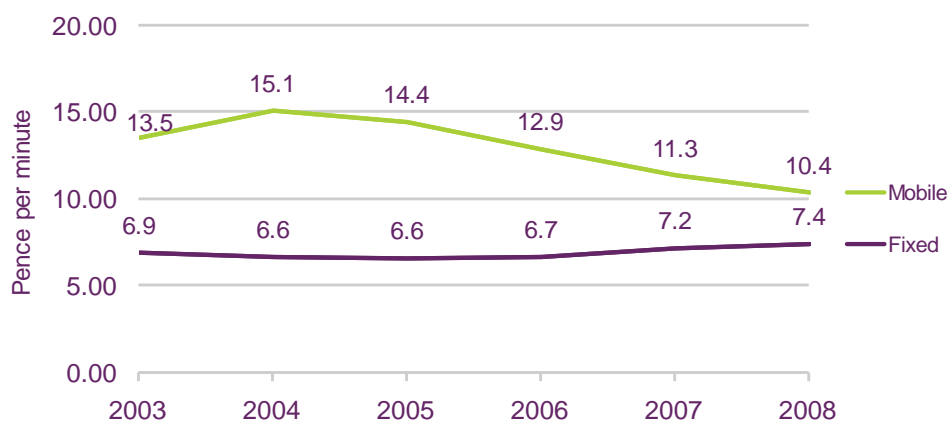
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volumes had come partially at the expense of fixed calls. While KCOM noted that they “believe that customers in the Hull area may well demonstrate a greater inclination to substitute fixed calls with mobile calls in the absence of the more extensive choice of fixed line providers available to customers outside of the Hull area. For example, during the period 2005 to 2007, KCOM experienced a 14.5% decrease in volumes of residential geographic, international direct dial and calls to mobile. By comparison annual volumes of the same residential calls for all operators reported in Ofcom’s Telecoms Market Data Tables published in Q4 2006, 2007 and 2008 decreased by only 10%. We believe this is illustrative of an increased tendency by customers in the Hull area to substitute fixed line calls with mobile calls.”

### Ofcom’s response

- 4.50 As noted above we accept that there is clear evidence of an increased level of competition from mobiles.
- 4.51 However, it is also clear from the evidence that the degree of substitution between mobile and fixed calls varies considerably depending on the nature of the mobile contract and the nature of the calls made. In addition, pay-as-you-go mobile users, who face higher marginal call costs are likely (on average) to have lower than average incomes, which must suggest caution in extending trends based on usage by those with higher incomes. In addition, average mobile call costs remain substantially higher than the average fixed line cost, although this differential is clearly decreasing, see Figure 4.3.

**Figure 4.3**  
**Comparison of mobile and fixed average nominal call costs**



Source: Communication Market Report 2009

- 4.52 Given this uncertainty we consider that it is appropriate to take a conservative view of the market boundaries. As discussed in the introduction, the purpose of market definitions is mainly to support analysis of market power. The exclusion of mobile calls from the market sets a higher hurdle, in any analysis, in establishing that that market is effectively competitive. This strengthens the robustness of our finding of no SMP for the UK (excluding Hull).
- 4.53 With respect to Hull, we also accept that in an environment of very limited competition for calls from other fixed providers, there will be greater reliance on mobile. However,

these circumstances would suggest caution in including what may be a second-best substitute as part of a wider calls market.

- 4.54 Accordingly, we consider it is appropriate to retain our proposed narrowband calls market definition, which excludes mobile calls.

### **Mobile calls and fixed line calls for business users are in different markets in Hull**

- 4.55 The March Consultation focused principally on the overall UK business market, rather than specifically at Hull, but there was no evidence to suggest that the attitude of businesses in Hull departed significantly, in this regard, from the UK as a whole. We did, however, use statistical data which was Hull specific.
- 4.56 In the March Consultation we noted that the fall in the volumes of Business fixed calls<sup>29</sup> between Q1 2003 and Q2 2008 was substantially in excess of the percentage decline in the number of business analogue exchange lines<sup>30</sup>. We considered this reflected a number of factors including increased competition from e-mail, voice over broadband, and mobile.
- 4.57 Our survey of SMEs suggested that the fixed mobile substitution element of this fall was limited. For example, of the businesses in our sample, only 68% had mobile phones, and 13% blackberries. Of the total sample, 69% agreed with the statement “we use landline services where possible because they are cheaper than mobile.” In contrast, only 14% of respondents indicated that they generally used mobile phones. Landline calls were also widely perceived to be cheaper than mobile calls apart from calls to mobile phones. For example, 70% believed that landline calls were cheapest for calls to UK landlines, and 82% for international calls.
- 4.58 With calls to mobile numbers often being perceived as being cheaper using a mobile phone, we might expect business calls to mobile to have declined at a faster rate than for calls to geographic numbers as the use of a mobile phone to call other mobile phones is cheaper than fixed to mobile calling. However, fixed calls to mobiles declined at a significantly lower rate than calls to geographic numbers. The most likely explanation for this is that, the call pattern of businesses has changed (for instance email is likely to be a better substitute for a fixed to fixed call than a fixed to mobile call). The data does not, however, provide conclusive evidence that businesses are using mobile phones in place of calling from a landline.

### **Consultation responses**

- 4.59 KCOM stated that “We are also concerned about the extent of the analysis which Ofcom has undertaken in respect of the substitution of fixed calls with mobile by business customers. Ofcom makes the comment that it does not have data of sufficient quality to determine the extent to which business have substituted to mobile while the customer research carried out by Ofcom is largely focused on very small business customers (84% of the SMEs questioned had 1-9 employees). We question how representative Ofcom’s survey sample is in terms of mobile usage by businesses – as Ofcom notes mobile penetration was found to be much higher in the larger companies surveyed with

<sup>29</sup> Geographic, international and call to mobile call types.

<sup>30</sup> Our recent revision of the statistics suggested that the 58% decline in business fixed calls quoted in the consultation should be increased to a decline of 48%, and the 3% reduction in the number of business analogue exchange lines should be reduced further to 18%. However, the reduction in the volume of calls is still substantially in excess of the decline in lines.

large companies more likely to use a mix of landline and mobile services. As a result we believe that Ofcom's research may well understate the propensity of business customers to substitute mobile calls for fixed line calls."

### Ofcom's response

- 4.60 We accept that there are some limits to the extension of our survey data based on SME behaviour to the business markets as a whole. However, while our survey focussed on the SME companies in terms of behaviour, our statistical evidence was based on the totality of business calls.
- 4.61 This statistical evidence suggested that those calls most likely to be made by using mobiles (i.e. calls to other mobiles) were not declining at the same rate as calls overall. While this is not conclusive it suggests that the decline in business call traffic is attributable to a use by businesses of a wide range of a communications tools, such as email, rather than just mobile substitution.
- 4.62 As discussed above, we consider that it is appropriate to be conservative in moving away from a more narrow market definition. For this and the above reasons we therefore believe that the balance of evidence supports the view that fixed business calls is a separate economic market.
- 4.63 However, clearly competition from mobile calls is increasing and we take this into account in our SMP assessment. We are also conscious that there are some other arguments put forward) by KCOM (discussed in the next section that for larger businesses there is an increased level of competition for calls (i.e. using leased lines). We will consider these arguments also in Section 7 in considering the remedies for our SMP findings.

### ISDN2 access

- 4.64 In the March Consultation, we reviewed demand and supply side substitution between ISDN2 and either leased lines or analogue access. We also considered ISDN30 but as noted earlier this market will be re-considered in a separate consultation.
- 4.65 We proposed that the market for ISDN2 was distinct.

### Consultation responses

- 4.66 BT stated that in their view, "ISDN is increasingly in competition with new technologies such as IP-based products. Ofcom's market definition analysis does not sufficiently take into account these forward-looking factors: a proper analysis would show that these new products (broadband and IP based solutions) are growing and are increasingly substitutable for ISDN and, at the very least, are constraining BT's supply and pricing of ISDN products."
- 4.67 BT also stated that the ISDN2 market did not satisfy the EU's three criteria test for ex ante regulation.

### Ofcom's response

- 4.68 In the assessment of ISDN2 as a separate and distinct market, we have not ignored the fact that there are some instances where these services are potentially substitutable by alternative technologies.

- 4.69 Broadband has clearly impacted on ISDN2 demand in some areas. Broadband has completely superseded ISDN2 in the residential sector and where internet access is the primary requirement broadband is replacing ISDN2 in the business sector.
- 4.70 However, and as BT has noted in its response to the Wholesale Fixed Narrowband Review, ISDN2 is used for a number of other purposes including point of sale machines, automated teller machines (ATMs) and resilient back-up for other services. Table 4.4 below shows ISDN2 volumes for the past four years, from BT's regulatory accounts:

**Table 4.4****ISDN2**<sup>31</sup>

	<b>2005/6</b>	<b>2006/7</b>	<b>2007/8</b>	<b>2008/9</b>
<b>Total channels</b>	1.515	1.459	1.428	1.299
<b>BT</b>	1.344	1.201	1.081	0.898
<b>Others</b>	0.171	0.258	0.347	0.401

*Source: BT Regulatory Accounts*

- 4.71 Table 4.4 shows a steady decline in the total number of ISDN2 lines supplied. The total number of ISDN2 channels had decreased by an average of around 4% a year from 2005/6 to 2008/9.
- 4.72 From 2005-2009, the functional differences between broadband and ISDN2 have widened (in terms of speeds available via broadband compared to the maximum 128kb/s available via ISDN2). At the same time, the retail price of broadband has fallen. BT's current retail ISDN2 price is £90.78/qtr versus analogue line plus broadband of £79.80/qtr. If broadband was an effective substitute for most customers, we would expect these trends to have resulted in a much higher rate of substitution.
- 4.73 This suggests broadband does not provide a constraint on the pricing of ISDN2 for all services for which ISDN2 has been used. The advantages of broadband over ISDN2 are likely to be irrelevant for ATMs. Indeed, the key advantage of ISDN2 is that it provides a resilient, secure and high-quality level of service. Users of ISDN2 for this reason may consider that broadband does not provide these features, and as such broadband cannot be considered to be an adequate substitute product. This is supported by a review of recent Openreach documents discussing substitution between ISDN2 and other products.
- 4.74 Another consideration for users is likely to be on-premises equipment. Changing from ISDN2 to an alternative will generally require an investment in alternative transmission equipment. This limits the scope for such alternatives to compete for existing business. So while there may be a relatively greater level of competition for new customers not currently using ISDN2, we consider that there is a large and relatively static set of customers for whom continued use of ISDN2 is the only reasonable approach until such time as their existing equipment needs to be replaced (provided that the alternatives are satisfactory).
- 4.75 We accept that the ISDN2 market is likely to decline steadily over the review period and we accept that there is likely to come a point when alternative technologies will be an effective substitute for ISDN2 for most customers. However, there is no clear evidence that this is likely to be that case for the forward look in this review and as a consequence we consider that our market definition should remain.

<sup>31</sup> Figures exclude Virgin which we estimate to be around 1% of the total market.

## Relationship between the retail market definition and the Commission's Recommendation on relevant product and services markets.

- 4.76 In Section 2 (and, in more detail, in the March Consultation), we have explained what Ofcom must do before making a market determination and that we are required to take due account of the Commission's Recommendations.
- 4.77 The Commission has in its Recommendation defined the following as a relevant market in accordance with Article 15(3) of the Framework Directive:
- Access to the public telephone network at a fixed location for residential and non-residential customers.
- 4.78 As set out above we have defined 6 separate access markets (three for UK (excluding Hull) and three for Hull), which will be narrower than and, therefore, different to the Commission's market definition.
- 4.79 We have also defined 4 separate calls markets (two for UK (excluding Hull) and two for Hull). The Commission have not included a calls market within their recommendation, indicating that this may be a market that is not susceptible to *ex ante* regulation.
- 4.80 Consequently, in determining the requirement for *ex ante* regulation due to market power, in the analysis set out below we will give careful consideration to the three criteria set out in the Explanatory Memorandum to the Recommendation (section 2.3), and discussed at paragraph 2.15 above, namely:
- barriers to entry and the development of competition ("Criterion 1")
  - dynamic aspects – no tendency towards competition ("Criterion 2")
  - relative efficiency of competition law and *ex ante* regulation ("Criterion 3")
- 4.81 As all 10 of the markets we have identified differ from the retail market identified in the Recommendation we have applied the test to each of those markets.
- 4.82 We consider that EC's criteria were addressed in the March Consultation document both in the market definitions section and in the sections that dealt with market power analysis. Whilst the latter sections primarily discussed whether an operator holds SMP for a proposed market, we are mindful that the three criteria test is different from the SMP assessment and specifically that the three criteria test focuses on the general characteristics of a market, whilst an SMP assessment is made in relation to a specific operator in a given market.
- 4.83 However, certain issues are relevant to both the three criteria test and to a consideration of market power. In the March Consultation we sought to keep such discussion in a single section of the document to avoid unnecessary repetition of argument.
- 4.84 We considered that Criterion 1 was covered with the discussion of barriers to entry and expansion. Criterion 2 was covered within the discussions of switching costs and the intensity of competition, market shares and prices and profitability. We addressed Criterion 3 where we identified competitive failure (i.e. in the ISDN2 market for the UK (excluding Hull) and all markets for Hull) within this section of the document.
- 4.85 We received some comments from stakeholders in relation to our assessment of the factors that are relevant to both the three criteria test and to the assessment of SMP, for

example, barriers to entry. Consistent with the approach that we adopted in the March Consultation document, we have addressed these issues in the sections on market power assessment (Sections 5 and 6). Where this additional analysis is relevant to the question of whether the three criteria test is met, we have reviewed our analysis.

- 4.86 In addition to the further arguments set out in Sections 5 and 6, we should note here that:
- 4.87 The nature of the ISDN2 market is such that at present there is limited scope for replacement of the ISDN2 services by alternative technology. As such the review against this criteria is limited to competition for the provision of ISDN2 itself.
- 4.88 As we will discuss in the next Section, there is some evidence of increased market entry. But there are clearly significant barriers to growth in that market as no competitor to BT holds more than 3% of the market. Entry is constrained by BT's existing market presence and a perception that there is limited benefit in substantial investment to increase market presence due to the threat that this market will diminish over time.
- 4.89 As a consequence, we consider that there is an effective barrier to significant market expansion.
- 4.90 The evidence, as set out in the March Consultation, shows that a key characteristic of this market is relatively stable prices. Even as BT has lost market share, prices have remained relatively constant.
- 4.91 The competitive focus appears to be on the next generation of services, leaving those using ISDN2 to purchase the same product for the same price.
- 4.92 The nature of the customer base, cost of ISDN2 as a proportion of business input costs and competing Communications Provider involvement in the market means that it is less likely that abuse by an incumbent would be effectively identified and addressed ex post.
- 4.93 This suggests that there is often insufficient individual harm to warrant the cost of pursuing a competition law complaint. Ex ante regulation, even if, in this case, it is confined only to the statement of SMP, would ensure that the cost of pursuing a complaint is lowered as there would be a greater presumption of incumbent dominance and we would reserve the right to directly intervene if abuse is indicated.

#### **Conclusion on application of the 3 criteria test**

- 4.94 We consider that our assessments of how the three criteria test applied to each of our defined markets, as set out in the March Consultation were correct, and we have not changed our position on market definition since the March Consultation (save to exclude ISDN30 access markets from our consideration), having regard to all of the comments received during the consultation process and our further analysis of the evidence.

## Section 5

# Access Markets - market power analysis

## Introduction

- 5.1 This Section sets out our assessment of market power for the access markets. We set out our assessment of market power for the calls markets in Section 6.
- 5.2 Where we have found a market to be effectively competitive, there is no continuing requirement for company specific regulation (see Section 8). However, Ofcom's involvement in the retail market will continue through sector-specific retail regulation, such as the General Conditions on communications providers (see Section 7).
- 5.3 Where we find SMP in a relevant market, we are obliged to consider what remedial regulations may be required to address the competitive failure. Such remedies as are required are set out in Section 7.

## Data corrections

- 5.4 Since the March Consultation, Ofcom has re-examined the market share statistics we compile for narrowband markets in the UK. We identified the need for a re-adjustment of the statistics, due to reclassification of exchange lines within the various ISDN and PSTN markets, including a number of non-BT lines which had been incorrectly classified as business rather than residential services. Additionally, we had under-counted some of the non-BT lines. We have also updated the information to take into account more recent data for Q4 2008 and Q1 2009.
- 5.5 The main impact of these changes is to slightly reduce BT's market share in residential lines and to increase BT's market share in business lines.

## Summary

- 5.6 Our conclusions with respect to market power remain unchanged from the March Consultation.
- 5.7 In summary, we have concluded that in the UK (excluding Hull):
- no company has SMP in either the residential or business fixed narrowband analogue access markets; and
  - BT has SMP in the market for ISDN2 access.
- 5.8 As discussed previously we are not considering ISDN30 markets for the UK (excluding Hull) or the Hull area at this time.
- 5.9 In the Hull area we have concluded that KCOM holds SMP in the following access markets:
- Residential fixed narrowband analogue access;
  - Business fixed narrowband analogue access; and
  - ISDN2 access.

## Our approach

5.10 Article 14 of the Framework Directive defines SMP as equivalent to the competition law concept of dominance:

*"An undertaking shall be deemed to have significant market power if, either individually or jointly with others, it 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."*

5.11 In assessing whether BT and KCOM have SMP we have taken into account the following factors both with regard to the current and recent experience, and the likely competitive picture during the forward look period covered by this market review:

- Market shares;
- Barriers to entry and expansion;
- Customer switching costs and the intensity of competition in the market;
- Prices and profitability;
- Countervailing buyer power;
- Other competitive constraints; and
- International comparisons.

5.12 As noted above, the test for SMP is essentially whether the undertaking is in a position of economic strength affording it the power to behave to an appreciable extent independently of competitors, customers and ultimately consumers. For example, a firm will have SMP where it has an ability to raise prices significantly above the competitive level. Firms are more likely to have SMP where they have a persistently high market share. However, even when market shares are relatively high, a firm may not have SMP where there are low barriers to entry and expansion or where there are other significant competitive constraints on its behaviour. A company's market share is only one of a number of relevant factors that need to be jointly assessed to determine whether that company has SMP in a particular market.

5.13 It is important to bear in mind that in overall assessments on SMP it is possible that some markets will display both features consistent with a no SMP finding and features consistent with an SMP finding. That is, by its very nature a binary SMP finding (either SMP or no SMP) summarises a much richer assessment of the competitive conditions in a particular market.

## Access markets

5.14 In this Section we consider whether any provider is likely to possess SMP in each of the fixed access markets identified in Section 4.

5.15 These markets are:

- Residential narrowband fixed analogue access (for UK (excluding Hull) and for Hull)
- Business narrowband fixed analogue access (for UK (excluding Hull) and for Hull)
- ISDN2 access (business only) (for UK (excluding Hull) and for Hull)



## **Residential Markets for fixed analogue access**

### **UK (excluding Hull)**

- 5.16 In the March Consultation, we considered that, despite BT's relatively high market share, the level of competition in the market for the provision of fixed analogue access was such that BT had no SMP for the following reasons:
- The wholesale remedies (e.g. WLR) have led to the development of products which enable competitors to replicate the services offered by BT without making significant infrastructure investments. This has lowered barriers to entry and growth.
  - New firms have entered and expanded in the market resulting in a fall in BT's market share.
  - Some of the main competitors such as Sky are expected to rely increasingly on LLU during the review period to further reduce their costs and increase the competitive pressure on BT.
  - Consumers are willing and able to switch provider (evidenced by the fall in BT's market share).
  - Since RPCs were lifted the overall average increase in the phone bill has continue to fall in real terms.
  - The overall cost of a fixed line access and calls package is comparable to similar OECD countries.
- 5.17 Eleven stakeholders responded to our SMP analysis for the residential access market in the UK (excluding Hull) with a variety of viewpoints which we consider below, these included BT, T-mobile, Scottish & Southern Energy ("SSE"), COLT, TalkTalk Group, Cable & Wireless, FCS, UK Competitive Telecommunication Association ("UKCTA"), Sky and two confidential responses.

### **Overview of consultation responses**

- 5.18 BT agreed with our SMP analysis. They also noted that the market today is subject to significant churn which is principally due to the fact that customers are aware of their ability to switch supplier and the numerous alternatives provided by CPS, LLU, WLR and mobile operators.
- 5.19 BT strongly believed that Ofcom's proposals to deregulate the narrowband market will benefit all end consumers by allowing BT to compete on a more level playing field. Residential consumers are well informed about alternatives (both fixed and mobile) and their ability to switch meaning that concern over any negative consequences of deregulation was unfounded.
- 5.20 BT agreed with Ofcom's assessment that the proposals are not detrimental to residential consumers who are uninterested in changing supplier and that in any event it would be difficult to target such consumers. BT's research that we have reviewed shows that consumers who have never left BT are by and large inactive by choice. The research additionally shows that these consumers are making an informed decision to stay with BT and that they have high levels of satisfaction and trust with BT. BT concurred that there are sufficient measures in place via BT's Universal Service Obligations and other General Conditions to protect any vulnerable consumers.
- 5.21 TalkTalk Group and UKCTA noted that Ofcom's competition policy for fixed narrowband retail markets has been successful to some degree in ensuring sustainable market entry by strong players who have been able to challenge BT's legacy dominance. The

introduction of CPS, WLR and LLU/MPF as wholesale remedies have all contributed to the gradual erosion of BT's market power in the retail markets in the last 7-8 years. However, they believe that the fixed narrowband retail markets have not yet reached a stage where they can be said to be effectively competitive since BT still holds twice the market share of all other operators taken together.

5.22 The other stakeholders disagreed with aspects of the SMP analysis. The main areas of concern related to:

- BT's market share – some stakeholders thought BT's market share was sufficiently high to indicate a presumption of SMP.
- Wholesale narrowband product range – some stakeholders commented that if more wholesale product options were offered (e.g. xMPF) then retail competition in the residential voice access market would be enhanced, and that the current set of wholesale products was constraining retail competition and giving an advantage to BT Retail.

5.23 We discuss these points and other stakeholder comments in further detail below.

### **BT's market share and related comments**

#### **Consultation responses**

5.24 A number of Communications Providers, the FCS and UKCTA commented that BT still has a relatively high market share which was indicative of SMP and expressed concern that the market was not sufficiently competitive to justify full deregulation. Several stakeholders commented that a market share in excess of 50% was evidence of a dominant position based on current case law.

5.25 COLT also commented that competition authorities such as the OFT usually use a benchmark of 40% market share at which it is unlikely that an individual undertaking will be individually dominant. COLT noted that BT's shares of lines and revenues are comfortably above that level.

5.26 COLT suggested that if the decline in BT's market share continues at the current rate it will be 2013 before BT's share falls below 50% and 2016 before it falls below the 40% threshold and both these dates are outside the expected time period for this market review. Sky, UKCTA and TalkTalk Group also commented that the evidence presented does not support the contention that BT's market share will continue to decline at a sufficient rate such that, during the forthcoming review period, the presumption of dominance can be rebutted.

5.27 Sky commented that, in order to rebut the presumption of dominance, Ofcom should be able to explain the extent to which it expects BT's market shares to decline (i.e. that they will decline to a level where BT no longer enjoys SMP). Such a decline should also not simply be by the end of the forthcoming review period. It is not sufficient for Ofcom merely to highlight a general decline in BT's market shares, based on a number of unsubstantiated prospective competitive trends: as the Commission has indicated, "the fact that an undertaking with a significant position on the market is gradually losing market share may well indicate that the market is becoming more competitive, but it does not preclude a finding of SMP".<sup>32</sup> Sky also commented that market shares are a more reliable indicator of market power in markets characterised by a high degree of product homogeneity and where market boundaries are reasonably clear. In the present

<sup>32</sup> Paragraph 75 of the EC SMP Guidelines.

case, access and calls are relatively uncontroversial as meaningful spheres in which to assess the degree of competition among firms. Accordingly such a presumption is appropriate in this case.

- 5.28 Sky think that in the present case, it is far from clear, even under the current regulatory framework that the downward trend in BT's market shares will continue. Absent SMP regulation, there is a risk that this trend will cease or even reverse.<sup>33</sup> Without sufficient supporting evidence to show that BT's market share will inevitably decline, an approach based on 'anticipation' runs counter to Ofcom's duties: rather than justify a removal of ex ante regulation, anticipated market share movements simply indicate a continuing need for Ofcom to keep the relevant markets under review.
- 5.29 In addition, COLT commented that the OFT Guidelines state that market power is more likely to exist when competitors have low market shares. Table 5.1 in the March Consultation shows that the next nearest competitor (Virgin) has an 18% share of lines and 17% share of revenues. In both cases, Virgin Media's share is less than 30% of BT's share. As explained at paragraph 5.38 of the March Consultation there are 12 significant providers using WLR, but these providers have 12% market share between them: an average of 1% per provider. COLT regard this as evidence that other operators have low market shares, further undermining Ofcom's analysis that BT has no SMP.

### Ofcom's response

5.30 We address these concerns in the following order:

- The role of market share in assessing market power;
- Trends in BT's market share; and
- The relative size and share of competitors.

#### The role of market share in assessing market power

5.31 We accept that BT has a relatively high market share. However, as explained above we consider that it does not necessarily follow that BT therefore has SMP.

5.32 As noted in paragraphs A7.44-7.45 of the March Consultation, in its guidelines on market analysis and the assessment of SMP, the Commission discusses market shares as being one indicator of market power; however, the Commission also notes that:

"It is important to stress that the existence of a dominant position cannot be established on the sole basis of large market shares. ...the existence of high market shares simply means that the operator concerned might be in a dominant position. Therefore, NRAs should undertake a thorough and overall analysis of the economic characteristics of the relevant market before coming to a conclusion as to the existence of significant market power."<sup>34</sup>

<sup>33</sup> For example, extrapolating over the next 3 years the recent rate of decline of BT's market share for access of around 3-4% per annum, BT can be expected still to have a market share of over 50%. This is also consistent with the forecasts in Table A7.1 of Ofcom's May 2009 Statement on A New Pricing Framework for Openreach, which suggests a similar market share for access for BT in 2011/12.

<sup>34</sup> See "Commission guidelines on market analysis and the assessment of significant market power under the Community regulatory framework for electronic communications networks and services", paragraph 78.

- 5.33 Furthermore, the European Court of Justice (ECJ) has stated that dominance can be presumed in the absence of evidence to the contrary if an undertaking has a market share persistently above 50%<sup>35</sup> (emphasis added).
- 5.34 In other words, the Commission clearly states high market share alone is **not** sufficient to find dominance and the ECJ states an assessment of dominance should consider market share alongside other evidence.
- 5.35 Therefore, we consider it clear that high market shares alone are not sufficient to find that an undertaking has SMP. In fact, we are obliged to take into account a number of factors, not just market share, in assessing whether an undertaking has SMP (even in a market where products are relatively homogenous). To that end, the Competition Appeal Tribunal has ruled<sup>36</sup> in a case involving a 100% market share that, as part of an overall assessment of whether there is SMP:
- “The underlying principle in a case like this is whether there is effective competition. SMP is a tool in determining this question – indeed, it is the central tool...Various factors are relevant in determining whether there is SMP, and one of those is CBP.”
  - “A large market share gives rise to a presumption of dominance...However, the nature of that “presumption” must be properly understood. Normally, in English law, a presumption can be relied on by itself if there is no other evidence which goes to the point; no-one suggested that the position would be different so far as any European principles might be in play. The first sentence of paragraph 78 of the guidelines seems at first sight to detract from that principle. However, we are not satisfied that it does. What paragraph 78 provides is that a regulator is not entitled to find a large market share, rely on that as giving rise to a presumption of dominance and stop there. The regulator is obliged to go on and consider all other such factors as are relevant to a consideration of the point in the market in question. The paragraph then goes on to identify some of them. What is required by the Guidelines is a “thorough and overall analysis of the economic characteristics of the relevant market before coming to a conclusion as to the existence of significant market power.” This approach is demonstrated by various authorities, including *Hoffman-La-Roche* [1979] ECR 461, and we do not consider that anything appearing in *Tetra Laval* contradicts or modifies it.”
- 5.36 We believe that the available evidence shows that barriers to entry and expansion in this market are low because the wholesale remedies in place (in particular WLR) mean that competitors can easily enter the market and replicate the services offered by BT with, in the case of WLR, a relatively low level of infrastructure investments (clearly this is greater for LLU providers but the motivation for LLU is not purely narrowband). This is evidenced by the wide variety of retailers who have entered and successfully expanded within the market. We believe these competitors constrain BT. Additionally, one major provider, TalkTalk Group, is competing with BT on the basis of full LLU; and a further provider, Sky, has announced its intention to provide services based on full LLU. Furthermore, the consumer research we conducted, evidence on actual switching behaviour and the reduction in BT’s market share to date indicate that consumers are willing and able to switch to alternative providers (see paragraphs 5.31-5.42 and 5.44-

<sup>35</sup> Case C62/86 AKZO Chemie BV v Commission [1991] ECR 1-3359.

<sup>36</sup> See paragraphs 110 and 42, respectively, of the Tribunal’s Judgment in *Hutchison 3G (UK) Limited v Ofcom* [2005] CAT 39.

## Fixed Narrowband Retail Services Market Review

5.67 of the March Consultation). We discuss a number of other factors which we have taken into account in our SMP assessment in the sections below.

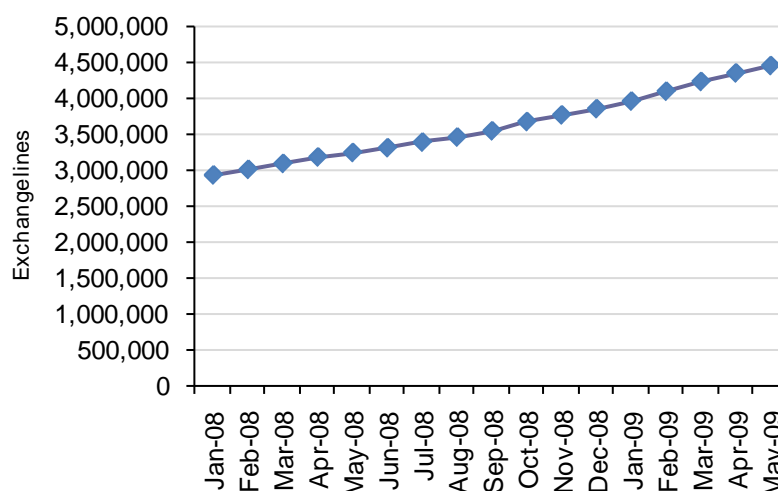
### Trends in BT's market share

5.37

Since the publication of the March Consultation we have collected further information on exchange lines from Communications Providers. This information suggests that competition has continued and BT's market share has decreased further. Residential WLR and LLU lines supplied by competing Communications Providers have continued to increase strongly, up by almost 500,000 lines (an increase of 13%) from January 2009 to May 2009. The total number of lines provided by BT has continued to fall – by over 441,000 from January 2009 to March 2009 (more recent data, as yet not fully audited confirms shows this trend continuing from April 2009 to May 2009). We show the growth in the number of LLU and WLR lines provided by BT's competitors in Figure 5.1 below.

**Figure 5.1**

**Number of residential LLU and WLR lines supplied by BT's competitors (excluding Virgin Media)**



Source: Ofcom/operators

5.38 Updated information on market share is presented below.

**Figure 5.2**

**Updated market shares of residential fixed narrowband access<sup>37</sup>**

	Exchange Lines			Revenues		
	BT	Virgin Media	Other fixed	BT	Virgin Media	Other fixed
2003	83%	17%	0%	80%	19%	1%
2004	82%	17%	0%	78%	20%	2%
2005	78%	17%	5%	76%	20%	4%
2006	72%	17%	11%	71%	19%	11%
2007	69%	18%	14%	66%	18%	15%
2008	64%	18%	18%	64%	18%	19%

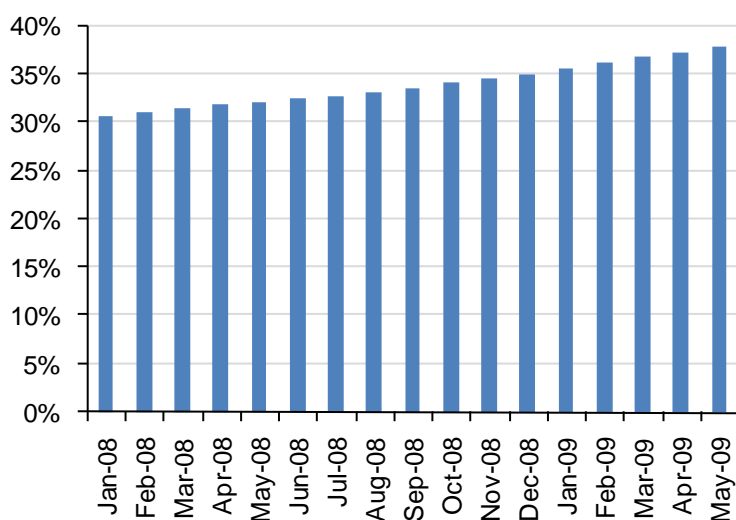
<sup>37</sup> Original information was provided in Table 5.1 of the consultation.

2008 Q1	67%	18%	15%	64%	18%	17%
2008 Q2	66%	18%	16%	65%	17%	18%
2008 Q3	65%	18%	17%	63%	17%	19%
2008 Q4	64%	18%	18%	62%	17%	20%
2009 Q1	62%	18%	20%	62%	18%	20%

Source: Ofcom/operators

- 5.39 We have also used the information gathered using formal powers to compile more detailed market share information for BT's competitors up to May 2009. The Figure below shows that the (monthly) market share for BT's competitors (including Virgin Media) has steadily increased since January 2008 and shows no signs of slowing down. BT's market share has continued to decline in the first five months of 2009.

**Figure 5.3**  
**BT's competitors market share (including Virgin Media)**



Source: Ofcom/operators

- 5.40 In addition, BT has experienced significant levels of churn which provides further evidence that consumers are willing and able to switch provider of residential access lines. In the 12 months to May 2009 BT's churn<sup>38</sup> was [redacted].<sup>39</sup> Over the same time period BT gained a substantial number of new lines through a combination of win back and new provision. Overall this suggests that many consumers are highly mobile and willing to seek out the best deals.
- 5.41 The new information on competition, including BT's market share and churn, supports our initial assessment that the wholesale remedies are effective and have led to low barriers to entry and growth.
- 5.42 However, it is important to note that we consider BT's continued loss of market share as just one indicator that they do not have SMP. Our conclusion that BT does not have SMP is not dependent on BT continuing to lose market share as suggested by some stakeholders (who expressed a concern that BT's market share may not fall significantly

<sup>38</sup> Churn is defined as lines ceased or transferred over 12 months divided by average lines provided over 12 months. Line transfers includes home moves.

<sup>39</sup> The churn statistics are commercially sensitive and have been redacted.

over the review period, in particular, that BT's market share may not fall to a level where it is no longer 'presumed' to be dominant<sup>40</sup>).

- 5.43 We consider the market to be effectively competitive in particular because of the presence of low barriers to entry and growth, thus our assessment does not rest on a further decline in BT's market share over the period covered by the market review (although, as noted above BT's market share has continued to fall since the March Consultation was published). Our assessment is based on the competitive environment remaining broadly similar or increasing in intensity going forward. We will continue to monitor the competitive environment and, if conditions change materially, suggesting that competitive pressures are lessening, we would consider conducting a further review. We consider this in more detail in Section 7.

#### The relative size of competitors

- 5.44 In relation to COLT's comment that market power is more likely to exist when competitors have low market shares, we note in Table 5.2 above that Communications Providers other than BT or Virgin Media provide 20% of residential access lines, mostly using WLR, but also full LLU. The WLR providers do not have a uniform market share and, in addition, looking at WLR alone is an incomplete and inaccurate picture because a number of providers use both WLR and LLU. For example, TalkTalk Group (including Tiscali) has a market share of around [redacted]<sup>41</sup> of exchange lines as at May 2009. Furthermore, a number of WLR providers have entered the market relatively recently (e.g. since 2007) and we would expect it to take some time for them to build market share. We expect the market shares for this set of providers to increase in the future e.g. as providers such as Sky sell into their existing customer bases. As noted above the number of exchange lines provided by 'other' providers has increased since the March Consultation was published. Also, it is important to note that cable is only available in around half of the UK market, thus Virgin Media's market share is significantly higher within their addressable market. Furthermore, as discussed in the March Consultation, these competing providers offer many services alongside residential access lines (they usually sell voice calls and access lines but they may also provide broadband access, pay TV and/or mobile phone services) so some providers are able to enjoy significant economies of scope.

### Impact of LLU

#### **Consultation responses**

- 5.45 COLT believes LLU is well advanced in the UK, and BT's recently stated changes to the deployment of some 21CN voice products/services and its intention to continue using the older TDM voice network will cause BT's market share to fall more slowly than predicted meaning rigorous regulation would still be required.
- 5.46 Sky referred to paragraphs 5.39 and 5.40 of the March Consultation which noted that the rate at which exchanges are being unbundled slowed during 2007 and indicated that LLU does require some sunk investment. Sky commented that this implicitly acknowledged there was some form of barrier to entry or expansion. In light of the slowing rate of unbundling, and compounded by the concerns raised about the inadequacies in BT's wholesale products (discussed further below), it is not clear that

<sup>40</sup> This comment was also made in relation to business analogue access, residential and business calls. Our assessment in these markets is the same.

<sup>41</sup> Redacted as the information was provided in confidence.

BT's market shares will continue to fall, rather than stabilise at a level where it continues to have SMP.

### Ofcom's response

- 5.47 We noted in the March Consultation that the rate of exchange unbundling has slowed during 2007 and this might mean that the decline in BT's market share slows in the future. We reiterate that this is probably because the larger and most commercially important exchanges have already been unbundled. The proportion of premises connected to an unbundled exchange increased from 80% in 2007 to 84% in 2008<sup>42</sup>.
- 5.48 Despite the slowdown in exchange unbundling the number of LLU lines provided has continued to increase, from 1.6 million in December 2008 to 1.7 million in March 2009. In addition, Sky has announced its intention to move to MPF during the summer of 2009 and referred to the lower costs it expects to gain from this<sup>43</sup>. We consider that this is likely to lead to increased incentives being offered to customers to encourage them to purchase both narrowband and broadband services.
- 5.49 We also noted in paragraph 5.39 of the March Consultation that LLU requires some investment in equipment at local exchanges but that it also offers strategic advantages as services can be provided at lower cost. An entrant Communications Provider also has the option of using WLR/CPS to provide services which do not require any investment in infrastructure. The choice between using WLR or LLU thus depends on the preferences and strategy of the Communications Provider in question. The WLR/CPS option means that entry is possible without incurring sunk costs in infrastructure and that Communications Providers are able to purchase the WLR product to complement their on-net LLU-based offer. We believe the current suite of wholesale products allows each Communications Provider sufficient flexibility to compete effectively at the national level with BT in this market.

### Risks of removing regulations are asymmetric

#### Consultation responses

- 5.50 Sky noted that premature removal of ex ante conditions has the clear potential to result in significant harm to consumers – notably in the form of higher prices, and risk to emerging competition to BT. They argued that if the removal of ex ante regulation is based to a significant extent on the continuation of trends considered to undermine BT's SMP, then a high standard should be set for evidence in support of such conclusions. In addition, Sky commented that Ofcom fails to recognise the significant uncertainties associated with the prospective competitive trends identified. They further commented that there is little to be lost from waiting to see whether the trends do actually materialise.

### Ofcom's response

- 5.51 We consider that BT does not have SMP due to the competitive environment created by appropriate wholesale regulation and the resulting market entry and expansion. Therefore we do not agree that our conclusions are based on prospective competitive trends as suggested by Sky.

<sup>42</sup> Page 229 of the Ofcom Communications Market Report 2009.

<sup>43</sup> Press release for its results for the twelve months ended 30 June 2009

([http://media.sky.com/documents/pdf/press\\_releases/FY\\_0809\\_Press\\_Release](http://media.sky.com/documents/pdf/press_releases/FY_0809_Press_Release)).



- 5.52 We also disagree that there is little to be lost from waiting to see whether the trends do actually materialise. If our overall assessment shows that there is no SMP (as we have concluded) at this time, as well as prospectively in taking a forward look, we are required to withdraw regulation now. That aside, as already discussed above, we consider that a failure to withdraw regulation now would not achieve the policy objectives in Article 8 of the Framework Directive in promoting competition.
- 5.53 Any prevention on BT from bundling fixed narrowband voice services with other products and offering a discount relative to the sum of the list price of the individual component products may now be constraining competition to the detriment of consumers. Other Communications Providers frequently offer these types of proposition to customers, for example bundling voice services with broadband and/or pay TV. If BT was free to price discriminate and offer bundles at a discount (in a similar manner to other Communications Providers), we consider it is likely that prices would decrease for some consumers (e.g. consumers taking both voice and broadband services from BT might be able to get a better deal). This would, in turn, compel other Communications Providers to react to the change in competition. We believe that the regulatory outcome suggested by Sky and others, while commercially advantageous for them, would result in less intense competition and, therefore, we consider that a delay in deregulation is likely to have a detrimental impact on consumer welfare. The expected outcomes of deregulation are discussed further in Section 7 of the March Consultation.
- 5.54 As part of our Consultation process we considered whether BT would be able to adversely discriminate against its relatively inert customers if the current regulations were lifted. Our analysis concluded that BT would find it hard to target these customers specifically because it is difficult to differentiate them from other customer segments.
- 5.55 We have discussed above the trend in BT's market share and churn (including recent evidence) and, while there will always be a degree of uncertainty, on balance we consider that BT's rivals will continue to expand.

## **Barriers to entry and expansion**

### **Consultation responses**

- 5.56 Sky had concerns that, despite the introduction and successful uptake of regulated wholesale products, Communications Providers still encounter problems in differentiating the quality and/or scope of their own retail services from those offered by BT Retail. They believe that these constraints limit the extent to which Communications Providers can develop and differentiate their offering from that of BT Retail. The consequence of these limitations is that Communications Providers are unable to provide a comprehensive service of universal standard across the whole of the UK, and Communications Providers are limited to differentiating in their on-net areas only. Sky commented that the suite of wholesale products available is inadequate and BT's decision not to develop wholesale NGN products under the 21CN programme means that BT will retain a competitive advantage.
- 5.57 Sky does not believe that WLR and CPS are as effective at enabling effective competition as Ofcom suggests because they only facilitate replication of line access and call origination services. They do not allow Communications Providers to offer a unique set of line features (e.g. call termination, features, tones, voicemail). Sky further commented that the fact that BT has chosen not to introduce wholesale products that would give Communications Providers more control over their services (for example xMPF and wholesale voice connect (WVC)) helps perpetuate retail homogeneity, hindering the development of competition.

- 5.58 Sky also commented that the inability of LLU operators to provide an xMPF voice only service to on-net customers means that LLU operators are disadvantaged relative to BT Retail. Sky considered that LLU operators are placed at a disadvantage because they are reliant on WLR and CPS to supply voice only customers in unbundled areas and all customers outside the unbundled area. The voice services which can be offered to these voice only or ‘off net’ customers will differ compared with those taking voice and broadband in ‘on-net’ areas which means that an LLU provider cannot offer the same services to all customers across the UK.
- 5.59 A confidential respondent made similar comments about LLU as a competitive constraint i.e. they thought that LLU MPF is not currently capable of providing an effective supply side constraint in voice markets. They considered two things were required to address this: (i) ensuring that there is sufficient margin between MPF and WLR (at least reflecting the underlying cost difference between the two products), and (ii) requiring Openreach to offer a voice-only MPF (so-called xMPF) product to allow operators to provide network based voice services to all customers and not just to the subset who also take broadband from them.
- 5.60 Sky further commented that BT Wholesale’s decision not to offer products such as xMPF and WVC might reflect the commercial incentives of BT group as a whole. They suggest that where BT Retail does not want to consume a particular wholesale product then this is likely to have consequences for the decisions made by BT Wholesale (or Openreach). This could mean that wholesale products which would benefit the market as a whole are not introduced.

### Ofcom’s response

- 5.61 Sky appears to argue that some asymmetry exists between BT and other Communications Providers at the wholesale level and thus we ought to maintain asymmetric regulation at the retail level. We consider that any asymmetry at the wholesale level is limited once the wholesale regulations have been taken into account, and the wholesale products currently available are adequate to enable Communications Providers to fully compete with BT. The uptake of these products at the retail level over recent years and the significant decline in BT’s retail market share supports this assessment. As shown in Figure 5.2 above, other fixed Communication Providers (i.e. those using WLR and LLU) share of the residential exchange line market has increased from negligible in 2004 to 20% in Q1 2009 (representing around 4.6 million exchange lines). We do not consider that LLU operators are at a significant disadvantage relative to BT because they are free to use WLR/CPS to offer voice only services in on-net and off-net areas with no further infrastructure investment.
- 5.62 We accept that there may be other wholesale products that, if provided by Openreach, could offer benefits to Communications Providers which are not available through the current products specifically required as a result of the wholesale remedies. However, an improvement in the wholesale products is not a prerequisite for our assessment that BT does not have SMP, and the significant take up of WLR we have witnessed in recent years indicates that this is an adequate and attractive product.
- 5.63 Given that we do not consider that an enhancement of the current set of wholesale services is required for a determination of no SMP, we do not propose to discuss the pros and cons of such services further in this paper. However, we note that the provision of xMPF is considered as part of the review “Next Generation Networks: Responding to

recent developments to protect consumers, promote effective competition and secure efficient investment”<sup>44</sup>.

- 5.64 It is also appropriate to note that in each wholesale market where BT has been found to have SMP (e.g. Wholesale Local Access, various wholesale narrowband markets), BT has an obligation to provide network access on reasonable request. This allows Communications Providers the flexibility to request products from BT in addition to those specifically mandated by Ofcom. If a Communications Provider thinks BT has not responded appropriately to a reasonable request, Ofcom’s formal complaint or dispute procedures can be used. This issue is considered in the Narrowband Wholesale Market Statement.

## **Developments in NGN**

### **Consultation responses**

- 5.65 Sky commented that BT’s failure to invest in NGN technology has deprived Communications Providers of the opportunity to realise efficiencies through scale and scope economies. This is because interconnecting Communications Providers have lost an opportunity to manage their network footprint more efficiently and, to a large extent, will continue to hand-off voice and broadband traffic to BT at different locations and via differing interconnection technologies at greater expense (because there is a cost to NGN operators for carrying out IP-TDM conversion).
- 5.66 Sky noted that BT’s failure to move to NGN-based voice means that competing Communications Providers are hindered from fully leveraging their investment in their own voice networks, for example by ingressing calls to all their customers themselves. Instead, BT Wholesale will continue to receive wholesale geographic termination revenues for WLR and CPS end users.
- 5.67 TalkTalk Group also commented that Ofcom needs to ensure that BT offers a “better” wholesale line rental product as part of its 21CN product development programme.

### **Ofcom’s response**

- 5.68 As above, we consider that the retail access markets are competitive in the absence of NGN. Therefore the timing for NGN rollout does not affect our SMP assessment. However, we note that competition may be further enhanced when the benefits of BT’s rollout of its NGN are ultimately realised. We consider developments in NGNs further in the Ofcom consultation document, “Next Generation Networks: Responding to recent developments to protect consumers, promote effective competition and secure efficient investment”, referred to above.

## **Reliance on consumer survey evidence**

### **Consultation responses**

- 5.69 COLT commented that Ofcom relies heavily on survey data which asks customers how they are likely to behave in the event of a price rise. COLT noted that such surveys often overstate behaviour and are not supported by the limited empirical evidence reported in the March Consultation.

<sup>44</sup> <http://www.ofcom.org.uk/consult/condocs/ngndevelopments/main.pdf>.

- 5.70 COLT commented that Table 5.5 of the March Consultation shows BT's line rental prices to be amongst the cheapest which might suggest a lack of market power. However, the March Consultation points out that BT's price will rise by £1.00 (a little under 10%) per month from 1st April 2009 making BT the most expensive in the group. COLT have searched the websites of the other operators listed and found that they have not raised their prices in line with BT. According to Ofcom's research referred to at paragraph 5.51 of the March Consultation, such a rise would lead to 22% of customers switching supplier. However, this estimate is based on what survey respondent's state they will do and not on analysis of empirical data showing how consumers actually respond to price rises. Further, the survey data provides no indication as to the timescale over which customers state they would move to another supplier.
- 5.71 COLT concluded that the ability of BT to raise prices by 10% and the poor evidence of likely consumer response to such a price rise, strongly suggest that it is not possible to conclude that BT does not have SMP.
- 5.72 Sky also commented that Ofcom places too much weight on the consumer survey evidence. Specifically, Sky noted that Ofcom placed different emphasis on survey evidence in the retail narrowband and pay TV reviews. In the narrowband review Ofcom concluded that the evidence "*suggests that customers are relatively price sensitive and would be willing to switch*". Sky contrasts this with Ofcom's approach to the pay TV review, where little or no weight has been placed on similar evidence, ostensibly because of concerns that it would be affected by the Cellophane fallacy, and 'stated preference bias' (normally known as "*hypothetical bias*").

### Ofcom's response

- 5.73 Firstly, it is important to note that in both the narrowband and pay TV reviews we used a range of evidence to inform our market definition and market power assessments. We regard the narrowband survey evidence as complementary to the other sources of evidence considered (discussed elsewhere in this Section). For example, the decline in BT's market share is consistent with the survey evidence which found that consumers are willing to switch provider. We have not solely relied on consumer survey evidence in reaching our conclusions.
- 5.74 COLT commented that actual evidence on BT's recent price increases does not support the conclusion that consumers are willing to switch provider. However, this interpretation fails to recognise a number of other changes made to BT's pricing. At around the same time as BT raised its line rental price by £1, it made a number of other changes to its line/calls packages. In January 2009 BT included 0845 and 0870 numbers in the free element of its call plans. In addition BT relaunched the Friends and Family scheme. It is not clear that overall phone bills will rise if these factors are netted out. Indeed, Enders Analysis assessed that, "the direct impact of the changes [is] neutral taking into account the increase in line rental"<sup>45</sup>. Our research has indicated that consumers often tend to view the line and call package together and, therefore, we would not necessarily expect this line rental price change (when accompanied by savings in call prices) to result in significant switching away from BT. Nor would we necessarily expect other Communications Providers to raise their line rental prices unless they are also making changes to calls package.
- 5.75 We do not have the empirical evidence to assess the consumer reaction to a historic (and recent) increase in price (we would need more than a few months data to assess the reaction of consumers). Furthermore, as noted above, changes in the price of line

<sup>45</sup> Enders Analysis, BT residential telephony prices changes: rebalancing act, 11 February 2009, page 4.

rental may be accompanied by other offsetting package changes so it is difficult to isolate the consumer reaction to the price increase for line rental alone. We would also need to collect detailed information on the price changes implemented by BT's rivals (and other changes to factors affecting demand such as marketing spend). In the absence of empirical evidence we are reliant on survey information but note the limitations of this data.

- 5.76 The purpose of the survey is to prompt those questioned to make a decision. In the real world in response to a price increase consumers who switch will do so at different points in time: e.g. it will depend on individual time constraints, the time it takes to research alternatives and reach a decision. It is difficult to accurately assess this as part of a survey. The point to note is that a significant proportion of survey respondents clearly indicated an intention to switch in response to an increase in price. This is consistent with the evidence presented above which shows that BT has a significant rate of churn and win back (i.e. customers are willing and able to seek out the best deals).
- 5.77 We consider it unlikely that the narrowband survey suffered from cellophane fallacy because BT's prices were regulated via the RPCs until 2006. Furthermore, the evidence presented in Annex 6 to the March Consultation suggests that overall prices have increased by less than RPI since the RPCs were lifted (and, as such, prices are lower than the ceiling that would have been in place had the RPCs been continued in the same form as they had been in July 2006).
- 5.78 We accept that any survey answers could be subject to a degree of hypothetical bias (i.e. a difference between actual willingness to pay and willingness to pay revealed in a survey arising from the fact that in actual markets purchasers face real costs, while in surveys they do not). However, given that a substantial proportion (i.e. around one third) of consumers have actually switched provider (thus have a very good idea of the costs involved) the likelihood of systematically underestimating the costs of switching is likely to be less significant.

## **BT's pricing**

### **Consultation responses**

- 5.79 Sky commented that, despite the entrance of new operators, BT has been able to maintain its prices at a relatively stable level indicating an ability to act without regard to its competitors<sup>46</sup>.

### **Ofcom's response**

- 5.80 Although BT has maintained prices at a relatively stable level they have been losing market share (as illustrated above) i.e. in keeping prices at a stable level BT has lost subscribers as they have moved to competing providers. Competition began to intensify in 2006 with competitors offering discounts relative to BT's prices particularly for bundled offerings. BT has been constrained in its ability to respond flexibly to these offers given the constraints on BT linking SMP and non SMP services in its retail offers. Relaxing the present constraints on BT is likely to increase competition in the delivery of bundled offers and put downward pressure on prices.

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<sup>46</sup> Sky also made this comment in relation to the calls markets. Our assessment for these markets is the same.

- 5.81 Ultimately it is up to individual Communications Providers to decide what pricing strategy to pursue, however, the evidence suggests that consumers are willing and able to seek out the best deals and switch provider.

### **BT's scale advantages**

#### **Consultation responses**

- 5.82 FCS commented that BT still enjoys many scale advantages over the rest of the market and Ofcom had identified one of these advantages that “customers that are uninterested in changing providers are most likely to remain with BT”.

#### **Ofcom's response**

- 5.83 Given that BT is the incumbent operator, it will retain a number of consumers that have limited interest in switching. However, the evidence suggests that (i) a large proportion of consumers are price sensitive and willing to switch (as suggested by the consumer survey – see paragraphs 5.51-5.55 and 6.23-6.28 of the March Consultation); (ii) consumers are actively switching as evidenced by the fall in BT's market share (see Figure 5.2 above); and (iii) it would be difficult for BT to target price increases specifically at inactive customers (see paragraphs 5.56-5.62 of the March Consultation and paragraphs below).

### **Default supplier status**

#### **Consultation responses**

- 5.84 Sky commented that certain features of the market can be expected to help support BT's market shares, and thus perpetuate its SMP. For example, there is the asymmetry of BT being the ‘default supplier’, which continues to favour BT Retail: when a calls-only customer of another supplier cancels their contract without positively switching to another Communications Provider, their service will default to BT Retail (which remains the only provider able to offer stand-alone line rental).

#### **Ofcom's response**

- 5.85 In the example BT is not just a default supplier. In addition to adding CPS to their line, the customer has chosen to continue to take line rental (and possibly some calls using the CPS override code) from BT Retail. Where the customer has cancelled their calls only service it is appropriate that the service is removed from their line. Furthermore, BT retail is the only provider that offers standalone line rental because it is the only provider required to do so as a result of regulation at the wholesale level. BT's competitors are not prevented from offering line rental only services; they choose not to do so because commercially they would rather gain line rental and calls revenues.
- 5.86 Additionally, we do not consider that BT derives SMP from this position. Given that the customer has switched in the past (i.e. to a CPS provider) they would be able to switch away from BT again if so desired.

## **BT's profitability**

### **Consultation responses**

5.87 Sky commented that Ofcom's examination of BT's profitability is somewhat limited in relation to that undertaken in the pay TV review. In particular Sky noted that Ofcom employed consultants to undertake a detailed examination of Sky's profitability.

### **Ofcom's response**

5.88 We have conducted a proportionate analysis of BT's profitability drawing on various sources of information e.g. BT's regulatory accounts<sup>47</sup>, information collected under our formal powers, revenue per minute and revenue per line information (refer to paragraphs 5.70 to 5.76 of the March Consultation). Also, the existence of the RPCs (up to 2006) and the regulatory financial statements, mean that Ofcom has a strong existing understanding of BT costs, revenues and profits.

5.89 We have, nonetheless, undertaken a further detailed analysis of BT costs, revenues and returns for both access and calls as most consumers purchase them jointly (as set out in the March Consultation and below). These set out in detail the basis of changes in returns and their consistency with our assessment of the market.

5.90 To provide some further information on profitability we have used BT's 2008/9 regulatory accounts to update the analysis for the residential access and calls<sup>48</sup> market<sup>49</sup>. The updated numbers are shown below.

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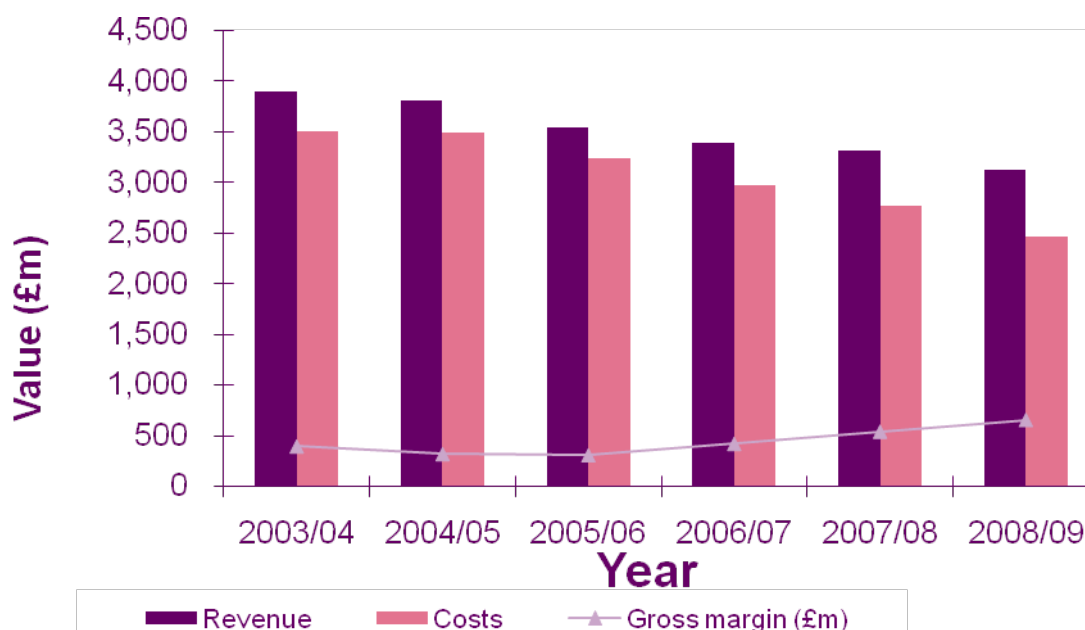
<sup>47</sup> Available at <http://www.btplc.com/Thegroup/RegulatoryandPublicaffairs/Financialstatements/index.htm>.

<sup>48</sup> Call types included are local, national, international direct dial category A and call to mobile.

<sup>49</sup> In light of the 2009 consultation and statement on changes to BT and KCOM's regulatory financial reporting, for 2008/9 BT was not required to report international direct dial category B or operator assisted calls due to the small size of these markets (refer to [http://www.ofcom.org.uk/consult/condocs/btkcom09/statement/btkcom\\_statement.pdf](http://www.ofcom.org.uk/consult/condocs/btkcom09/statement/btkcom_statement.pdf), section 4). These call types have been removed from the previous year's figures to ensure the time series is consistent.

Figure 5.4

## Residential access and calls markets – revenues, costs and returns from 2003/4 to 2008/9



Source: BT's regulatory accounts

- 5.91 The Figure shows that BT's revenues have continued to decline in 2008/9. However, BT's costs have decreased faster than revenues which means that gross margin and return on sales<sup>50</sup> for access and calls have increased (the return on sales has increased from 16% in 2007/8 to 21% in 2008/9).
- 5.92 There could be a number of possible reasons for the apparent rise in profitability, for example, it could reflect BT's ability to raise prices (which might suggest an element of market power). Alternatively it could reflect improved efficiency and cost cutting in response to aggressive competition.
- 5.93 There has been some increase in prices since 2005/6 though, as noted in our RPC review in Annex 6 to the March Consultation, the increase in prices from August 2007 to July 2008 was below the ceiling that would have been in place had the RPCs been in effect at the same level as July 2006. We have examined BT's costs as reported in the regulatory accounts in more detail to determine the underlying reasons for the apparent rise in profitability.
- 5.94 Comparing 2007/8 and 2008/9, BT's costs have decreased by £303m across the residential access and calls markets<sup>51</sup>. A significant portion of this (around 67%) was due to decreased charges from wholesale markets and reduced out-payments (e.g. to other operators for termination) both of which reflect decreased volumes in the number of lines and calls provided by BT.
- 5.95 However, the third largest contributor is general management. This contributes 13% or £38m to the cost reduction. Then there are 'other costs' which have decreased by £19m,

<sup>50</sup> Return on sales (%) = Gross margin (i.e. revenues minus costs) / revenue.

<sup>51</sup> Excludes roundings.

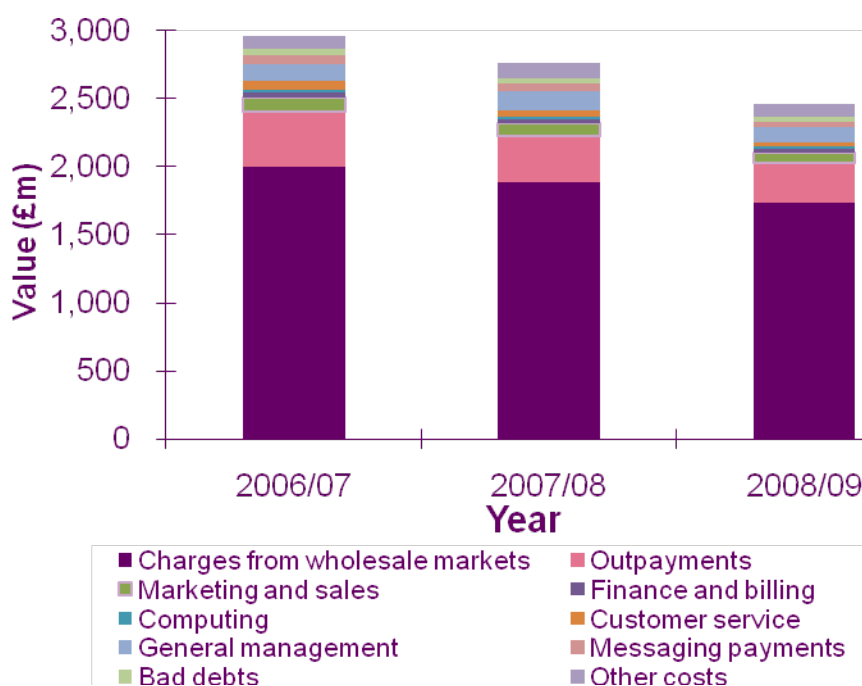


messaging payments and marketing and sales which have both decreased by £12m and customer services which has decreased by £11m. The evidence suggests that BT has maintained profitability by reducing costs. Nonetheless it is difficult to draw strong conclusions from these gross margin data as, from an economic point of view, the cost reductions could also reflect a decrease in economic investment (e.g. subscriber acquisition costs) that should be amortised rather than treated as a current costs and fully expensed.

- 5.96 BT's access costs per line have decreased from £127 per year in 2007/8 to £124 per year in 2008/9<sup>52</sup>.

Figure 5.5

Residential market costs reported in BT regulatory accounts



Source: BT's regulatory accounts

- 5.97 A further factor which has improved gross margin is customers migrating to higher value call packages i.e. packages with a higher fixed monthly costs and more inclusive minutes. This would appear to reflect customer choice as to which package offers optimal value (we discussed this in paragraph 6.39 of the March Consultation). The table below shows the proportion of BT's customers on the higher value packages (i.e. the unlimited evening and weekend and anytime plans) has increased in 2008/9.

<sup>52</sup> To calculate the cost per line we used the total costs for residential analogue exchange line services taken from BT's Current Cost Financial Statements 2009 (pages 78-79) and the number of exchange lines reported in Ofcom Telecommunications Market Data Tables.

Figure 5.6

**Residential customers by package**

Package	% of customers on package in 2007/08	% of customers on package in 2008/09
Unlimited weekend plan	63%	47%
Unlimited evening and weekend plan	20%	34%
Unlimited anytime plan	7%	11%
Other including LUS <sup>53</sup>	9%	8%

Source: BT

5.98 We have also provided some additional information on BT's profitability in the business analogue access and ISDN2 sections below.

**Ofcom's conclusion on the residential analogue access market**

5.99 To conclude, taking into account the available evidence (set out in the March Consultation and above) and stakeholder responses, we are of the view that the residential analogue access market is effectively competitive. Over the forward look period we believe competition is likely to increase e.g. as Communication Providers such as Sky sell narrowband services as part of a bundled package into their existing customer base.<sup>54</sup>

**Hull**

5.100 In the March Consultation, we considered that KCOM does have SMP in the residential fixed analogue market for the following reasons:

- There are no significant competitors in the market.
- Threat of entry is somewhat limited.

5.101 With respect to the three tests for *ex ante* competition in relation to the Hull area, we are of the view that the market does not tend toward competition due to the presence of barriers to entry and a lack of competition in the market. Therefore the Commission's first two tests are not satisfied.

5.102 In addition, we do not think that competition law alone is enough to address the SMP in this market, as the entry barriers are too high, and have proved to be effective in excluding competition. Therefore it is appropriate to impose *ex ante* regulation on the market.

**Barriers to entry in Hull****Consultation responses**

5.103 One stakeholder (KCOM) responded to the SMP analysis for the Hull area. KCOM do not agree with our conclusion that there remain significant barriers to entry in the Hull

<sup>53</sup> LUS is the Light User Scheme – a USO product now being replaced by BT Basic.

<sup>54</sup> In its press release for its results for the twelve months ended 30 June 2009, Sky stated "We are well positioned to drive increased take-up as customers respond to the value we offer, with still 7.9 million of our customers yet to choose Sky Broadband and Talk." ([http://media.sky.com/documents/pdf/press\\_releases/FY\\_0809\\_Press\\_Release](http://media.sky.com/documents/pdf/press_releases/FY_0809_Press_Release)).

area. Rather than acting as a disincentive to invest, they suggest the relatively small size of the Hull market offers competing providers access for a comparably small investment either in their own infrastructure or through the use of wholesale products offered by KCOM. They suggest this is particularly the case for the larger Communications Providers who have entered the UK market and grown their customer base significantly since Ofcom undertook the last narrowband market review and now benefit from much larger economies of scale and scope than KCOM. KCOM believes that this threat of entry has only intensified given the propensity for competing Communications Providers to offer bundled packages which enable even greater advantage to be taken of their extensive economies of scale and scope.

- 5.104 KCOM believe the fact that competitive entry remains a very real threat is evidenced by their pricing of retail services which Ofcom has noted is broadly comparable with that offered by BT. Furthermore, KCOM is very aware that its customers have a very clear view of offers available to consumers in the rest of the UK and as such will not hesitate to tell KCOM if their pricing, products or customer service compares negatively with that available through other providers. As such KCOM suggest their own customer base acts as an effective constraint. Despite the lack of significant market entry by competing providers, they state that KCOM is not in a position to act independently of the wider market.
- 5.105 KCOM have provided some more recent information on residential exchange line numbers which is presented below.

**Figure 5.7**

**Residential lines provided by KCOM**

	2003	2004	2005	2006	2007	2008	2009 (May)
Number of exchange lines	157,856	155,666	152,449	150,483	149,106	146,901	[redacted] <sup>55</sup>
% change over previous year	-1%	-1%	-2%	-1%	-1%	-1%	[redacted]

Source: KCOM

**Ofcom's response**

- 5.106 The lack of actual or prospective market entry in the Hull area suggests that significant non-transitory barriers to entry exist. KCOM notes that larger Communications Providers who have entered the UK market and increased their market share may benefit from economies of scale. KCOM seem to infer that these competitors could easily expand into the Hull area. However, it is not simple for competitors in the rest of the UK to roll out their existing arrangements in Hull: products and processes are likely to differ and wholesale arrangements would likely need to be negotiated on a different basis. In particular, Communications Providers would not be able to leverage their systems development unless KCOM used the same processes and systems interfaces as BT. It is much less likely that a Communications Provider could justify developing specific system interfaces to KCOM, given the size of the market in the Hull Area.

<sup>55</sup> Redacted as not yet audited.

- 5.107 Given the relatively small size of the Hull market the opportunity for achieving sufficient scale to reap scale and scope economies may be limited which is likely to act as a deterrent to entry in the Hull area – especially given the significant investment in marketing and advertising that would be required to attract customers away from the longstanding incumbent. The lack of alternative providers and the presence of barriers to entry create a strong presumption of SMP.
- 5.108 The fact that KCOM's pricing is comparable to BT is not compelling evidence of a competitive constraint as KCOM could change its prices and its customers would currently have no alternative options to obtain fixed line access.
- 5.109 The number of exchange lines provided by KCOM in Hull has declined slowly over time. The more significant decline in early 2009 may well reflect greater substitution to mobile-only access as people economise in response to the economic downturn. However, it is not possible to say whether this trend is permanent or will change when economic conditions improve.

### **NGA impacts in Hull**

#### **Consultation responses**

- 5.110 KCOM also believe that the introduction of NGA has the potential to prove an even greater competitive constraint. KCOM see NGA rollout as a key issue over the timeframes for this market review. KCOM suggest that investment in a new geographic area such as Hull would represent a very small increment for an alternative provider and offer the opportunity of access to a new market. They would therefore expect Ofcom to carry out further analysis of the likely impact of NGA developments over the coming 4-5 years.

#### **Ofcom's response**

- 5.111 We do not believe that the introduction of NGA will have a significant impact on the Hull area over the period of this Review.
- 5.112 While BT has indicated that it will seek to speed up its NGA roll-out their plans, for the present they will focus on replacement of their own infrastructure and new greenfield sites. BT's focus where existing infrastructure exists is to deliver fibre to the cabinet rather than the home so, even in the event that BT did decide to consider rollout in the Hull area, they would still require access to the KCOM cabinets. Virgin is also looking into developing an NGA product but, again, we are not aware of plans for rollout in the Hull area.
- 5.113 There is also no evidence of other companies proposing large scale NGA roll out at this stage.
- 5.114 We do accept that if/when NGA is rolled-out in Hull, even by KCOM, this is likely to offer a significant opportunity for new wholesale access which may encourage strong retail competition. But we do not consider this is likely to act as a significant constraint on KCOM within the current review horizon.

## **Business Markets for fixed analogue access**

### **UK (excluding Hull)**

5.115 In the March Consultation, we suggested that the business market for fixed analogue access in the UK (excluding Hull) was competitive with no company holding significant market power for the following reasons:

- The wholesale remedies have led to the development of products which enable competitors to replicate the services offered by BT without making significant infrastructure investments. This has lowered barriers to entry and growth.
- New firms have entered and expanded in the market resulting in a fall in BT's market share.
- Relaxation of the SMP regulations in 2007 for large businesses appears to have been successful.
- Recent market research has shown that businesses are aware of alternative providers and appear willing to switch.

### **Overview of consultation responses**

5.116 Ten stakeholders provided comments on the business access SMP assessment for the UK (excluding Hull). Stakeholder views were similar to those presented above for the residential market with a number of stakeholders providing comments for the business and residential markets combined. To avoid repetition, combined comments have been covered in the residential discussions above, although a further discussion is provided below where warranted.

5.117 BT agreed with our assessment that they no longer have SMP in the business access market. They believe that our proposals are fully justified and are a logical progression from the 2007 Replicability decision where Ofcom found that BT's Retail access services are replicable by its competitors.

5.118 The other respondents disagreed with our conclusions. The main issues of concern were BT's market share and apparent ability of BT Retail to charge a price premium. We discuss these points and other stakeholder comments in more detail below.

### **BT's market share**

#### **Consultation responses**

5.119 The comments made on BT's market share in the business analogue access market were very similar to those made in relation to the residential market (discussed above). A number of stakeholders, including TalkTalk Group, COLT, SSE, Cable & Wireless, FCS and UKCTA, commented that BT still has a relatively high market share which was indicative of SMP and expressed concern that the market was not sufficiently competitive to justify full deregulation. Some Communications Providers further commented that BT's market share would not decline at a sufficient rate to rebut the presumption of dominance over the forthcoming review period.

#### **Ofcom's response**

5.120 As noted in the residential section above, a high market share alone is not enough to conclude that SMP is present. A wide range of factors need to be taken into account in

an overall SMP assessment. In particular, we believe that the available evidence shows that barriers to entry and expansion in this market are low because the wholesale remedies in place (particularly WLR) mean that competitors can easily enter the market and replicate the services offered by BT without making significant infrastructure investments. New firms have entered and expanded in the market resulting in a 19% fall in BT's share of business exchange lines from 85% in 2003 to 66% in 2008.

- 5.121 The information collected formally from Communications Providers since the March Consultation was published suggests that strong competition has continued and BT's market share has fallen further. The number of business analogue lines provided by BT fell by around 5% from January to May 2009. Research we have examined suggests that price is the main reason why customers are moving away from BT.
- 5.122 Updated market share information is presented below. As noted in the introduction to this section, this data has been revised since the March Consultation was published, in particular, the revised estimates suggest BT's share of exchange lines is higher over the period 2006-2008 than previously reported.

**Figure 5.8**

**Updated market shares of business fixed narrowband access<sup>56</sup>**

	Exchange Lines		Revenues	
	BT	Others	BT	Others
2003	85%	15%	87%	13%
2004	83%	17%	86%	14%
2005	78%	22%	79%	21%
2006	74%	26%	72%	28%
2007	69%	31%	68%	32%
2008	66%	34%	65%	35%
2008 Q1	68%	32%	66%	34%
2008 Q2	67%	33%	66%	34%
2008 Q3	67%	33%	65%	35%
2008 Q4	66%	34%	63%	37%
2009 Q1	65%	35%	63%	37%

Source: Ofcom/operators

- 5.123 In the 12 months to May 2009 BT's churn<sup>57</sup> was [X]. This is partly driven by a decline in market size (e.g. some businesses have ceased trading) but also indicates that BT is losing customers to other Communications Providers. Research also suggests that churn has increased between Q2 2008 and Q4 2008. Over the same time period BT gained a substantial number ([X]) of new lines. Overall this suggests that businesses are willing and able to seek out the best deals and switch provider.
- 5.124 Churn in business is lower than in residential lines, which may, in part be a factor of longer and stronger contractual commitments and less movement in premises (moves often prompt a review of service providers).

<sup>56</sup> Original information was provided in Table 5.16 of the consultation.

<sup>57</sup> Churn is defined as lines ceased or transferred over 12 months divided by average lines provided over 12 months. Line transfers includes change of premises.

- 5.125 The new information on competition including BT's market share and churn supports our assessment that the wholesale remedies are effective which has led to low barriers to entry and growth.

### **BT's pricing and profitability**

#### **Consultation responses**

- 5.126 COLT suggested a further reason why Ofcom's analysis does not prove a lack of SMP is that BT is able to retain a price premium evidenced by its share of revenue being greater than its share of volumes. COLT stated that BT's ability to maintain this price differential without losing market share indicates the persistence of market power. COLT further commented that Ofcom's analysis is often one-sided, explaining why it believes BT's ability to charge a price premium does not indicate the presence of SMP, but not exploring why it might indicate the presence of SMP.

#### **Ofcom's response**

- 5.127 We have updated BT's market share for lines and revenues since the March Consultation was published. The revised figures show that since 2006 BT's share of lines has been greater than their share of revenues. The evidence therefore suggests that BT is not charging a price premium.
- 5.128 Moreover, it is not necessarily the case that a price premium indicates SMP, as demand for access is linked to the price of calls and other products. This means it is not necessarily possible to conclude that a price premium is being charged without considering access together with the prices of related products.
- 5.129 We also formally requested additional information from BT to further assess profitability in the business market. The Figure below presents BT's revenues, costs and gross margin for the business analogue access combined with local and national business analogue calls<sup>58 59</sup> for 2005/6 to 2008/9.

**Figure 5.9**

#### **Business analogue access and local/national calls – revenues, costs and returns 2005/6 and 2008/9<sup>60</sup>**

[X]

*Source: BT*

- 5.130 BT's revenues for calls and access have decreased over time. Revenues decreased by around 9% in 2008/9 relative to 2007/8. The return on sales<sup>61</sup> has varied over the period and decreased by 8 percentage points from 2006/7 to 2007/8 (from [X] to [X]), though increased by 2 percentage points in 2008/9.
- 5.131 BT's regulatory accounts do not contain a more detailed cost breakdown for the business markets so our analysis here is more limited. However, the information

<sup>58</sup> It is useful to consider lines and calls together as customers tend to buy these services as a package, and a low price for access can increase demand for calls.

<sup>59</sup> It was not possible to include mobile and international calls because it was not possible to split the data between PSTN and ISDN services.

<sup>60</sup> Redacted as the information is commercially confidential.

<sup>61</sup> Gross margin / revenue.

obtained from BT shows that BT's costs per business analogue access line decreased £6 between 2007/8 and 2008/9.

### **BT has advantages of scale**

#### **Consultation responses**

5.132 FCS said that BT has advantages of scale, for example, they thought that the popularity of inclusive business packages (referred to in paragraph 4.91 of the March Consultation) was largely due to BT marketing and the power of the BT brand. They noted that other Communications Providers can use e.g. indirect access, to replicate this type of service offer but do not always have the knowledge or expertise to do so.

#### **Ofcom's response**

5.133 We are not convinced that the popularity of inclusive business packages is necessarily a reflection of BT marketing and the power of the BT brand. The popularity of inclusive packages is as likely to be demand driven with customers attracted by the convenience of a one stop shop to purchase services. In addition, the wholesale products available (e.g. WLR/CPS and LLU) allow Communications Providers to create offerings similar to BT. We believe that small scale entry in the business market is feasible because business customers are more interested in purchasing bespoke or value added services with a number of small providers offering a package of services to businesses. This is supported by the available evidence showing competing Communications Providers winning sales from BT.

### **Ofcom's conclusion on the business analogue access market**

5.134 To conclude, taking into account the available evidence (set out in the March Consultation and above) and stakeholder responses, we are of the view that the business analogue access market is effectively competitive. Over the forward look period we believe competition is likely to increase.

### **Hull**

5.135 In the March Consultation we considered that KCOM still held SMP due to the muted prospects for entry and high market share of KCOM.

#### **Consultation responses**

5.136 Only one stakeholder (KCOM) commented on the SMP analysis for the Hull area. KCOM thought that the impact of leased lines substitution in the business analogue exchange lines and calls markets had been substantially underestimated. In particular, KCOM thought that if traffic using leased lines to bypass the PSTN was taken into account in the business calls market, KCOM's market share is substantially lower than estimated by Ofcom and no longer justifies a finding of SMP and the imposition of regulatory remedies.

5.137 KCOM noted that although Ofcom recognises that some Communications Providers offer fixed exchange line services by other means in the Hull area (e.g. leased lines or fixed radio access) no estimate was given for the market share this represents. The only figures given are the number of business exchange lines provided by KCOM during 2006/07 and 2007/08 which Ofcom concludes is a high market share creating a presumption of market power.



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5.138 KCOM further noted that in its statement on the Business Connectivity Market Review published in December 2008 Ofcom concluded that KCOM no longer had SMP in the retail market for low bandwidth TI leased lines based largely on KCOM's low market share of 25%. KCOM commented that this would suggest rather more extensive use of alternative access methods than suggested by Ofcom and must be taken into account by Ofcom in assessing the constraints which apply to KCOM's provision of business analogue exchange lines.

5.139 KCOM has provided some revised information on the number of business exchange provided in the Hull area:

**Figure 5.10**

**Business exchange lines provided by KCOM**

	2003	2004	2005	2006	2007	2008	2009 (May)
Number of exchange lines	41616	41629	44334	44612	45072	44581	[redacted] <sup>62</sup>
% change over previous year		0%	6%	1%	1%	-1%	[redacted]

Source: KCOM

### Ofcom's response

5.140 We note that there are Communications Providers offering fixed line exchange services by other means in the Hull area. However, we lack information to ascertain the number of lines offered by alternative providers specifically in the Hull area. For example, leased lines are not part of the narrowband access market and are assessed as part of a separate market review. While it is possible that leased line calls are exerting some competitive pressure on KCOM PSTN access, this is only likely to be evident for larger businesses where leased lines are a viable alternative. The information provided on the number of business exchange lines suggests the market size is relatively static and substitution to mobile access or other alternatives is limited.

5.141 We are nonetheless open to considering whether competition in the calls market for larger businesses is sufficiently developed to warrant a relaxation of the remedies. This is discussed in more detail in Section 7.

## ISDN2

### UK (excluding Hull)

5.142 In the March Consultation we considered that BT still held SMP due to:

- the absence of significant competitors and apparent barriers to expansion;
- BT's high market share combined with apparently increasing retail margins; and
- lack of evidence of increased competitive intensity.

<sup>62</sup> Redacted as not yet audited.

## Consultation responses

- 5.143 Three stakeholders commented on the SMP assessment for ISDN2 in the UK (excluding Hull).
- 5.144 Two stakeholders agreed with our assessment (COLT and a confidential respondent).
- 5.145 BT disagreed with the SMP assessment. BT commented that we had failed to properly assess whether the ISDN2 market meets the EC three criteria test which we have already discussed in the market definition section above.
- 5.146 BT also stated that ISDN2 is increasingly in competition with new technologies such as IP-based products and there is a strong level of competition from neighbouring products. BT considered that our analysis does not sufficiently take into account these forward looking factors.
- 5.147 BT further commented that the finding of SMP in the ISDN2 market was not justified for the following reasons:
- barriers to customers' switching are low, and this is demonstrated by the very high levels of churn;
  - BT's declining revenue and profit margin;
  - the significant buying power of business customers, their market awareness and their ability to multi-source; and
  - the fact that BT gains no advantage from its vertical integration as a result of the existing wholesale remedies.

## Ofcom's response

- 5.148 We recognise that BT and other retail suppliers of ISDN2 are likely to face increased competition from IP based solutions, leading to a progressive decline in the ISDN market (this is noted in paragraphs 5.175 and 5.177 of the March Consultation). Based on information in BT's regulatory accounts we estimate that the number of ISDN2 channels provided by BT and others has decreased by an average of around 4% per year from 2005/6 to 2008/9. We anticipate that the number of channels will continue to decline steadily over the review period.
- 5.149 Nonetheless, there remains a significant number of customers who have invested in equipment specific to ISDN2 technology who are unlikely to switch to alternative technologies until the equipment requires replacement. In the current economic environment it is possible that such capital replacement programmes will be deferred which will slow any decline in the ISDN market, though equally, difficult market circumstances may also lead to investments in new services which give rise to cost savings. However, rivalry from neighbouring products is likely to be strongest when competing for new customers and existing customers are less likely to benefit from this process.
- 5.150 A further barrier to substitution is the need for reliable and resilient services – which is particularly important for business customers. For example, broadband service levels are lower with higher fault rates relative to ISDN services. This means customers requiring high reliability are likely to remain with ISDN until more resilient IP based

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services are available. Some businesses who have switched to IP services retain ISDN2 as a secondary back up line.

- 5.151 We have not observed, in any event, that the declining market size has significantly increased the competitive constraints on BT, for example, BT's margin over wholesale access costs has increased over the period (see paragraph 5.168 of the March Consultation).
- 5.152 We explained in the March Consultation (paragraphs 5.150-5.152) why we believe some barriers to entry, expansion and switching remain. We also discussed above why we think competition from neighbouring (e.g. IP based) products has not significantly increased the competitive constraints on BT. In summary, we consider that barriers to entry remain because:
- a. ISDN tends not to be purchased in isolation but as part of a suite of business products/services and to win ISDN market share quickly, firms may well need to offer a whole range of attractive communication products which makes entry and expansion more difficult than for analogue exchange lines.
  - b. It can be difficult and costly to reach ISDN customers because ISDN is purchased by a minority of businesses.
  - c. Although a number of new providers have entered the ISDN market, these resellers are relatively small scale.
  - d. Even if switching costs are small in absolute terms they may well be high relative to the financial benefits of switching (see paragraph 5.157 of the March Consultation).
- 5.153 In support of their position BT noted that they have lost a substantial number ([redacted]<sup>63</sup>) of ISDN 2 channels over the past 5 years and have a high level of churn. However, this figure includes any movement including location moves and customers who switched to other BT products, so this is not an accurate measure of the competitiveness of the market.
- 5.154 BT noted that their revenues and profit margin are in decline. We would expect ISDN2 revenues to fall over time given that the market is in decline and the number of channels is falling (as noted above). The information submitted by BT shows that return on sales for ISDN2 access fell by 5 percentage points from 2006/7 to 2007/8 but then increased 3 percentage points in 2008/9. The return on sales for ISDN2 access combined with local and national calls via ISDN2 was constant (at [redacted]) in 2007/8 and 2008/9<sup>64</sup> <sup>65</sup>. Access costs (i.e. the costs to BT) per ISDN2 channel have increased from 2006/7 to 2008/9. Overall we consider that profit margins are not under significant pressure due to increased competition.
- 5.155 BT considered that the types of customers who purchase ISDN2 (e.g. business customers who multisource) reduced their ability to exert market power. We are not convinced that these customers have sufficient buyer power. ISDN2 customers are likely to multisource to obtain security of supply (e.g. for contingency purposes) and are not

<sup>63</sup> Redacted as commercially sensitive.

<sup>64</sup> It was not possible to include mobile and international calls within this measure because these calls were not split between those made on PSTN, ISDN2 and ISDN30.

<sup>65</sup> We recognise that ISDN 2 calls are not a separate market (as noted in section 4 we have defined a market for business calls which includes ISDN and PSTN calls), however, it is useful to consider ISDN2 access and calls together as customers tend to buy these services as a package.

likely to switch between these suppliers based on small difference in price. As such, it is not clear that multi-sourcing would drive competition in this market.

- 5.156 The fact that BT does not gain advantage from vertical integration due to wholesale remedies is an important step towards achieving a competitive market. However, it does not necessarily mitigate SMP in markets characterised by barriers to expansion (as discussed above).
- 5.157 We have updated the information on BT's market share in ISDN2 which is presented below:

**Figure 5.11**  
**BT Market share for ISDN 2<sup>66</sup>**

	2005/6	2006/7	2007/8	2008/9
<b>Total channels</b>	1.515	1.459	1.428	1.299
<b>BT</b>	1.344	1.201	1.081	0.898
<b>Others (WLR resellers)</b>	0.171	0.258	0.347	0.401
<b>BT market share</b>	89%	82%	76%	69%

Source: BT Regulatory Accounts

- 5.158 BT's market share of channels and revenues has continued to fall which reflects the entry of small scale Communications Providers offering WLR services. However, it remains the case that BT's competitors are relatively small and no entrant has a market share above 3%. The evidence still suggests that the market structure is characterised by a single dominant player with a number of competitors with very low individual market shares.
- 5.159 We believe that BT faces little incentive to respond to competition from the fringe of smaller firms by lowering prices to business customers. As noted in paragraph 5.173 of the March Consultation, as the market declines low prices are less likely to result in increased sales, but instead will simply benefit existing customers. In a declining market the incentive to invest in entry and expansion is likely to be limited. In addition, businesses will increasingly use ISDN2 as a backup line which means it is a less attractive proposition for Communications Providers to offer e.g. because there is a limited ability to generate revenues from calls. The significant increase in BT's margin over wholesale access costs (discussed in paragraphs 5.168 and 5.169 of the March Consultation) indicates the lack of incentive to compete on price.
- 5.160 Overall we consider that the ISDN2 market has certainly become significantly more competitive since the last review due to the wholesale remedies which have reduced barriers to entry. However, we consider that on balance an SMP finding is still appropriate because:
- Although the number of players in the market has increased, this does not appear to have increased the intensity of competition to a sufficient degree to support a no SMP finding. Prices have remained relatively static and BT's margin over wholesale access costs has increased since the last review.

<sup>66</sup> Figures exclude Virgin media which we estimate to be around 1% of the total market.

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- BT's competitors are relatively small and the market is characterised by a single dominant player, a fringe of competitors and a constant set of products. BT faces little incentive to respond to competition by a fringe of competitors by lowering prices.
- BT's profitability (as indicated by the return on sales figure) shows little sign of consistent material decline.

5.161 However, as discussed in Section 7, we consider that the existing remedies for SMP are not effectively promoting competition. We consider that there is a value in encouraging more active price competition between BT and other Communications Providers through removal of some of the pricing transparency provided by these remedies. This is also consistent with our view that while at the margin we find SMP for BT, we observe that competition is increasing since the wholesale remedies seem to be working.

5.162 While we find a number of similarities in the way competition takes place in the supply of analogue lines and ISDN2 to businesses, we believe that at the margin BT does not have SMP in the supply of analogue lines while it has SMP in the supply of ISDN2 for the following reasons:

- The ISDN2 market is less attractive for BT's rivals to invest in going forward as it is in decline;
- The ISDN2 market is smaller in size and more expensive to reach in terms of marketing and sale costs as only a small share of businesses are interested in it; and
- The increased use of ISDN2 as a back-up line going forward means expected future revenues (from access and calls) when winning a new customer are lower for ISDN2 than for analogue exchange lines.

### Hull area

5.163 In the March Consultation, we considered that KCOM had SMP in the ISDN2 market due to the lack of competitors and KCOM's high market share.

### Consultation responses

5.164 One stakeholder (KCOM) commented on the ISDN2 SMP assessment for Hull. KCOM stated that Ofcom had concluded that the prospect of significant entry in the ISDN market appears muted, particularly as this is a product nearing the end of its lifecycle with customers opting for alternative technologies to provide the functionality they require. For these reasons KCOM believe that the continued application of regulatory remedies is no longer justified.

5.165 KCOM also provided some updated information on ISDN2 channels as follows:

**Figure 5.10**

#### **KCOM ISDN2 channels and revenues**

	<b>Number of ISDN2 channels</b>	<b>% change over previous year</b>	<b>ISDN2 revenues (£000's)</b>	<b>% change over previous year</b>
<b>2005</b>	10490	-6%	1452	Not available
<b>2006</b>	9840	-6%	1540	6%
<b>2007</b>	9676	-2%	1610	5%

Source: KCOM

### Ofcom's response

5.166 KCOM faces no actual competition in the supply of ISDN 2 in Hull. The fact that ISDN products are nearing the end of their lifecycle as customers move to alternative technologies does not necessarily imply that the competitive constraints in the ISDN 2 market have increased. In particular, we note that KCOM's ISDN2 revenues have increased in recent years despite a fall in the number of ISDN2 channels provided. We do not have any compelling evidence to suggest that the competitive constraints will increase significantly over the forward looking review period. Accordingly, in our overall assessment, we remain of the view set out in the March Consultation that this market is not effectively competitive.

## Section 6

# Calls Markets – market power analysis

## Introduction

- 6.1 The purpose of this assessment is to determine the effectiveness of competition in the various fixed narrowband calls markets, both currently and in the foreseeable future. This assessment will inform our decision as to whether retail fixed calls markets are effectively competitive.
- 6.2 Where we find a market to be effectively competitive, the SMP obligations previously imposed must be withdrawn (see Section 8). However, our involvement in the retail market will continue through sector level retail regulation, such as the General Conditions on communications companies (see Section 7).
- 6.3 Where SMP is found, we are obliged to consider what remedial regulations may be required to address the competitive failure.

## Summary

- 6.4 We have concluded that in the UK (excluding Hull) no company has SMP in either the residential or business fixed narrowband calls markets.
- 6.5 We have concluded that in the Hull area KCOM holds SMP in both the residential and business fixed narrowband calls markets, though as set out in Section 7 we are open to further consideration on how remedies should be imposed.

## Our Approach

- 6.6 Our approach was the same as set out in Section 5. Many of the features of the calls market are common with the access market. In the analysis that follows, rather than repeat our access analysis we instead focus on supplemental evidence.
- 6.7 As noted in Section 5, because access and calls are closely linked in a number of cases the evidence we present relates to both products combined. Where this is the case the evidence is presented once in the access section to avoid repetition. For each calls market we consider separately the UK (excluding Hull) and the Hull area.

## Residential Market for calls

### UK (excluding Hull)

- 6.8 In the March Consultation we set out our view that BT does not have SMP in the fixed calls market for the following reasons:
- The wholesale remedies (e.g. WLR and CPS) have led to the development of products which enable competitors to replicate the services offered by BT without making significant infrastructure investments. This has lowered barriers to entry and growth.
  - New firms have entered and expanded in the market resulting in a fall in BT's market share.

- Some of the main competitors such as Sky are expected to rely increasingly on LLU during the review period to further reduce their costs and increase the competitive pressure on BT.
- Consumers are willing and able to switch provider (evidenced by the fall in BT's market share).
- Since RPCs were lifted the overall average increase in the phone bill has continue to fall in real terms.
- The overall cost of a fixed line access and calls package is comparable to similar OECD countries.
- Mobile calls represent a significant constraint for at least some types of calls and some consumers.

### **Overview of consultation responses**

- 6.9 A number of stakeholders made overarching comments in relation to the SMP assessment for the markets where we are proposing to deregulate – particularly relating to BT's market share. To avoid repetition, where these comments have been discussed in the sections above they are not covered again unless further discussion is warranted. Comments specific to the residential calls SMP assessment are covered below.
- 6.10 BT agreed with our SMP assessment. They commented that the wholesale remedies are sufficient which has resulted in plenty of choice for consumers and led to considerable levels of switching. They commented that prices have significantly declined since 2003.
- 6.11 Other stakeholders did not agree with our assessment – largely for the reasons set out in the residential analogue access section above. The main comment made was that BT's market share was indicative of SMP and stakeholders expressed concern that the market was not sufficiently competitive to justify full deregulation.

### **BT's market share**

#### **Ofcom's response**

- 6.12 As noted above, BT's market share is only one factor in the SMP assessment and a high market share alone not sufficient to conclude that SMP is present. When set against the other factors considered as part of the SMP assessment we believe that the evidence points to BT no longer having SMP – for further discussion see paragraphs 5.31-5.44 above.
- 6.13 Since the March Consultation was published we have updated the market share information, which is shown below.

**Figure 6.1**

#### **Updated market shares of residential fixed narrowband calls (geographic, international and call to mobile)<sup>67</sup>**

	Volumes BT	Virgin Media	Other fixed	Revenues BT	Virgin Media	Other fixed
2003	71%	18%	11%	69%	19%	12%
2004	65%	19%	17%	63%	20%	17%
2005	59%	19%	22%	56%	20%	24%

<sup>67</sup> Original information was provided in Table 6.1 of the consultation.



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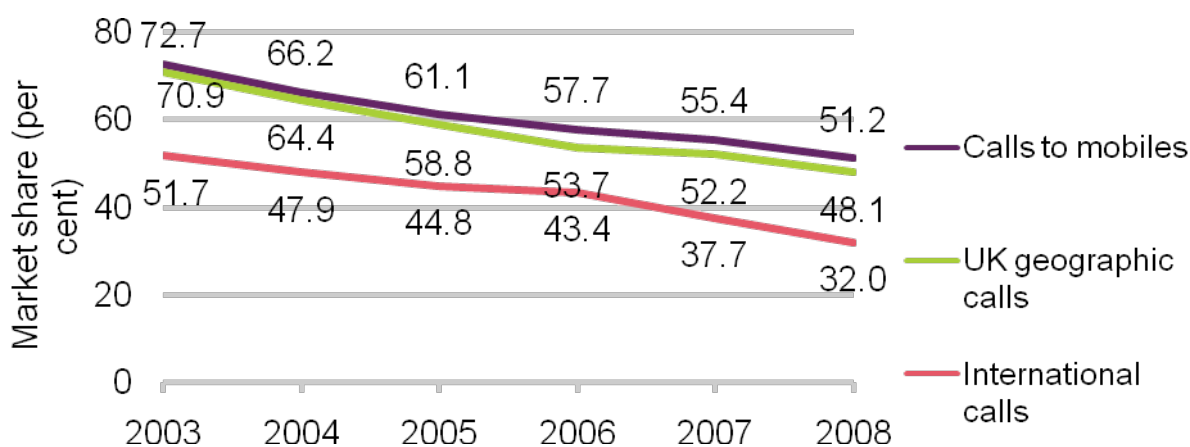
2006	54%	20%	26%	54%	19%	27%
2007	52%	18%	30%	55%	17%	27%
2008	48%	18%	35%	52%	17%	31%
2008 Q1	49%	18%	32%	51%	18%	31%
2008 Q2	47%	17%	36%	52%	17%	31%
2008 Q3	48%	17%	35%	52%	17%	31%
2008 Q4	47%	17%	35%	52%	17%	31%
2009 Q1	46%	17%	37%	51%	17%	32%

Source: Ofcom/operators

- 6.14 The information shows that BT's market share of volumes and revenues has decreased over 2008 relative to 2007. We noted in the residential access section above that BT has continued to lose market share in exchange lines through 2009 (e.g. as competitors like Sky sell into their existing customer base), and we would expect the market share in calls to follow this trend (as customers who move their line to an alternative Communications Provider will in virtually all cases also move their calls).
- 6.15 The Figure below shows that BT's market share for all residential call types has fallen since 2003.

Figure 6.2

BT share of residential retail voice call volumes, by type



Source: Ofcom/operators

### BT's profitability

#### Consultation responses

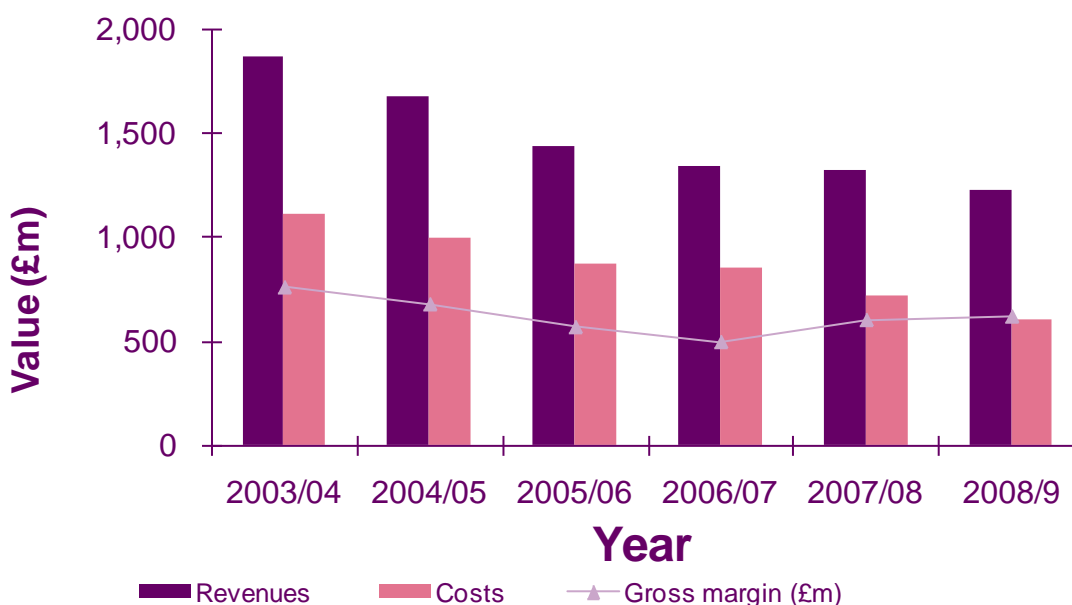
- 6.16 COLT commented that Figure 6.3 in the March Consultation (which shows BT's gross margin through time) shows an upturn in the final year (2007/8). COLT commented that this increase could be a one off or a result of BT's ability to profitably raise prices above the market level.

## Ofcom's response

- 6.17 An examination of the gross margin information shows that BT's total revenue from SMP call markets has been falling since 2003/4. BT's gross margin increased in 2007/8 because costs decreased by more than revenues (total costs decreased by £128m and revenues decreased by £23m<sup>68</sup>).
- 6.18 We have updated gross margin data from BT for 2008/9 which we present below<sup>69</sup>.

**Figure 6.3**

### Residential call markets – revenues, costs and returns from 2003/4 to 2008/9



Source: BT regulatory accounts

- 6.19 The Figure shows that BT's revenues have continued to fall and gross margin has increased only slightly in 2008/9. Again, it appears that BT's ability to maintain gross margin is driven by a proportionately larger decrease in costs rather than rising revenues.
- 6.20 We have examined the costs reported in BT's regulatory accounts in more detail. Across the residential local, national, IDD category A and call to mobile call categories in aggregate there was a £116m decrease in total costs in 2008/9 versus 2007/8<sup>70</sup>. £72m of this arose from reduced wholesale charges and out-payments (62% of the total). This will reflect a decrease in the volume of calls provided by BT. The decrease in out-payments for call to mobile will also reflect reduced mobile termination rates. The third

<sup>68</sup> Figures exclude IDD category B and operator assisted calls.

<sup>69</sup> In light of the 2009 consultation and statement on changes to BT and KCOM's regulatory financial reporting, for 2008/9 BT was not required to report international direct dial category B or operator assisted calls due to the small size of these markets (refer to [http://www.ofcom.org.uk/consult/condocs/btkcom09/statement/btkcom\\_statement.pdf](http://www.ofcom.org.uk/consult/condocs/btkcom09/statement/btkcom_statement.pdf), section 4). These call types have been removed from the previous year's Figures to ensure the time series is consistent.

<sup>70</sup> Excludes roundings.

largest contributor was general management which contributed £14m (or 12%) to the cost reduction. Messaging, other costs and marketing and sales contributed £28m combined to the reduction. This evidence suggests that BT has maintained profitability by reducing costs. Nonetheless it is difficult to draw strong conclusions from these gross margin data as, from an economic point of view, the cost reductions could reflect a decrease in economic investment (e.g. subscriber acquisition costs) that should be amortised rather than treated as a current costs and fully expensed.

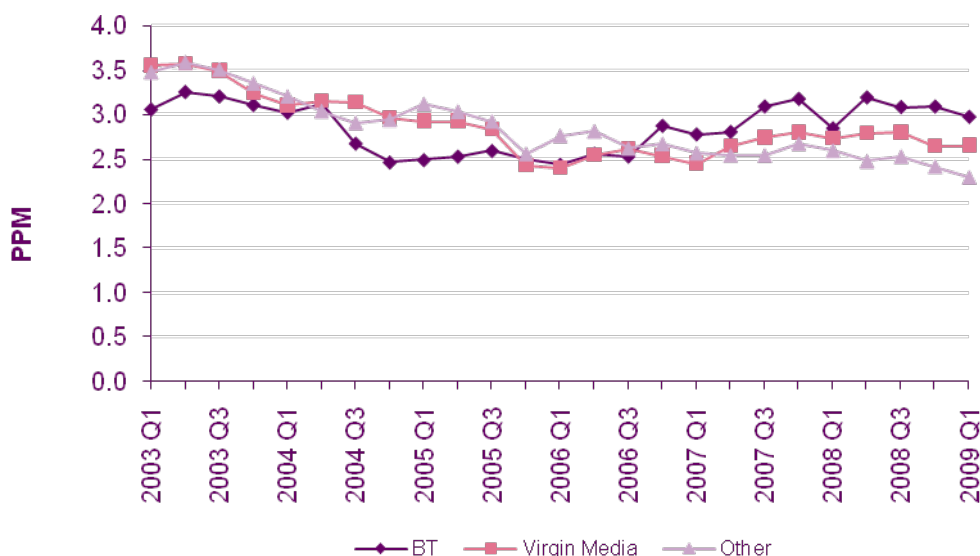
- 6.21 BT's revenue per minute (as shown in Figure 6.4 below) has declined over 2008/9 which, again, suggests that the ability to maintain gross margin is due more to cost reductions than increased prices.
- 6.22 As noted in the residential access section above, a further factor which has helped BT to maintain gross margin in the face of falling call volumes is that customers have tended to migrate to higher value call packages i.e. packages with a higher fixed monthly costs and more inclusive minutes. This would appear to reflect customer choice as to which package offers optimal value.

### **BT's pricing**

#### **Consultation responses**

- 6.23 COLT commented that since 2007 BT's share of revenues has been higher than their share of volumes which indicates that BT is able to charge a price premium. They noted that until 2006 the reverse was true and BT's share of volumes was higher than their share of revenues. COLT contended that the ability of BT to charge a price premium despite falling market share countered the assumption that BT does not have market power.
- 6.24 In Figure 6.4 of the March Consultation (updated and shown below) we presented BT's revenue per minute (RPM) for residential calls. COLT commented that we do not discuss SMP as an explanation of BT's ability to raise prices above the market level. Also in relation to Figure 6.4, Sky commented that despite the entry of new operators BT has been able to maintain its prices at a relatively stable level, indicating an ability to act without regard to its competitors.

**Figure 6.4**  
**Revenue per minute – geographic, international and call to mobile**



Source: Ofcom/operators

### Ofcom's response

6.25 We explained in paragraphs 6.34-6.49 of the March Consultation a number of reasons to explain why BT's RPM could have risen since 2006 including that we would expect BT to have a first mover advantage in the market and that BT has an established brand. A price premium for the first mover is consistent with a competitive market where rivals need to offer a discount to compensate for the switching costs incurred by subscribers for a relatively homogenous product<sup>71</sup>. In addition, the RPM on calls cannot be considered in isolation from pricing strategies for the products they are sold with. For example, Communications Providers might strategically charge a lower price for calls to drive demand for related products meaning it is difficult to draw comparisons of RPM across different providers.

6.26 In addition, the analysis of BT's pricing changes since the RPCs were lifted shows that the total phone bill has increased by less than RPI (paragraph 6.46 of the March Consultation).

### Use of survey data

#### Consultation responses

6.27 COLT commented that Ofcom's analysis of sensitivity to price changes (paragraphs 6.23-6.28 of the March Consultation) was based entirely on survey data where customers were asked how they would respond to a price change. COLT noted that such surveys are always likely to overstate customers' willingness to switch/reduce calls and it would be better for Ofcom to use statistically valid research data of consumer behaviour in response to a price change. Sky also commented that we placed a different

<sup>71</sup> This assessment is also relevant for the business calls market below.

emphasis on survey evidence presented in the pay TV review due to concerns that it might be affected by cellophane fallacy and hypothetical bias (we have discussed this in the access section above).

- 6.28 COLT commented that the March Consultation showed that BT lost 17% market share when its prices were below the average (i.e. from 2003-2006) but only 7% since its prices moved above the average (Figure 6.1). COLT considered that this did not support the results of the market survey and calls into question our reliance on survey data to assess market power.
- 6.29 COLT further commented on paragraph 6.25 of the March Consultation which reported that the survey evidence showed BT customers to be slightly more price sensitive than those of their rivals. COLT asked whether this result was statistically significant and also commented that the information on market share appeared to contradict this finding by showing that BT's customers are prepared to pay a premium over the average price.

### **Ofcom's response**

- 6.30 We have commented on the use of survey data in the residential access section above and addressed Sky's points regarding the different emphasis placed on survey data in the pay TV and retail narrowband reviews in paragraphs 5.73--5.78. To reiterate, we have used the consumer survey evidence as complementary evidence to inform our conclusions on SMP rather than relying on this information to draw conclusions.
- 6.31 COLT commented that the survey evidence was contradictory because it appears that BT's customers are prepared to pay a price premium and at the same time are more price sensitive. In fact the evidence may reflect the heterogeneity of BT's customers. There is likely to be a subgroup of customers who have a strong preference for BT and are willing to pay a price premium. In addition, there is also likely to be a segment that is highly price sensitive. The churn figures presented above suggest that a significant portion of BT's customers are willing and able to switch.
- 6.32 Our comment in paragraph 6.25 of the March Consultation which discussed the price sensitivity of BT's customers relative to their rivals was intended to be a descriptive comment to which we do not attach statistical significance.

### **Porting charges**

#### **Consultation responses**

- 6.33 Sky commented that the current porting charges favour BT. Under the current fixed number portability arrangements calls to ported numbers are typically routed by the originating Communications Provider to the original number range holder (donor network) who will then onward route the calls to the network to which the number was ported (the recipient network). The donor network is entitled to charge the recipient network for the cost of onward routing. Because an LLU operator will typically port their customer's telephone number from BT's network to their own, this means that an LLU operator effectively returns a proportion of their wholesale geographic termination revenues for calls to these customers back to BT as compensation for the routing of ported calls over BT's network.
- 6.34 Sky argues that as BT is a net exporter of numbers to other operators it is in a better position than other operators. They suggest that lower call margins for non-BT terminating networks can feed through to have adverse consequences for retail competition.

## Ofcom's response

- 6.35 Number portability is an important feature to encourage switching and competition in this market. New entrant Communications Providers, in particular, benefit from number portability because it reduces the barriers to switching and makes it easier to 'win' new customers with attractive deals.
- 6.36 Onward routing of ported numbers results in additional conveyance and transmission costs for the donor network and under the current mechanism the recipient operator is charged to cover these costs. It is beyond the scope of this review to consider the policy underlying this decision<sup>72</sup>. We recognise that the cost recovery mechanism reduces the revenues earned by the recipient network for calls to customers with ported numbers. However, we do not consider that BT derives SMP from this. Even under the current arrangement BT has lost substantial market share (as discussed above) which indicates that the cost of number portability is not a substantial impediment to competition. The main LLU operator (TalkTalk) has grown substantially since the last review and is one of BT's largest competitors.

## Calls to mobile and pass through of changes in the mobile termination rate

### Consultation responses

- 6.37 T-mobile commented specifically on the calls to mobiles sub segment of the calls market. They noted that the price of calls to mobiles increased after 2007 when the new mobile call termination price control came into place. They commented that this is counter-intuitive and implies that the reductions in mobile termination rates have only lead to an increase in BT's margins on these calls, as opposed to any direct consumer benefit. They thought that Ofcom should investigate this area and ensure that the price of calls from fixed to mobile is linked directly to the regulated mobile termination rate.
- 6.38 The respondent argued that there is no competitive pressure on BT or other fixed operators to bring down the price of fixed to mobile calls and that more prescriptive regulation on BT was necessary.

## Ofcom's response

- 6.39 As discussed in the March Consultation in the definition of the calls market, customers now tend to buy a calls package which includes some inclusive minutes. Up to the present time, competition has focussed on bundles of inclusive minutes to fixed locations, with mobile, some NTS and international calls outside those bundles. Accordingly, fixed providers will structure their rates for out of bundle call types to ensure that their headline offering is attractive<sup>73</sup>. This structure and practice is following the lead of mobile offerings (although mobile companies are also able to include mobile calls in the bundles). This means margins are lower for calls types that represent the focal point of competition and higher for calls that are not included in the headline bundles. This means that while margins differ across different call types it is meaningful only to look at margins across all call types as we discuss above.
- 6.40 More recently competition has started to focus more strongly on the price of mobile calls with BT offering a 'mobile add on' which gives unlimited calls to mobile at 7ppm<sup>74</sup> in

<sup>72</sup> The case for direct routing of calls to ported numbers is being considered as part of a separate project see [http://www.ofcom.org.uk/consult/condocs/gc18\\_routing/routing.pdf](http://www.ofcom.org.uk/consult/condocs/gc18_routing/routing.pdf).

<sup>73</sup> By headline offering we mean the offer that is routinely advertised in the national marketing campaigns.

<sup>74</sup> An 8p call set up fee applies.

return for a £1.50 per month flat fee. Virgin media offer a ‘talk mobile’ package for £1.50 a month which provides a 25% discount on standard mobile rates<sup>75</sup>, and TalkTalk also offer a ‘mobile boost’ package which offers a discount on mobile calls in return for a flat monthly fee.

- 6.41 For BT’s customers the overall phone bill has in fact increased by less than inflation since the RPCs were lifted (see Annex 6 of the March Consultation) and the reduction in mobile termination costs has contributed to this outcome. As shown in Figure A5.8 of the March Consultation BT’s revenue per minute for residential calls to mobiles is lower than that of Virgin Media and those charged by other fixed providers, which suggests that, on average, BT’s prices are lower than other providers.

### **Hull area**

- 6.42 In the March Consultation we set out our view that KCOM does have SMP in the fixed calls due to the muted prospects for entry and high market share of KCOM.
- 6.43 With respect to the three tests for *ex ante* competition in relation to the Hull area, we are of the view that the market does not tend toward competition due to the presence of barriers to entry and a lack of competition in the market. Therefore the Commission’s first two tests are not satisfied.
- 6.44 In addition, we consider that competition law alone is not enough to address the SMP in this market as the entry barriers are too high and have proved to be effective in excluding competition. Therefore it is appropriate to impose *ex ante* regulation on KCOM in this market.

### **Fixed-mobile substitution in Hull**

#### **Consultation responses**

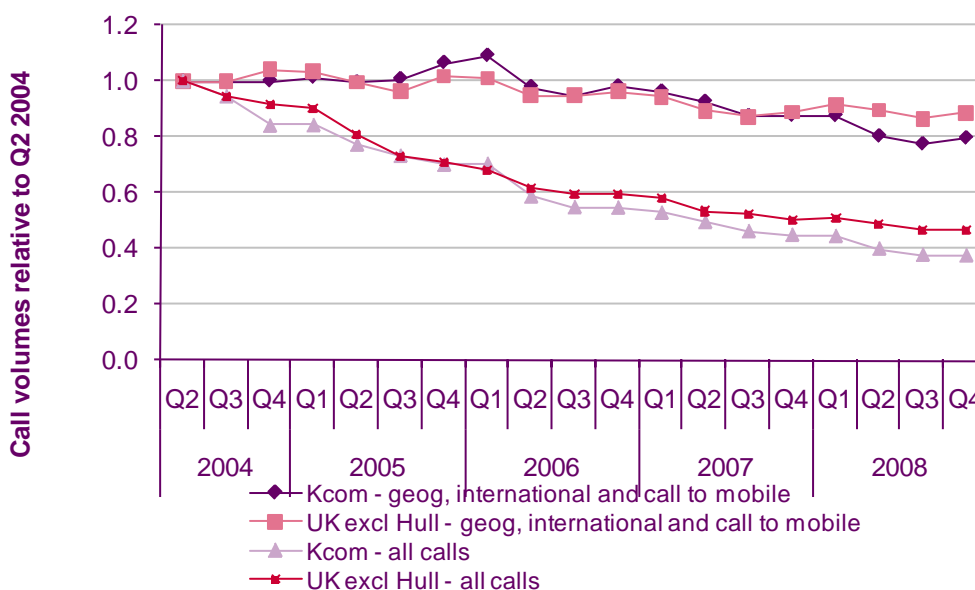
- 6.45 Only KCOM commented on the SMP analysis in Hull. KCOM disagreed with our conclusion on the basis that mobile substitution in the Hull area was likely to be more pronounced than the rest of the UK. KCOM considered that Ofcom had not fully explored the real extent of this substitution, particularly in light of the limited range of fixed alternatives actively marketed to Hull customers. As a result KCOM believe that the degree of fixed to mobile substitution in the Hull market may well be higher and more constraining than is the case in the rest of the UK. KCOM noted that at paragraph 6.29 of the March Consultation we stated that “most consumers want the same provider for both lines and calls”, however, there appears there was no specific research carried out on consumer preferences or the reaction to a rise in call prices in the Hull market. KCOM suggested that there is a likelihood that an increase in call prices would result in further mobile substitution.

#### **Ofcom’s response**

- 6.46 In paragraph 6.17 of the March Consultation we noted that call volumes have fallen at a slightly faster rate in the Hull area than in the rest of the UK in 2008. This is shown in the Figure below.

<sup>75</sup> An 8.8p call set up fee applies.

**Figure 6.5**  
**KCOM versus rest of UK – residential call volumes over time**



Source: KCOM/Ofcom/Operators

- 6.47 We accept that there is possibly a higher level of mobile substitution in Hull relative to the rest of the UK. The volume of geographic, international and calls to mobiles has declined by 20% in Hull between Q2 2004 and Q4 2008 and by 11% across the rest of the UK. However, the gap between the rest of the UK and Hull has opened up over 2008 and it is difficult to draw definitive conclusions based on a few quarters of data. We do not believe the level of substitution is substantial enough to 1) include mobile calls within the fixed calls market in Hull (refer to the section 4 of the March Consultation for our analysis on mobile substitution) or 2) mitigate KCOM's SMP in the fixed calls market. The reasons why we believe KCOM has SMP are set out in section 6 of the March Consultation.
- 6.48 We accept that the situation in Hull is somewhat different from the rest of the UK due to the absence of alternative fixed line providers. However, as discussed in Section 4, we do not think consumer preferences are significantly different relative to the rest of the UK. We agree that, as in the rest of the UK, there is a degree of substitution from fixed to mobile calls for some call types and this would be influenced in the event of increases in price of fixed calls. However, there is not sufficient evidence that this movement in Hull would be substantially higher than the rest of the UK.

### **Barriers to entry in Hull**

#### **Consultation responses**

- 6.49 KCOM noted that wholesale remedies are in place in Hull should other Communications Providers wish to offer services to customers. KCOM does not agree with any suggestion that there remain significant barriers to entry. KCOM stated that the relatively small size of the Hull market offers competing providers access to the market for a comparably small investment, particularly where they can utilise wholesale products to provide call services. KCOM concluded that the threat of competitive entry is a very real constraint on their behaviour in the pricing of its retail call services. They do not believe



that the current regulatory remedies are justified or proportionate and, may act to place Hull customers at a disadvantage in terms of the choice of service packages which can be offered.

### **Ofcom's response**

- 6.50 The lack of actual market entry in the Hull area (e.g. no WLR/CPS providers) suggests that barriers to entry exist. For the reasons set out in paragraphs 5.106-5.109 above we believe this supports our SMP finding.
- 6.51 However, we are mindful that Hull customers should not be at a disadvantage in terms of the service packages which can be offered. We consider this in more detail in Section 7 below.

## **Business market for calls**

### **UK (excluding Hull)**

- 6.52 In the March Consultation we set out our view that BT does not have SMP in the fixed calls market for the following reasons:
- The wholesale remedies have led to the development of products which enable competitors to replicate the services offered by BT without making significant infrastructure investments. This has lowered barriers to entry and growth.
  - New firms have entered and expanded in the market resulting in a fall in BT's market share.
  - Relaxation of the SMP regulations in 2007 for large businesses appears to have been successful.
  - Recent market research has shown that businesses are aware of alternative providers and appear willing to switch.
  - Mobile calls represent a significant constraint for at least some types of calls and/or at least some business customers.

### **Overview of Consultation responses**

- 6.53 A number of stakeholders made overarching comments in relation to the SMP assessment for the markets where we are proposing to deregulate – particularly relating to BT's market share. To avoid repetition, where these comments have been discussed in the sections above they are not covered again unless further discussion is warranted. Comments specific to the business calls SMP assessment are covered below.
- 6.54 BT agreed with our analysis that it does not have SMP in the business calls market. BT believes that all sizes and sectors of the UK business market are fully and intensely competitive, which has resulted in BT's falling market share, and the trend is expected to continue. In addition, BT supported our analysis that there are sufficient wholesale remedies in place giving businesses plenty of options to choose from in terms of CPS, WLR, LLU and mobile operators. They further commented that customers are fully aware of competing Communications Providers and their ability to switch suppliers.
- 6.55 Other stakeholders disagreed with our assessment – largely for the reasons set out in the residential/business analogue access and residential calls sections above. The main comment made was that BT's market share was indicative of SMP and stakeholders expressed concern that the market was not sufficiently competitive to justify full deregulation

## **BT's market share**

### **Ofcom's response**

6.56 We have discussed why BT's market share is not indicative of SMP in length above. In any case, BT's market share (both volumes and revenues) is lower than 50% in the business calls market. Since the March Consultation was published we have updated the information on market share, which is shown below.

**Figure 6.6**

### **Updated market shares of business fixed narrowband calls (geographic, international and call to mobile)<sup>76</sup>**

	Volumes BT	Virgin Media	Other fixed	Revenues BT	Virgin Media	Other fixed
2003	42%	7%	51%	50%	7%	43%
2004	41%	7%	53%	48%	7%	46%
2005	40%	7%	53%	45%	6%	49%
2006	39%	7%	54%	45%	6%	49%
2007	39%	6%	55%	45%	5%	49%
2008	38%	6%	56%	44%	5%	51%
2008 Q1	39%	6%	55%	45%	5%	50%
2008 Q2	39%	6%	55%	45%	5%	50%
2008 Q3	38%	6%	56%	44%	5%	51%
2008 Q4	38%	6%	56%	44%	5%	51%
2009 Q1	36%	6%	57%	43%	5%	52%

Source: Ofcom/operators

6.57 The information shows that BT's market share of volumes has remained at less than 40% over 2008 while the share of revenues has stayed at around 44%.

## **BT's pricing**

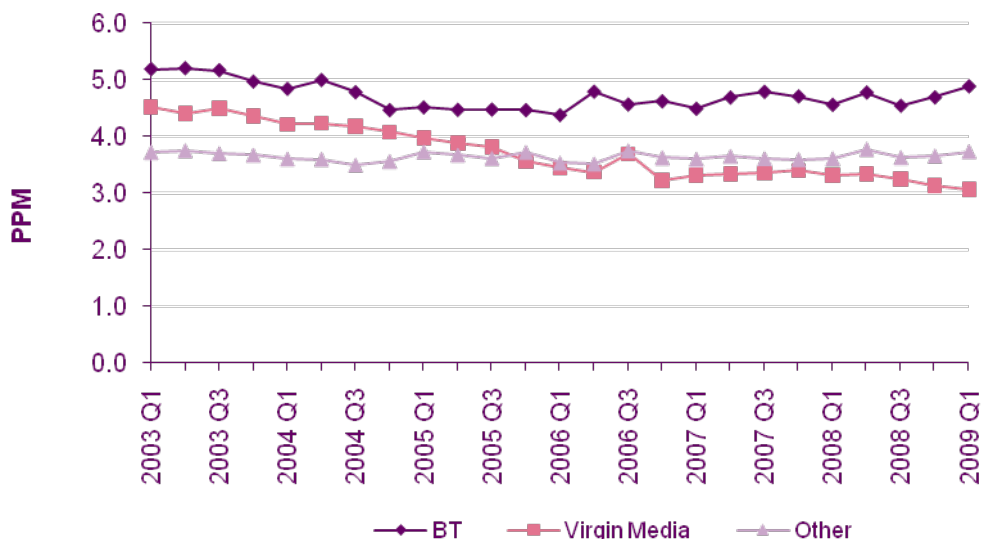
### **Consultation responses**

6.58 COLT commented that BT is able to sustain a price premium because their share of revenues is greater than their share of volumes. They consider that ability to command such a premium for an undifferentiated product should be taken as evidence of SMP.

6.59 COLT commented that in the discussion of Figure 6.10 of the March Consultation (updated and shown below) we do not discuss SMP as an explanation for BT's ability to achieve a higher RPM.

<sup>76</sup> Original information was provided in table 6.7 of the consultation.

**Figure 6.7**  
**Revenue per minute – business geographic, international and call to mobile**



Source: Ofcom/operators

### Ofcom's response

- 6.60 We noted in the residential calls discussion above that a price premium is not necessarily evidence of market power. Even if the products supplied by different Communications Providers are similar, rival providers have different business models which can lead to different pricing strategies in a competitive market.
- 6.61 We discussed in paragraphs 6.76-6.79 of the March Consultation a number of reasons why BT might be able to charge a price premium relative to other providers. A particular feature of the business market is that some organisations have multiple suppliers and may retain a few lines with BT for contingency/resilience reasons. BT might be able to charge a premium for the perceived reliability of its services but actually earns limited revenues from these organisations.
- 6.62 Furthermore, as discussed in the residential calls section above we would expect BT to have a first mover advantage in this market. BT's brand presence might allow it to charge a premium over less well established rivals. This would be expected to diminish to some degree over time but does not itself indicate SMP or act as a substantial barrier to competition.
- 6.63 We note above that BT's revenues for business calls have fallen since the last review and BT has a relatively low market share (i.e. less than 50%), these factors do not suggest that BT is able to exploit a dominant position.

## Information on switching

### Consultation responses

6.64 COLT commented that Ofcom had presented little quantitative evidence on the switching behaviour of SMEs.

### Ofcom's response

6.65 We focused our switching evidence on the behaviour of residential consumers because businesses are likely to be more sophisticated and thus be aware of alternative providers. In addition, it would be a significant exercise to collect sufficiently reliable data from SMEs to undertake a detailed switching analysis.

6.66 We noted in the business analogue access section above that BT's churn in exchange lines was ([redacted]) in the 12 months to May 2009. While this will be partly driven by a decline in market size, it does indicate that businesses are switching from BT to other providers.

## BT's profitability

### Consultation responses

6.67 COLT commented that information on gross margin data was not presented so they cannot tell from the March Consultation document whether BT's margins on business calls are increasing.

### Ofcom's response

6.68 For the residential markets we used information in BT's regulatory accounts to assess gross margin. BT is not obliged to report on business market profitability in its regulatory accounts. However, since the March Consultation we have formally requested information on revenues and return on sales from BT for the business calls<sup>77</sup> market, which is presented below.

### Figure 6.8

#### Business calls – revenues, costs and returns from 2004/05 to 2008/09<sup>78</sup>

[redacted]

Source: BT

6.69 The Figure shows that call revenues have declined over time. This reflects the general decline in the volume of business calls and the decline in BT's market share. Since 2004/5 BT's revenues have fallen by [redacted] and their costs by [redacted], resulting in a significant reduction in gross margin of [redacted].

<sup>77</sup> Includes local, national, international and inland calls BT to mobile for business PSTN, ISDN2 and ISDN30.

<sup>78</sup> Redacted as the information is commercially confidential.

**Hull area**

- 6.70 We consider that KCOM has SMP in the business fixed calls market for the same reasons set out for the residential calls market (see paragraphs 6.42 to 6.44).

**Consultation responses**

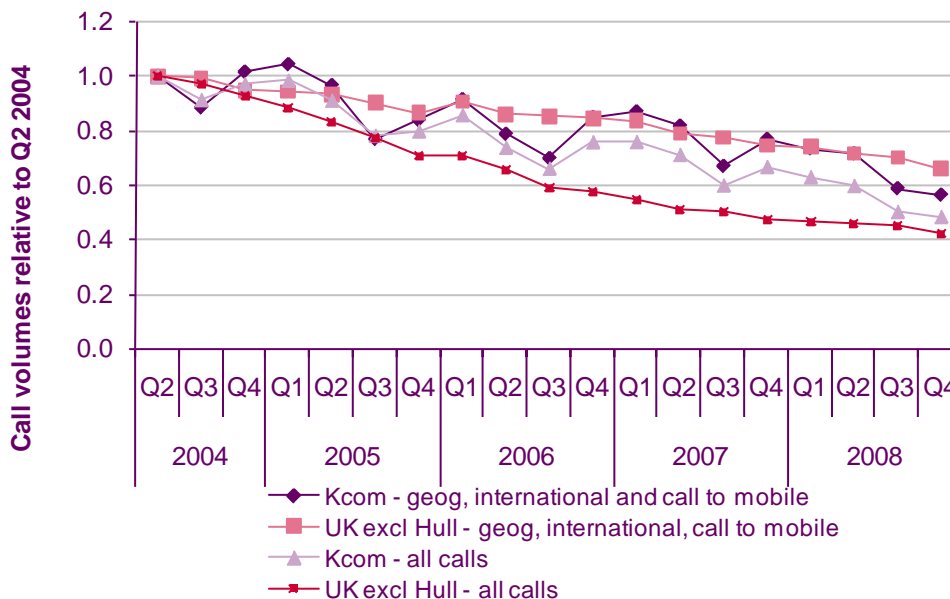
- 6.71 Only KCOM commented on the SMP assessment for the business calls market in the Hull area. KCOM did not agree with our analysis.
- 6.72 KCOM noted that by Q3 2008 there had been a decrease of approximately 40% in the volume of geographic, international and calls to mobile in the Hull area relative to Q2 2004. KCOM commented that this represented a significant decrease and clearly points to a degree of substitution by business call users. Furthermore, during 2008 KCOM's business call volumes have shown a marked decrease compared to the rest of the UK with a differential of close to 10%. KCOM believes this differential requires further investigation.
- 6.73 KCOM thought that we had substantially underestimated the overall size of the business calls market in Hull. Our analysis had concluded that fixed calls to business customers via indirect access and alternative means, such as leased lines, accounted for a small proportion of the market. This assessment had been reached on the basis that information provided by KCOM on average monthly minutes from February 2008 to January 2009 shows that indirect access minutes (both residential and business) were 10% of total outbound revenue. However, KCOM noted in their response that their assessment was that, for the same period, business indirect access minutes accounted for 26% of total outbound business minutes (excluding local).
- 6.74 Furthermore, KCOM noted that this did not take account of business calls which are carried over leased lines supplied to customers by either KCOM or an alternative provider. In the statement on the Business Connectivity Market Review published in December 2008 Ofcom concluded that KCOM no longer had SMP in the retail market for low bandwidth TI leased lines based largely on KCOM's low market share of 25%. KCOM believe that this finding also has a knock-on effect in the context of the market for narrowband business calls.
- 6.75 KCOM have provided further information which suggests that, after accounting for indirect access providers and leased lines which enable calls to bypass the KCOM PSTN in the Hull area, their market share of calls originating in Hull is actually around 57%.

**Ofcom's response**

- 6.76 We agree that there has been substitution away from business calls since 2004 e.g. to mobile calls and email. This trend is apparent both in Hull and across the rest of the UK as shown in the Figure below.

Figure 6.9

## KCOM versus rest of UK – business call volumes over time



Source: KCOM/Ofcom/Operators

- 6.77 Over the latter part of 2008 KCOM appears to have lost call volumes (geographic, international and calls to mobile) at a higher rate than the rest of the UK. However, it is difficult to form definitive conclusions based on two quarters of data.
- 6.78 We note that there are Communications Providers offering business calls via leased lines in the Hull area. While it is possible that leased line calls are exerting some competitive pressure on KCOM business calls, in any case, this is only likely to be evident for larger businesses where leased lines are a viable alternative.
- 6.79 KCOM have also identified a high use of indirect access (“IA”) call services for non local calls. We accept that this does offer a competitive alternative to KCOM calls, but its high use is itself likely to be a reflection of the lack of full competition. Also the IA market is constrained by KCOM packages which have inclusive calls within the base rental. It is not at all clear that IA would be an effective future competitive constraint.
- 6.80 We are open to considering whether competition in the market for larger businesses is sufficiently developed to warrant deregulation. However, we do not have sufficient information currently to decide whether deregulation is appropriate at this time and what form it should take. However, we are minded to assess this as part of a further review, see Section 7.

## Section 7

# Market Remedies and Impact Assessment

## Introduction

- 7.1 We set out our proposals on market remedies along with a full impact assessment in Section 7 of the March Consultation Document. In this section we consider stakeholder responses on the remedies, impact assessment and concerns around potential risks to competition from current and proposed contract terms and migration processes.
- 7.2 We also set out our conclusions on the remedies that we will establish for the SMP findings in Sections 5 and 6.

## Summary

- 7.3 BT's SMP in ISDN2 market: We have decided to rely solely on the wholesale remedies imposed in the Wholesale Market Review.
- 7.4 KCOM's SMP in all narrowband markets (excluding ISDN30): we have decided to continue the existing remedies:
- No undue discrimination; and
  - Price publication.
- 7.5 We may need to further review these remedies in the Hull area to consider:
- Options to allow the introduction of bundles of residential services which would include SMP narrowband market services; and
  - Modifications of the application of SMP remedies for segments of the business calls markets, should evidence be presented of higher levels of competition for those segments.
- 7.6 In addition, we confirm the need to review the impact of automatic rolling contracts and alternative migration processes on competition in the narrowband market. We note that should such contracts or processes be found to have an impact on competition then either measures will need be taken to address this impact or we may need to reconsider our SMP findings set out in this statement.

## Remedies for BT's SMP in ISDN2

- A1.1 In the March Consultation we considered the effectiveness of the current retail remedies on ISDN2. We considered that the existing remedies may in effect be counterproductive as the conditions within this, largely static, market are conducive to price following. We were concerned that the price publication and non-discrimination requirements would likely dull the incentive for BT to compete strongly as any price cuts only ensure that the total revenue in the market would reduce without delivering BT any competitive advantage or attracting new customers into the market.
- 7.7 The March Consultation considered the option of more intrusive remedies (i.e. price controls) but we consider that this would risk discouraging innovation in the markets. Instead, we recommended the removal of all specific retail controls, relying on wholesale

remedies alone for the reasons set out in paragraph 7.33 of the March Consultation ie that the existing remedies did not appear to be continuing to contribute to improvement in competition in the market and, instead, appeared to be inhibiting full price competition. This approach was consistent with Article 17 of the Universal Service Directive and section 91 of the Communications Act, which both restrict the imposition of regulatory controls on retail services to situations where obligations that could be imposed under the Access Directive or Framework Directive would not, in themselves, be sufficient to achieve the objectives set out under Article 8 of the Framework Directive.

### Consultation responses

- 7.8 Some stakeholders were concerned about the removal of retail remedies. The particular concerns were around the fitness for purpose of the existing wholesale remedies and the risk of margin squeeze.
- 7.9 The FCS said “continuing delays in delivery of fully fit-for purpose services via WLR3 mean that there is still no true equivalence in this area with consequences for effective competition. There is also a replicability issue with regard to e.g. site offices.” COLT noted that “Although BT has been able to raise prices and margins on ISDN2 ..., COLT would be concerned that the removal of all retail regulation could allow BT to effect an anti-competitive margin squeeze by reducing its retail prices whilst maintaining wholesale prices. We therefore prefer to maintain the existing obligations, or at least the continued obligation of price publication which allows competitors to monitor, at least prima facie, whether a margin squeeze is taking place”.

### Ofcom's response

- 7.10 While we accept there will continue to be a need to improve the ISDN2 WLR product, we consider that the product is sufficiently fit-for-purpose to allow competitors to compete with BT equally at the retail level (we understand that the next WLR3 release, R1100, on 29<sup>th</sup> September should address most of the current concerns). We, therefore, consider that there is equivalence in access to ISDN2 at the wholesale level, which is an important consideration in our reliance on wholesale remedies.
- 7.11 Communications Providers can provide to site offices using WLR3 (not available on WLR2) though each order requires a full survey and the construction costs are treated differently from permanent lines. This is the same for BT Retail as they will now be using WLR3 not BT Classic.
- 7.12 With respect to the risk of price squeeze, as discussed in the March Consultation, our current concern is that, despite the entry of new competitors and a decline in fixed wholesale costs in 2004, there is little indication of improved prices to end customers. BT has had price flexibility yet not chosen to exercise this.
- 7.13 We think that the removal of the existing remedies will open the prospect of greater price competition. In particular, the current price publication remedy supports the maintenance of existing margins for BT Retail and other Communications Providers rather than encouraging competition for the benefit of customers. We remain conscious of the possibility of price squeezing as we are with all products BT sells both at the retail and wholesale level.
- 7.14 Our SMP finding indicates that BT retains a dominant market position in the supply of these services and allows us to intervene in the event of concerns over potentially abusive conduct.



7.15 We, therefore, consider it appropriate to rely solely on the wholesale remedies for the ISDN2 market.

### **Remedies for KCOM SMP markets**

7.16 KCOM's SMP operations in Hull are all subject to two SMP remedies:

- No undue discrimination; and
- Price publication.

7.17 In the March Consultation we observed, that while these remedies have not led to a significant entry by retail competitors in the access markets, there has been some market entry in the calls markets.

7.18 We discussed the encouragement of competitor entry through wholesale products in more detail in the Wholesale Narrowband Services Market Review. In the March Consultation we considered the following options in respect of retail remedies:

- Option 1 – Remove existing remedies and rely on wholesale remedies;
- Option 2 – Maintain the existing remedies; or
- Option 3 – Introduce more direct intervention on pricing.

7.19 Our assessment was that, given the lack of competitive entry, the case for reliance on wholesale remedies would not be appropriate. Wholesale remedies have clearly, so far, not enabled or encouraged sufficient competitive entry. Accordingly we consider that the wholesale remedies do not allow us to fully perform our duties under Section 4 of the Communications Act. In particular, the protection against abuse of its SMP position as provided by the price publication and non-discrimination remedies (which ensure that KCOM's actions are transparent) remains essential.

7.20 The argument for price controls rested on a consideration of whether the Hull markets are ever likely to see new competitor entry. Any price controls on the incumbent also constrains the viable prices for a rival entrant and thus would necessarily increase the barrier to entry.

7.21 At present, KCOM charges are not noticeably out of alignment with national charges. This is possibly due to the potential threat of price controls, the risk of encouraging market entry by exposing high profits and/or the reaction of its customer base/shareholders (an overlapping group). There is no reason to expect this to change (except with respect to bundles of products which we discuss separately below). Equally, it is not clear that price controls would lead to controls substantially below that which is currently being charged.

7.22 Given the lack of clear benefit from increased intervention, the costs of such an intervention and the continuing prospect of new market entry, price controls would not appear justified at this time.

7.23 We concluded that it was appropriate to continue with the existing remedies for all markets.

7.24 We did note, however, that there was potential complication with the retention of current remedies. We observed that our proposed deregulation of BT should encourage

competition in bundled offerings (i.e. narrowband and other services with pricing below the sum of the component service charges) in the UK (excluding Hull).

- 7.25 Such bundles are already offered by many Communications Providers in the UK (excluding Hull) and we can foresee the situation where the only consumers/business customers unable to benefit from such an arrangement would be Hull residents, unless new market entrants were to provide this.
- 7.26 We set out the following options to address this in the March Consultation, though we did not recommend any specific option. The options were:
- Option 1 – Allow the situation to evolve and restrict KCOM from bundling, thus encouraging entry by bundlers (including now BT);
  - Option 2 – Allow KCOM to offer a bundled product without specific further conditions;
  - Option 3 – Allow KCOM to offer bundled products but require referral of that product to Ofcom for consideration – with the aim of minimising the increase in barriers to entry.
- 7.27 Ultimately, each option would need to be assessed against our general duties to further the interests of consumers and citizens, having regard to choice, price and value for money for customers.
- 7.28 We have considered to what extent the current conditions prohibit bundling. While this is not explicit in the regulations, as noted in earlier reviews (most recently the Consent on Business Exchange Line Replicability, published 29 May 2007<sup>79</sup> (see Section 3)) Ofcom's current stated interpretation of the no undue discrimination SMP services condition, is that we assume that bundles of SMP and non-SMP products would be likely to be unduly discriminatory. Were we to allow KCOM to offer bundles without further regulations, we would need to re-examine how we applied this condition to these markets.
- 7.29 ERG common position on remedies is that specific requirements can be imposed under A17(2) USD to not unreasonably bundle services. This would be beyond the current conditions (it seems as though the non discrimination is being taken (currently by BT and KCOM) as a restriction on bundling). The Common position then goes on to suggest that where such a restriction could rule out "welfare enhancing bundles", an alternate condition could be imposed that an undertaking be obliged to report proposed new bundles to the NRA who would then judge whether they were anti-competitive.<sup>80</sup>
- 7.30 Clearly, as discussed by the ERG, NRAs should take into account the danger of prohibiting bundles which may increase welfare and that a blanket prohibition of bundles may rule out welfare enhancing bundles, balancing that against the welfare gains in preventing dominant undertakings from distorting competition in horizontally related markets. This consideration is also consistent with S4 of the USD which considers the need to balance promotion of competition and promotion of citizens' interests.
- 7.31 While this approach appears to allow the acceptance of bundles in principle, the difficulty is in setting criteria for their review which do balance consumer interest and competition effectively.

<sup>79</sup> <http://www.ofcom.org.uk/consult/condocs/draftconsent/statement/consent.pdf>.

<sup>80</sup> [http://www.erg.eu.int/doc/meeting/erg\\_06\\_33\\_remedies\\_common\\_position\\_june\\_06.pdf](http://www.erg.eu.int/doc/meeting/erg_06_33_remedies_common_position_june_06.pdf).

7.32 It may also be appropriate to link any development in this area to KCOM improvement in systems supporting retail competition.

### Consultation responses

7.33 Only KCOM responded in any detail on this discussion.

7.34 With respect to the analogue markets they suggested “there is the potential for a lighter touch regime to be imposed in the residential calls and access markets, particularly in the light of the effects noted above. Certainly, there has been no evidence of issues arising in terms of compliance with the current obligations or of any consumer harm.” They also noted that they “fully agree with Ofcom’s view that there is a need to ensure that Hull residents are not unduly disadvantaged compared to residents in the rest of the UK. However, we believe that they are being unduly disadvantaged as a result of Ofcom’s current interpretation of the undue discrimination obligation which assumes that bundles of SMP and non-SMP products would be likely to be unduly discriminatory.” They suggested that any potential future broadband USO would make the current situation untenable.

7.35 KCOM offered as an alternative approach to formal remedies “to explore the possibility of voluntary undertakings primarily designed to provide both consumers and other Communications Providers with an appropriate level of visibility and certainty regarding Kingston’s retail offerings:

- An undertaking to publish prices as currently required by the SMP conditions.
- An undertaking to benchmark prices against an identified BT entry level package and
- Not to increase prices above those benchmarks.
- An undertaking that taken together the elements of any package will not fall below cost. “

7.36 With respect to the ISDN Markets, because the prospect of significant entry in the ISDN market appears muted as this is a product nearing the end of its lifecycle and customers are moving towards alternative technologies, KCOM did not think that the continued application of regulatory remedies was justified.

7.37 As discussed in Section 6, KCOM have also highlighted differences in competition for business calls for companies of sufficient size to justify the use of leased lines for the provision of services.

### Ofcom’s response

7.38 As discussed in Sections 5 and 6 we do not consider that KCOM have put forward sufficiently strong arguments to justify a movement away from our SMP finding.

7.39 Equally given the lack of substantial change in the level of direct competition we consider that there is no evidence to support general deregulation or reliance on voluntary commitments.

7.40 That being said, as we noted in the March Consultation, we consider that in the interest of Hull consumers and businesses we should explore how the range of services offered to Hull customers could be expanded, to help ensure that those customers do not miss out on developments available to the rest of the country.

- 7.41 Similarly, we accept that there may be some merit in the argument KCOM have advanced that there are different competitive conditions for business calls for those companies of whose size and usage levels merit the leasing of dedicated communications lines.
- 7.42 There is an inherent difficulty in setting market regulations linked to business sizes because it is difficult to determine how to set the boundary. The current Replicability regulations for BT set a £1M communications spend level to ensure that the boundary was safely drawn. We propose, therefore, to continue our discussions with KCOM and other relevant stakeholders on this issue. If a clear case for some relaxation or modifications of the SMP conditions with respect to a subset of companies becomes apparent we would re-consult on this matter.

### **Potential threats to future competition – UK (excluding Hull)**

- 7.43 In the March Consultation we noted that even with the removal of SMP-related regulation, BT is and will remain bound by the General Conditions and Universal Service Conditions, in addition to non sector-specific consumer protection legislation which covers all providers.
- 7.44 In particular, we noted that Ofcom needs to monitor developments in contract terms and migration processes which could have a deleterious impact on competition. We specifically identified the introduction of automatic roll-over contract terms and any changes to regulations that would allow BT to discriminate between active and inactive customers, such as losing provider-led switching processes as potential areas for concern. For example, we may need to consider the implications of any proposals that would allow BT to target discounts to customers indicating an intention to leave.<sup>81</sup>
- 7.45 With respect to automatic roll-over contracts, we noted that we had set out some general guidelines on contract terms which apply to all Communications Providers based in the Unfair Terms in Consumer Contracts Regulations (“UTCCR”)<sup>82</sup>.

### **Overview of consultation responses**

- 7.46 There was a considerable degree of concern expressed by stakeholders over the issues of contract terms and changes to migration procedures.

### **Automatic roll-over contracts**

#### **Consultation responses**

- 7.47 With respect to contract terms a number of stakeholders argued that restrictive contract terms allow incumbents to leverage their market share and would act as a barrier to continued competition.
- 7.48 Cable & Wireless noted that “BT seem to be entrenching their market position and protecting their market share by requiring customers to sign up to extended rolling contract terms in order to receive ‘standard’ benefits and discounts. If customers don’t

<sup>81</sup> For example ‘losing provider led’ migration is the process by which the customer must contact the provider to notify them of his/her intention to move. In order to complete this move, as is the case for broadband, the customer must seek a Migration Authority Code (MAC). For those customers requesting a MAC, BT could identify those with an intention to switch and offer them bespoke rates.

<sup>82</sup> Ofcom Review of Additional Charges Statement Annex 1 sets out the guidelines (<http://www.ofcom.org.uk/consult/condocs/addcharges/statement/>).

accept BT's extended contract terms they face the prospect of paying higher charges and /or finding another supplier at short notice. If they do accept the extended contract term and later decide to switch supplier they face paying a high early termination charge."

7.49 A confidential respondent noted that rolling contracts were a market anomaly.

7.50 Sky said that:

"It is only as a result of BT's continuing SMP that it has been able to introduce rolling contracts of this nature (for example, BT has not introduced corresponding restrictions in its customer broadband contracts; nor have other fixed line operators in their customer contracts). Despite the inducement of a reduction in call package costs, such contractual terms are hardly representative of what would be expected in a market that is effectively competitive: allowing customers only a short window (as short as 6 days from receipt of a notification letter) within which to switch without contractual penalty, even if they have been a BT customer for a significant period of time, could only be introduced by a provider that had the ability to act independently of its customers and competitors. The effect of this is, as Ofcom itself recognises, designed to aid customer retention, by severely limiting a customer's opportunity to switch.

As currently proposed, BT would also be able to discriminate against its "*more inert (non market active/aware customers)*" by offering discounts only to more active customers. This discrimination would be directly linked to BT's ability to target active customers at the point where they attempt to churn. As such targeting of discounts would be independent of factors such as age and socio-economic group which may characterise a social grouping, we dispute that BT might have difficulty in targeting"

### Ofcom's response

7.51 In February 2008 BT began offering automatic roll-overs contracts to residential customers for their Free Evening and Weekend Calls package. We requested further information on customer behaviour with respect to those with automatic rollover contracts.

7.52 We do not consider that the existence of automatic roll-over contracts *per se* directly impacts on our assessment of the competitive state of the market which as discussed in earlier sections appears robust based on current evidence. In this context it is appropriate to note that BT has also begun to introduce similar rolling contracts in broadband (since February 2009) – i.e., in a market that was already found not to have an operator with SMP.

7.53 Our assessment of the level of competition is premised on an assumption that the terms and conditions in BT's contract would not have a strong detrimental impact on the competitive process. Clearly, if it is proven that such contracts do have a detrimental competition impact, then we may need to re-assess our view of BT's position in the retail markets. This is likely to depend on the extent to which such impacts are material and could not be mitigated by other actions (for example changes to General Conditions relating to the provision of narrowband services).

7.54 Given the short time since the introduction of these contracts for residential customers by BT, there is limited evidence so far of its impact on customer behaviour. BT has continued to lose market share with no immediately apparent impact on the rate of loss since the introduction of automatic roll-over contracts. BT's competitors have continued to grow.

- 7.55 BT signed up a significant proportion of their residential customers on automatic roll-over contracts in the second half of 2008. It is likely that we would only see the impact (if any) on aggregate churn rates feeding through over the next few months. It is worth noting that there are some small providers other than BT that offer rollover contracts to residential consumers including AdEPT and Axis, though given their small size the impact on overall competition is likely to be low.
- 7.56 Information provided by BT suggests that a significant majority of residential customers on a roll-over contract are being rolled over without change to the contract. However, given the information currently available it is difficult to draw any firm conclusions on the impact on customers' willingness to consider alternative providers or the potential long term impact on switching behaviour.
- 7.57 There is also a concern that the opt out process for rollovers also offers an opportunity for BT to influence consumers that may be thinking about switching and targeting those intending to leave – this risk of consumer differentiation was one of the main concerns highlighted in the impact assessment.
- 7.58 Our view is that this issue warrants further review. We will, therefore, undertake a more detailed examination of the issue, which is likely to include :
- direct contact with customers signed up to automatic rollover contracts;
  - consideration of the use of automatic rollover contracts in other countries and industries; and
  - other detailed data analysis as required.
- 7.59 A key focus of our analysis will be on the impact on competition as well as on the fairness of the terms of the contracts. If a material impact on competition is found, it would be appropriate for us to intervene.

### **Switching processes**

#### **Consultation responses**

- 7.60 Stakeholders raised concerns that any movement to loser provider led processes for narrowband services might risk allowing BT to differentiate customers e.g. by offering those who expressed an interest in leaving a more attractive deal and allow BT to build on their market share to the detriment of competition.
- 7.61 TalkTalk Group stated that they “believe that Ofcom must reach a conclusion in its single migration programme sooner rather than later to avoid prolong the debate and uncertainty among providers. Ofcom has already made pronounced statements in support of a gaining provider led switching process. We believe that it would be inappropriate to remove the SMP designation on BT without first making clear that a new single switching process must be gaining-provider led (whilst being robust enough to allay any concerns Ofcom may have around mis-selling).”
- 7.62 Cable & Wireless also noted “BT’s ability to bundle voice services with broadband, which has a losing provider-initiated switching process also allows BT to protect its dominance by creating a barrier to customers switching. BT’s tactics lock in a large proportion of customers, making it prohibitively expensive to seek a new supplier and results in a significantly reduced addressable market available to BT’s competitors.”

## Ofcom's response

- 7.63 Switching is a vital part of the competitive process, and Ofcom remains committed to ensuring that there are no obstacles in the way of consumers who choose to move between different companies and products. For consumers to benefit from competition, they must be able to shop around and, once they have found a good deal, to switch providers without undue effort, disruption or anxiety. A good customer experience is vital to the competitive process, as competition can only work where customers are confident in the switching and transfer process.
- 7.64 Given the trend towards convergence and, in particular, an increase in retail bundling, switching is already becoming more complex for customers. For example, at present, a consumer who switches landline and broadband at the same time (sometimes as a bundle) will have to go through one of two processes:
- if the customer's existing or new services are provided at the network level using local loop unbundling, then the process follows the 'Notification of Transfer' process and is 'gaining provider'-led;
  - if the customer is moving to or from a landline-broadband combination which does not involve local loop unbundling at the network level, then the customer needs to use a combination of MAC and 'notification of transfer' processes and requires contact with both the losing and gaining providers.
- 7.65 The choice of underlying network technology is something that will be invisible to the consumer, so we recognise that it is likely to be confusing from an end user perspective that the process used varies. In addition, such differences in switching processes may not be competitively neutral in terms of impact between Communications Providers. As such, we can see the merit in establishing processes for switching which are the same for particular types of switches regardless of the underlying network choice. A single process for any switch in which more than one service is involved would be easier to communicate to consumers, and is likely to be simpler to execute, than the current situation in which the choice of switching mechanism varies for reasons that the consumer cannot observe.
- 7.66 Ofcom is currently undertaking a separate project as part of its migrations work which is looking to determine how we can ensure that regulations and processes are in place that do not inhibit consumers' ability to switch, both in a world of single and bundled product offerings. This work is assessing the extent to which there is a need for harmonisation of switching processes across different services. We plan to publish a consultation document on this issue in the first half of 2010.
- 7.67 In making this determination on migrations we will be informed by the analysis set out in the March Consultation and this Statement around the risk of allowing BT to discriminate among its customers in a manner detrimental to consumer welfare (this is discussed further in the impact assessment).

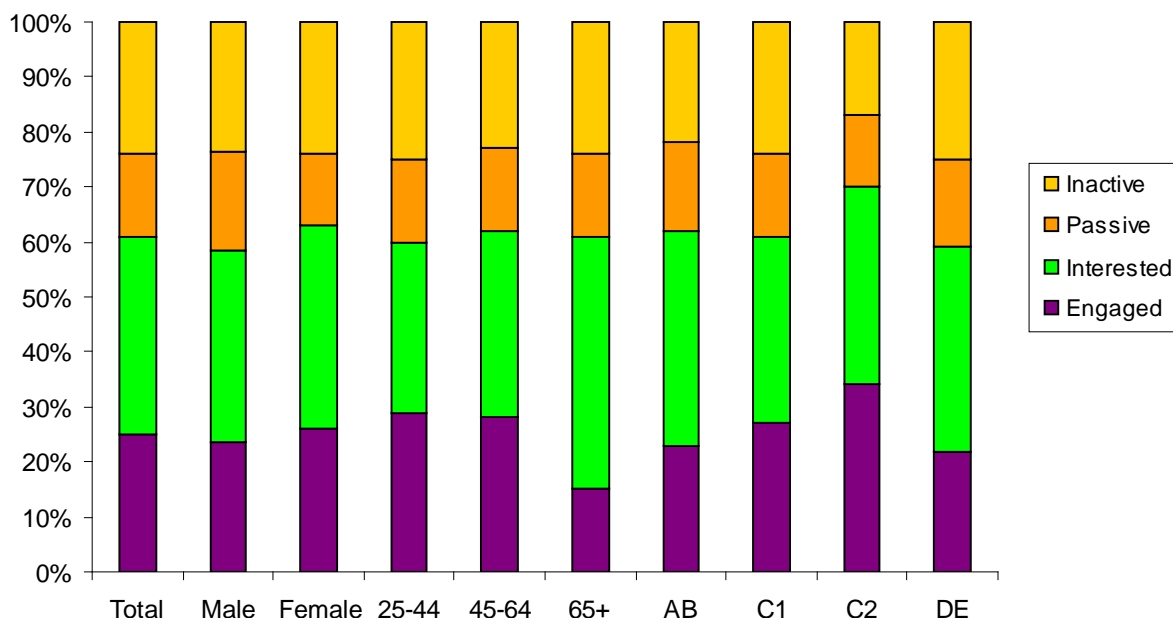
## Equality impact assessment

- 7.68 We are required to have due regard to any potential impacts our decisions in this statement may have on race, disability and gender equality – an Equality Impact Assessment (EIA) is our way of fulfilling this obligation. We have accordingly undertaken a full EIA. In particular, we have examined what impact our decisions will have on different demographic groups.

- 7.69 One clear characteristic of this market is a relatively high percentage of inactive customers in terms of fixed line telephone market participation. Given this, it is to be expected that the default position for customers not making a choice is almost always to remain with BT. As discussed in Sections 5 and 6, we do not consider that the continuing relatively high market share of BT is itself an indicator of competition failure. As the incumbent, BT will, for the foreseeable future, retain a relatively high market share.
- 7.70 We would be concerned if BT were able to exploit the existence of this group, say through targeted packages which advantaged consumers who were more likely to be market active.
- 7.71 Our analysis suggests that this would be difficult for BT. According to Ofcom's Consumer Experience (2008) report, this inactivity is spread fairly evenly across age, gender and socio-economic groups (see Figure 7.1).

Figure 7.1

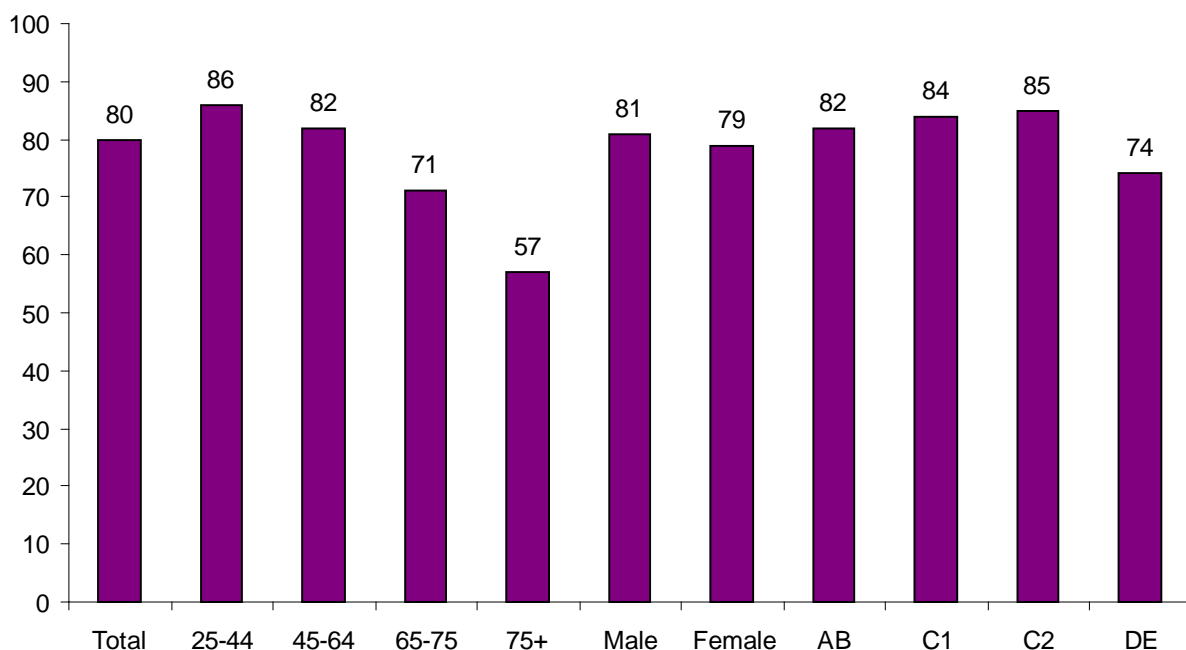
## Demographic differences in participation in fixed line markets



- 7.72 Inactivity does not seem to be simply a factor of awareness of competition. As Figure 7.2 shows, levels of awareness are higher than levels of activity. This suggests that a significant proportion is inactive through choice.



**Figure 7.2**  
**Awareness of competition**



- 7.73 The absence of a clearly defined social grouping for lack of activity suggests that BT would have difficulty targeting such groups. Equally, the fact that for at least some of the customers this lack of activity is a factor of choice suggests that, if the price differential between providers increased, activity might also increase.
- 7.74 We are already seeing the growth of retail providers who are specifically targeting narrowband customers on price alone and who have a wide and effective distribution and marketing presence (e.g. the Post Office and Tesco). The availability of attractive alternative products means BT would be less likely to find a discriminatory strategy profitable (because customers could easily switch away to other providers).
- 7.75 The above notwithstanding, we consider that it is important to avoid changes to regulations that would allow greater customer segmentation to the detriment of inactive customers. For example, we may need to be careful about any proposals that would allow BT to target discounts to customers indicating an intention to leave.
- 7.76 Based on the above analysis we consider that we have taken into account any equality issues in making our decisions in this review.

## Section 8

# Conclusions

## Introduction

8.1 In this Section we set out a summary of the decisions of the market review. We also demonstrate how our remedies, for the remaining SMP markets, satisfy the legal tests for their imposition (or removal).

## Summary of conclusions

8.2 Tables 8.1 set out a summary of the market structure and SMP determinations and how they differ from the 2003 review.

**Table 8.1**

**Summary of conclusions on market definition and market power**

2003 Markets	SMP BT	SMP KCOM	2009 Proposed Markets	SMP BT	SMP KCOM
Residential fixed narrowband access	Yes	Yes	Residential fixed narrowband access	No	Yes
Business fixed narrowband access	Yes	Yes	Business fixed narrowband access	No	Yes
Residential ISDN2 access	Yes	Yes	N/A	N/A	N/A
Business ISDN2 access	Yes	Yes	Business ISDN2 access	Yes	Yes
Residential fixed local calls	Yes	Yes	Residential fixed calls  Single market for all calls	No	Yes
Residential fixed national calls	Yes	Yes			
Residential fixed international calls	Yes	Yes			
Residential fixed calls to mobile	Yes	Yes			
Residential fixed operator assisted calls	Yes	Yes			
Business fixed local calls	Yes	Yes	Business fixed calls  Single market for all calls	No	Yes
Business fixed national calls	Yes	Yes			
Business fixed international calls	No	Yes			
Business fixed calls to mobile	Yes	Yes			
Business fixed operator assisted calls	Yes	Yes			

## Fixed Narrowband Retail Services Market Review

- 8.3 As shown our determinations are largely deregulatory. We have found that BT no longer holds an SMP position in the analogue access markets or calls markets.
- 8.4 We have found that BT retains an SMP position in the ISDN2 market, but we consider that it is appropriate to rely on wholesale remedies alone to promote consumers' interests in those markets. As noted in Section 5, the SMP finding represents a binary assessment of a number of complex evidentiary sources.
- 8.5 For Hull, we do not consider that the market conditions have altered substantially. While KCOM is experiencing some increased competition it still holds SMP in the relevant markets and we consider the continuation of the existing SMP remedies is appropriate. As discussed in Section 7, however, we are open to further review of the application of the remedies subject to further discussion with KCOM and other stakeholders.

**Legal tests****Tests for setting of SMP conditions and directions from the Communications Act**

- 8.6 As noted, in Section 2 we need to satisfy a number of tests set out under the Communications Act where we decide to impose SMP conditions. We consider that our decisions meet the tests set out in the Communications Act. Our reasoning is set out below for each of the conditions set out in Annex 1.
- 8.7 We also consider that it is appropriate to consider the legal test in respect to the removal of the SMP retail remedies (and reliance solely on wholesale remedies) for the SMP determination on BT for the ISDN2 market, in that we are obliged to impose appropriate regulation on markets in which a finding of SMP is made. In assessing what remedies are "appropriate" we believe that it is important to assess the existing remedies, in light of our assessment of the market.
- 8.8 We have concluded that BT no longer holds SMP in a number of markets. Section 84(4) of the Communications Act requires that, where such a finding is made we, "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". Where we make a finding of no SMP in a market, we will revoke all existing SMP conditions in accordance with the requirement in section 84(4).

*BT ISDN2*

- 8.9 Section 3 of the Communications Act imposes general duties on Ofcom, in carrying out its functions, to further the interests of citizens in relation to communications matters and of consumers in relevant markets, where appropriate by promoting competition. The Section also requires us to consider the interests of consumers in respect of choice, price, quality of service and value for money
- 8.10 We consider that our removal of retail remedies fulfil these general duties under section 3 of the Communications Act as we consider that there is insufficient price and service competition in this mature market and that the existing remedies discourage such competition, by allowing price following of the SMP provider and discouraging BT from cutting prices and innovation in service.
- 8.11 Section 4 of the Communications Act sets out the Community requirements on Ofcom which flow from Article 8 of the Framework Directive. In considering which, if any, SMP services conditions to propose, Ofcom has taken account of all of these requirements. In

particular, Ofcom has considered the requirement to promote competition and to secure efficient and sustainable competition for the benefit of consumers.

- 8.12 We have placed particular emphasis on the promotion of competition, which we consider is likely to be the most effective way of furthering citizen and consumer interests in the markets under review.
- 8.13 We will always seek the least intrusive regulatory measures to achieve our policy objectives, in accordance to its duty under section 6 of the Communications Act to minimise the burden of regulation. Given this approach and the requirement to promote competition we consider that the removal of retail remedies is appropriate and justifiable.
- 8.14 In addition to the overarching objective referred to above, we have taken into account a number of secondary objectives, including
- Prices:* to ensure that services are available at prices that are reasonably related to the efficient costs of supply, preferably as a result of effective competition; and
- Investment and innovation:* to promote efficient investment in the development of new and innovative service.
- 8.15 We carried out a full regulatory impact assessment in relation to the proposals for ISDN2 as required by section 7 of the Communications Act.

### Section 91 test

- 8.16 Section 91 requires that retail level remedies authorised by that section shall only be applied where “Ofcom are unable, by the setting of conditions of the sorts specified in subsection (3) to perform, or fully perform, their duties under section 4 in relation to the market situation in the relevant market.” (section 91(2))
- 8.17 The conditions specified in subsection (3) are access related conditions and SMP conditions authorised or required by sections 87 to 90. Such conditions include the conditions imposed in the related wholesale review.
- 8.18 We consider that those proposed conditions are sufficient for us to fully perform our section 4 duties. Further we have considered whether additional remedies would add to or assist us in our compliance with section 4. We do not consider this to be the case. In particular we have reviewed the current remedies imposed.
- 8.19 The nature of the ISDN2 market, which is characterised by a slowly declining customer base and price following by other providers, are such that the requirements on BT to publish price and non-discriminate no longer are appropriate. We consider that the regulations lead to reluctance by BT to actively compete on price, in case the value of the market falls for BT and other Communications Providers (e.g. as any price cuts only ensure that the total revenue in the market would reduce without delivering BT any competitive advantage or attracting new customers into the market.) A removal of the remedies and a reliance on wholesale remedies should introduce the opportunity for BT and other Communications Providers to actively compete on a contract by contract basis with a long term benefit for all customers. The section 4 duty to promote competition is, therefore, better served by not imposing additional retail remedies.
- 8.20 We, therefore, consider that, whilst we have found SMP in the ISDN2 retail market, the test in section 91(2) is not satisfied and we should not set additional conditions at the retail level.

## EC Guidelines

- 8.21 The Commission's SMP Guidelines state, at paragraphs 21 and 114, that NRAs must impose one or more SMP conditions on a dominant provider. This reflects Article 16(4) of the Framework Directive which states that NRAs "shall on such undertakings [with SMP] impose appropriate specific regulatory obligations". We consider that the appropriate SMP remedies for the identified markets are at the wholesale level and we are compliant with the principles of the Framework Directive and the SMP Guidelines. This is consistent with Article 17 of the Universal Service Directive which restricts the imposition of specific retail remedies to situations where wholesale remedies are not effective (the same test is essentially repeated in section 91 of the Communications Act, as described above).
- 8.22 In removing of retail remedies for ISDN2, set out above, Ofcom is, therefore, satisfied that it has considered all of the relevant requirements of the Communications Act.

## KCOM Markets

- 8.23 We consider below the SMP remedies for the markets where KCOM has SMP. We consider that the justification for individual remedies applies equally to each of the markets. For that reason, we will set out the tests for each remedy and then confirm to which markets the remedy applies.
- 8.24 Given the discussion above, we would also wish to confirm that we consider that, in the case of KCOM, we do not consider that it is sufficient to rely on wholesale remedies, as the level of competition in the Hull market is so limited that retail remedies are still required to encourage competitive entry.

### SMP Condition no undue discrimination condition

- 8.25 Given KCOM's SMP position our view is that KCOM should be required not to discriminate unduly between retail customers in the following markets in Hull:
- Residential analogue exchange line services;
  - Business analogue exchange line services;
  - Business ISDN2 exchange line services;
  - Residential calls;
  - Business calls;
- 8.26 In the 2003 review, we considered how we should treat undue discrimination in its implementation. We consider that this remedy does not mean that there should not be any differences in treatment between undertakings, rather that any differences should be objectively justifiable and/or not have a material adverse effect on competition for example, by differences in underlying costs of supplying different undertakings.

### *Section 3 test*

- 8.27 As noted above, Section 3 of the Communications Act imposes general duties on Ofcom, in carrying out its functions, to further the interests of citizens in relation to communications matters and of consumers in relevant markets, where appropriate by promoting competition. The Section also requires us to consider the interests of consumers in respect of choice, price, quality of service and value for money
- 8.28 We consider that our proposed condition on non undue discrimination fulfils these general duties under section 3 of the Communications Act as there is a risk that a

provider with SMP may exercise undue discrimination against a particular person or persons. In general, a provider can be said to be discriminating when it applies dissimilar conditions to equivalent transactions.

- 8.29 Such discrimination may be in various forms including price offers, terms and conditions or information. Such behaviour would represent undue discrimination if it has no objective justification e.g., if it has a material adverse effect on competition.
- 8.30 We consider that this condition is appropriate given the level of competition in the markets where KCOM has SMP. Competition law alone cannot be relied upon to prevent certain pricing strategies that could restrict the development of competition. The condition will enable Ofcom to carry out its duties to promote competition and the interests of citizens by prohibiting such undue discrimination.

#### *Section 4 tests*

- 8.31 In setting this SMP condition we have considered those requirements set out in section 4 of the Communications Act to act in accordance with the Commission requirements.
- 8.32 By preventing undue discrimination, it meets the first requirement to promote competition and the third requirement to protect the interests of EU citizens.

#### *Section 47 tests*

- 8.33 We consider that the setting of this condition meets the tests set out in section 47 of the Communications Act.
- 8.34 It is justifiable, in that it is required to ensure that KCOM does not exploit its market power by discriminating unduly in the retail markets in which it has SMP.
- 8.35 It does not discriminate unduly against KCOM because, although it only applies to them, they have SMP and it is justified to impose the condition only on them. Where providers have SMP, discrimination can be effectively applied by the provider in question. Without market power, discrimination can be undermined by competitors or customers and attempted discrimination would not be considered undue.
- 8.36 It is proportionate in that it does not prevent the application of dissimilar conditions to different transactions where there are objective reasons for doing so. It is therefore the least burdensome means of achieving its aim.
- 8.37 We consider we have met the requirement of transparency set out in the Communications Act by setting out the proposed requirements on KCOM and the justification for the condition.

#### *Section 91(2)*

- 8.38 We also consider that the condition meets the test set out in Section 91(2) of the Communications Act. We do not consider that the current state of competition in the Hull markets would allow us to rely on wholesale remedies alone. Those remedies have, so far, not enabled or encouraged sufficient competitive entry. Accordingly, we consider that we continue to require retail remedies to address the concerns set out above.

#### *SMP condition to notify charges terms and conditions*

## Fixed Narrowband Retail Services Market Review

- 8.39 Ofcom has wide powers to seek specific information needed to assess allegations of anti-competitive behaviour. Some general and reliable visibility of a dominant operator's prices is needed, however, to enable both us and competitors to monitor those prices for possible anti competitive behaviour.
- 8.40 We, therefore, propose to require KCOM to publish charges, terms and conditions, including bundled services and to publish amendments and new charges, terms and conditions within 24 hours of the time that those amendments or new charges, terms and conditions come into force including notification to Ofcom.
- 8.41 The requirement would apply to KCOM in respect of the following markets in the Hull area:
- Residential analogue exchange line services;
  - Business analogue exchange line services;
  - Business ISDN2 exchange line services;
  - Residential calls;
  - Business calls;

*Section 3 test*

- 8.42 As noted above, section 3 of the Communications Act imposes general duties on Ofcom, in carrying out its functions, to further the interests of citizens in relation to communications matters and of consumers in relevant markets, where appropriate by promoting competition. Section 3 also requires us to consider the interests of consumers in respect of choice, price, quality of service and value for money
- 8.43 We consider that the setting of conditions on price notification fulfil these general duties under section 3 of the Communications Act. This option provides certainty that charges, terms and conditions will be published and offers the benefits of notification for monitoring purposes without facilitating price following in accordance with our duties to promote competition and the interests of citizens.
- 8.44 We consider that this condition is appropriate given the level of competition in the markets where KCOM has SMP.

*Section 4 tests*

- 8.45 In setting this condition we have considered those requirements set out in section 4 of the Communications Act to act in accordance with the Commission requirements.
- 8.46 Ensuring price visibility meets the first requirement to promote competition and the third requirement to protect the interests of EU citizens.

*Section 47 tests*

- 8.47 We consider that the condition meets the tests set out in section 47 of the Communications Act. The justification for imposing the condition is that general and reliable visibility of a dominant operator's prices enables Ofcom and competitors to monitor the dominant operator's prices for possible anti competitive behaviour.
- 8.48 Imposition of this condition does not discriminate unduly against KCOM as they are the only operator in the market with SMP; the behaviour of other operators is not capable of

having a materially adverse effect on competition as these operators do not have market power.

- 8.49 The remedy is proportionate, as it is the least burdensome means of achieving the objective, and the requirement is made fully transparent in the condition which is published at Annex 1 to this document.
- 8.50 We also consider that the condition meets the tests set out in Section 91(2) of the Communications Act as we set out above.

#### Revocation of existing SMP conditions

- 8.51 In changing our market definitions from those that we set in 2003, we have decided that it would be appropriate to revoke all of the SMP conditions imposed in 2003 on markets where we have reached a conclusion in this Statement. The only market from 2003 where we have not yet reached a conclusion are the ISDN30 exchange line services markets. It would not be appropriate, therefore, to revoke the SMP conditions applying in these markets prior to our conclusions on these markets. The Notification attached to this document confirm that, in relation to all other markets defined in 2003 all SMP conditions should be revoked.
- 8.52 In setting new SMP conditions for relevant markets in the Hull area, we have retained the basic numbering of the 2003 SMP conditions, but differentiated the two sets of conditions by replacing the prefix for each condition, moving from a “DA” to “DAA” prefix. It is important to maintain a distinction between these conditions, as, although they are similar in content, the 2003 conditions will continue to apply (as imposed) to the ISDN30 market, whereas the 2009 conditions will only apply to the Hull markets set out at paragraph 8.41 above.



**Annex 1****Legal Instruments****NOTIFICATION UNDER SECTIONS 48(1) AND 80 OF THE COMMUNICATIONS ACT 2003****Identifying markets, making market power determinations and the setting of SMP services conditions in relation to BT and KCOM under section 45 of the Communications Act 2003.****Background**

1. On 28 November 2003, the Director General of Telecommunications (“the Director”) published the *Fixed Narrowband Retail Services Markets explanatory statement and notification*<sup>83</sup> (‘the 2003 statement’).
2. On 29 December 2003, Ofcom took over the functions and responsibilities under the Communications Act 2003 relating to the EC Communications directives from the Director.
3. On 12 April 2006, Ofcom published *The Replicability of BT’s regulated retail business services and the regulation of business retail markets statement*<sup>84</sup>.
4. On 19 July 2006, Ofcom published the *Retail Price Controls explanatory statement*<sup>85</sup> allowing retail price controls confirmed in the 2003 statement to lapse.
5. On 19 March 2009 Ofcom published a consultation document *Review of the fixed narrowband services wholesale markets*<sup>86</sup> consulting on proposals made in relation to fixed narrowband markets identified at the wholesale level.
6. Following a period of consultation and having carefully considered the responses received during the consultation, this Notification now sets market definitions, market power analysis and SMP service conditions.
7. Ofcom is not, in this Notification, making decisions in relation to the previously defined ISDN30 access markets<sup>87</sup>. Ofcom will further consult on proposals for these markets and existing market definitions, market power determinations will, in the interim, remain extant for these markets. SMP service conditions for these markets will remain in force unless specifically revoked.

**Decisions**

8. Ofcom hereby makes, in accordance with sections 48(1) and 80 of the Act, the following decisions for identifying markets, making market power determinations and the setting of SMP services conditions by reference to such determinations.

<sup>83</sup> [http://www.ofcom.org.uk/static/archive/oftel/publications/eu\\_directives/2003/fix\\_narrow\\_retail0803.pdf](http://www.ofcom.org.uk/static/archive/oftel/publications/eu_directives/2003/fix_narrow_retail0803.pdf).

<sup>84</sup> <http://www.ofcom.org.uk/consult/condocs/busretail/statement/statement.pdf>.

<sup>85</sup> <http://www.ofcom.org.uk/consult/condocs/retail/statement/rpcstatement.pdf>.

<sup>86</sup> [http://www.ofcom.org.uk/consult/condocs/retail\\_markets/fnrsm\\_condoc.pdf](http://www.ofcom.org.uk/consult/condocs/retail_markets/fnrsm_condoc.pdf).

<sup>87</sup> Business ISDN30 exchange line services market for UK excluding Hull and Business ISDN30 exchange line services market for the Hull area, as defined in Notification to the 2003 statement.

*Market Definitions*

9. Ofcom has decided to identify the following markets for the purpose of considering market power determinations:

(a) for the United Kingdom, except the Hull Area:

- (i) Residential Fixed Narrowband Analogue Access;
- (ii) Business Fixed Narrowband Analogue Access;
- (iii) Residential Fixed Narrowband Calls;
- (iv) Business Fixed Narrowband Calls; and
- (v) ISDN2 Access.

(b) for the Hull Area:

- (i) Residential Fixed Narrowband Analogue Access;
- (ii) Business Fixed Narrowband Analogue Access;
- (iii) Residential Fixed Narrowband Calls;
- (iv) Business Fixed Narrowband Calls; and
- (v) ISDN2 Access.

*Market Analysis*

10. Ofcom has decided to make market power determinations that the following persons have significant market power:

- (a) in relation to the market set out at paragraph 9(a)(v) above, BT;
- (b) in relation to each of the markets set out at paragraph 9(b) above, KCOM.

11. Ofcom has decided that each of the markets set out in 9(a)(i) to 9(a)(iv) are effectively competitive and, therefore, has determined that BT is no longer a person with SMP in those markets.

*Setting and revocation of SMP Conditions*

12. Ofcom has decided to set SMP conditions on the person referred to in paragraph 10(b) above as set out in Schedule 1 to this Notification.

13. The effect of, and Ofcom's reasons for making, the decisions to identify markets set out in paragraph 8 above and to make the market power determinations set out in paragraphs 9 and 10 above are contained in, in the case of the markets set out in:

- (a) paragraphs 9(a)(i), 9(a)(ii), 9(a)(v), and 9(b)(i), 9(b)(ii), 9(b)(v), in Section 5 of the explanatory document accompanying this Notification;
- (b) paragraphs 9(a)(iii), 9(a)(iv) and 9(b)(iii), 9(b)(iv) in Section 6 of the explanatory document accompanying this Notification;

14. The effect of, and Ofcom's reasons for making, the decisions to set the SMP conditions set out in Schedule 1 to this Notification, and for not setting retail SMP conditions as set out at paragraph 11 above are contained in Sections 7 and 8 of the explanatory document accompanying this Notification.

15. Ofcom has decided that the SMP conditions set out at Annex H of the 2003 statement be revoked for the following markets only<sup>88</sup> (as defined in the 2003 statement);

(a) for the United Kingdom, except the Hull Area:

- (i) Residential analogue exchange line services;
- (ii) Residential ISDN2 exchange line services;
- (iii) Business exchange line services;
- (iv) Business ISDN2 exchange line services;
- (v) Residential local calls;
- (vi) Residential national calls;
- (vii) Residential calls to mobiles;
- (viii) Residential operator assisted calls;
- (ix) Residential IDD category A calls;
- (x) Residential IDD category B calls (on a route by route basis);
- (xi) Business local calls;
- (xii) Business national calls;
- (xiii) Business calls to mobiles; and
- (xiv) Business operator assisted calls.

(b) for the Hull area;

- (i) Residential analogue exchange line services;
- (ii) Residential ISDN2 exchange line services;
- (iii) Business exchange line services;
- (iv) Business ISDN2 exchange line services;
- (v) Residential local calls;
- (vi) Residential national calls originating in the Hull area;
- (vii) Residential calls to mobiles originating in the Hull area;
- (viii) Residential operator assisted calls originating in the Hull area;
- (ix) Residential IDD category A calls originating in the Hull area;
- (x) Residential IDD category B calls (on a route by route basis) originating in the Hull area;
- (xi) Business local calls;
- (xii) Business national calls originating in the Hull area;
- (xiii) Business calls to mobiles originating in the Hull area;
- (xiv) Business operator assisted calls originating in the Hull area;
- (xv) Business IDD category A calls originating in the Hull area; and
- (xvi) Business IDD category B calls (on a route by route basis) originating in the Hull area.

*Amendment of associated regulation*

16. Ofcom has further decided that the conditions set out at Annex 2 of *The regulatory financial reporting obligations on BT and Kingston Communications Final statement and notification* dated 22 July 2004 (as amended) (“the financial reporting Notification”), shall be revoked only in so far as they apply to the markets number 18 to 24, as identified in the table at Part 2 of Schedule 1 to the Annex to the financial reporting Notification.

17. The revocations, set out in paragraphs 15 and 16 above, will take effect on the publication of this Notification.

<sup>88</sup> Specifically excluding ISDN30 markets.

18. Ofcom proposes to further amend Annex 2 to the financial reporting Notification, by amending the table, “Part 2: Retail Markets” of Schedule 1 to the Annex by removing references to markets 18 to 24 inclusive; the amended table to read as follows:

### Part 2: Retail Markets

Market identified and in which BT found to have SMP in previous Notification pursuant to section 79 of the Communications Act	Date
25. Provision of traditional interface retail leased lines up to and including a bandwidth capacity of eight megabits per second within the UK but not including the Hull Area	24.06.04

19. For the avoidance of doubt, the SMP conditions set under the financial reporting Notification shall continue and not otherwise be affected by the Notification, save to the extent set out in paragraphs 16 and 18 above.

### Ofcom’s duties and legal tests

20. In identifying and analysing the markets referred to above, Ofcom has, in accordance with section 79 of the Act, taken due account of all applicable guidelines and recommendations which have been issued or made by the European Commission in pursuance of a Community instrument, and relate to market identification and analysis or the determination of what constitutes significant market power.

21. Ofcom considers that the SMP conditions referred to in paragraph 12 above comply with the requirements of sections 45 to 47, 87, 88 and 90 of the Act, as appropriate and relevant to each such SMP condition.

22. In making all of the decisions referred to in paragraphs 8 to 19 of this Notification, Ofcom has considered and acted in accordance with its general duties set out in section 3 of the Act and the six Community requirements in section 4 of the Act.

23. Copies of this Notification and the accompanying consultation document have been sent to the Secretary of State for Business, Innovation and Skills in accordance with sections 50(1)(a) and 81 of the Act, as well as the European Commission and to the regulatory authorities of every other member State in accordance with sections 50(2) and 81 of the Act.

### Interpretation

24. Save for the purposes of paragraph 9 of this Notification and except as otherwise defined in paragraph 25 of this Notification, words or expressions used shall have the same meaning as they have been ascribed in the Act.

25. In this Notification:

(a) “the Act” means the Communications Act 2003 (c. 21)

(b) “**BT**” means British Telecommunications plc, whose registered company number is 1800000, and any of its subsidiaries or holding companies, or any subsidiary of such holding companies, all as defined by section 736 of the Companies Act 1985 as amended by the Companies Act 1989;

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(c) “**Hull Area**” means the area defined as the 'Licensed Area' in the licence granted on 30 November 1987 by the Secretary of State under section 7 of the Telecommunications Act 1984 to Kingston upon Hull City Council and Kingston Communication (Hull) plc.

(d) “**KCOM**” means KCOM Group plc, whose registered company number is 2150618, and any of its subsidiaries or holding companies, or any subsidiary of such holding companies, all as defined by section 736 of the Companies Act 1985 as amended by the Companies Act 1989;

**Gareth Davies**  
**Competition Policy Director**

A person duly authorised in accordance with paragraph 18 of the Schedule to the Office of Communications Act 2002

**15 September 2009**

## Schedule 1

### **The Conditions imposed on KCOM under Sections 45 and 91 of the Communications Act 2003 as a result of the analysis of the markets set out in paragraph 9(b) of this Notification in which KCOM has been found to have significant market power**

#### **Part 1: Application, definitions and interpretation relating to the SMP conditions in Part 2**

1. Conditions DAA1 and DAA2 shall apply to the markets set out in paragraph 9(b) of this Notification.
2. In this Schedule 1:
 

"the Act" means the Communications Act 2003 (c. 21);

"Dominant Provider" means KCOM Group plc, whose registered company number is 2150618, and any of its subsidiaries or holding companies, or any subsidiary of such holding companies, all as defined by section 736 of the Companies Act 1985 as amended by the Companies Act 1989;
3. Except insofar as the context otherwise requires, words or expressions shall have the meaning assigned to them and otherwise any word or expression shall have the same meaning as it has in the Act.
4. The Interpretation Act 1978 shall apply as if each of the conditions were an Act of Parliament.
5. Headings and titles shall be disregarded.

#### **Part 2: The conditions**

##### **Condition DAA1 – Requirement not to unduly discriminate**

DAA1.1 The Dominant Provider shall not unduly discriminate against particular persons or a particular description of persons in relation to services offered.

DAA1.2 Nothing done in any manner by the Dominant Provider shall be regarded as undue discrimination under this Condition if and to the extent that the Dominant Provider is required or expressly permitted to do such thing in that manner by or under any condition set under section 45 of the Communications Act which applies to the Dominant Provider.

##### **Condition DAA2 – Requirement to publish charges**

DAA2.1 Except in so far as Ofcom may otherwise consent in writing, the Dominant Provider shall publish charges, terms and conditions and act in the manner set out below.

DAA2.2 The Dominant Provider shall publish charges, terms and conditions, including bundled charges, terms and conditions (whether or not those bundles include charges, terms and conditions for services supplied in markets to which this Condition does not apply).

## Fixed Narrowband Retail Services Market Review

DAA2.3 The Dominant Provider shall publish any amendments to the charges, terms and conditions published under paragraph DAA2.2, including charges, terms and conditions for any new services, within 24 hours of the time that the amendment comes into effect.

DAA2.4 Publication referred to in paragraphs DAA2.2 and DAA2.3 shall be effected by placing a copy of the information on any relevant website operated or controlled by the Dominant Provider.

DAA2.5 The Dominant Provider shall send to Ofcom a written notice of any amendment to the charges, terms and conditions published under paragraph DAA2.2 (including charges, terms and conditions for any new services) within 24 hours of the time that the amendment comes into effect and shall send a copy of the notice to any person who may reasonably request such a copy.

DAA2.6 Where it would be impractical for the Dominant Provider to publish under paragraphs DAA2.2, DAA2.3 or DAA2.5 any charge or amended charge, the Dominant Provider shall instead publish the method to be adopted for determining that charge or amended charge.

DAA2.7 The Dominant Provider shall provide services at the charges, terms and conditions published under this Condition, and shall not depart therefrom either directly or indirectly.

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**ANNEX 12**

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## Helping consumers to engage in communications markets

Consultation on end-of-contract and out-of-contract notifications

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NON-CONFIDENTIAL VERSION

Redactions are indicated by [X]

### **CONSULTATION:**

**Publication Date:** 31 July 2018

**Closing Date for Responses:** 9 October 2018

## About this document

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In this consultation, we put forward proposals to set new rules that will require communications providers to send a notification to their customers when they approach the end of their minimum contract period. We are also proposing a new rule that will require providers to send a one-off notification to their customers who have already passed the end of their minimum contract period, where these customers were not informed of that at the time. These notifications will be sent to both residential and small business customers (ten individuals or fewer).

In April 2018, we announced that we would focus our consumer engagement work on end-of-contract notifications. This document sets out our findings and invites stakeholder views on our proposals.

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## 1. Summary

- 1.1 We want people to be able to take advantage of the wide choice of communication services available and shop around with confidence, so that they can get the best deals for their needs. This could mean keeping their current deal, taking up a new deal with their current provider, or switching to a new supplier.
- 1.2 Many landline, broadband, mobile and pay TV deals in the market today are offered on contracts with a minimum term of 12, 18 or 24 months. Customers cannot leave until the end of this term, unless they pay an early termination charge. At the end of this minimum contract period, customers are no longer tied into their existing deal and have different options available to them. Although practices differ across the sector, if the consumer does nothing at this point, their contract is likely to continue on a monthly rolling basis. They may face a price increase, or elements of the deal they originally signed up to may change.
- 1.3 Most providers do not notify their customers when their minimum contract period is coming to an end. Nor do most providers explain what this means for the customer's service and price, or the options available to them. Instead, many suggest that customers upgrade their services, with important information missing.
- 1.4 Our view is that providers need to do more to treat their customers fairly, by sending them important information about their services at an appropriate time. This information will help consumers make informed decisions about their current deal, exercise choice, and be protected against unexpected or unwelcome changes – such as price increases at the end of their minimum contract period.

### Consumers are paying more than they need to

- 1.5 We have found that some people lack information that is fundamental to their ability to make informed decisions about their services. In particular:
- **Many don't know the status of their contract.** Up to 26% of people taking landline, broadband and pay TV services (standalone or as a bundle) do not know or are confused about their contract status.<sup>1</sup> The same is true of 15% of mobile phone customers.
  - **Some are unclear about future charges.** Around a quarter of people who do not know when their contract ends, also do not know what will happen to the price they pay when it does; and
  - **People often don't understand their options.** Some consumers do not understand what coming to the end of their minimum contract period means. They are also unaware of the options, savings or benefits available to them. Around one in ten are unaware that they could switch to a better deal with their current provider once their contract ends. One quarter of customers on a mobile handset contract are unaware of

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<sup>1</sup> The research did not cover standalone landline, standalone broadband, or quad play packages.

the possibility of moving to a SIM-only deal. And up to a quarter of out-of-contract customers do not think they could make any savings.

- 1.6 We have found that more than 20 million consumers are outside their minimum contract period, and more than 10 million are on deals with an automatic price increase at the end of this period. As a result, many consumers pay more because of higher prices or because they miss out on deals that could improve their package or save them money.
- 1.7 For example, customers taking landline and broadband services in a single package pay, on average, around 20% more when they are out-of-contract. This reflects the fact that providers tend to offer promotional discounts to new customers, or ‘retention’ or ‘loyalty’ discounts to existing customers who negotiate their price or threaten to leave.
- 1.8 Also, certain mobile consumers continue to pay the same price after the end of their minimum contract period, which for some consumers could be significantly higher than if they switched to a SIM-only deal.

## **We are consulting on new rules for end-of-contract and out-of-contract notifications<sup>2</sup>**

- 1.9 We propose to introduce requirements as follows:
- Providers should send end-of-contract notifications to their customers before the end of their minimum contract period, to allow them sufficient time to act effectively on receiving this information.
  - We also want providers to send a notification to their customers who are already outside their minimum contract period. A one-off notification would ensure these customers are appropriately informed that they are out-of-contract, together with the relevant implications of remaining on their existing deal.

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<sup>2</sup> For the purpose of this consultation, we use the term ‘end-of-contract’ as this is how consumers tend to talk about the end of their minimum contract period or ‘minimum term’. Where we refer to ‘end-of-contract’ or being ‘in-contract’ or ‘out-of-contract’, this refers to customers’ minimum contract period.

### What we are proposing – in brief

- Providers will be required to send:
  - an **end-of contract notification** to their customers, 40-70 days before the end of their minimum contract period, which allows customers sufficient time to take action and gives providers some flexibility on when to send the notification;
  - a one-off, **out-of-contract notification** to customers who are already out-of-contract and have not previously been informed about their contract coming to an end.
- The notifications should be sent to all residential and small business customers (ten individuals or fewer) who use services including landline, broadband, pay TV and mobile (standalone or as a bundle), using the customer’s preferred communication route (e.g. SMS, email or post).
- The notifications should include specific information, including:
  - the date on which the customer's minimum contract period will end, or has ended;
  - the services currently provided to the customer and the price paid;
  - changes to the service and price at the end of the minimum contract period, where relevant;
  - that the customer has options available to them (such as SIM-only deals for mobile<sup>3</sup>) and may be able to make savings.

1.10 Our proposals will benefit consumers by protecting them against unexpected and unwelcome changes, such as higher prices, and ensuring that they get the right information at the right time, enabling them to make informed decisions and exercise choice. We expect the proposals to lead to material benefits for consumers, particularly those who are able to avoid higher prices, save money or move to a better service package. Our plans will also benefit consumers by increasing competition in the market, and reducing the time and effort required for consumers to monitor and seek out information.

1.11 We expect limited costs to industry in implementing our proposed notifications, given that they involve a single communication to each customer. Therefore, our assessment is that these costs are proportionate in view of the likely benefits and our objectives to achieve what is fair for consumers.

### Next steps

1.12 We invite comments on our proposals by 9 October 2018. We will assess the available evidence and take account of consultation responses before deciding how to proceed.

1.13 We propose that consumers should start to receive end-of-contract notifications from six months after the date of our final statement, and that they should receive the one-off out-of-contract notification within 9 months.

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<sup>3</sup> A contract between a mobile network provider and a customer whereby the customer is only paying for the monthly network service and not a handset.

## 2. Background and introduction

### Introduction

- 2.1 One of Ofcom’s core aims is to ensure that markets work effectively for consumers, through regulation where appropriate, so that they can gain from the benefits of competition.<sup>4</sup> This reflects our principal duty to further the interests of citizens and consumers.
- 2.2 In our 2016 *Strategic Review of Digital Communications*, we noted that competition is generally the best way to deliver good outcomes for consumers, but that for consumers to gain the benefits of competition they need to be able to engage with the market and make informed choices.<sup>5</sup> Consumers should be able to take advantage of the choice available, shop around with confidence equipped with the right information, and ultimately secure the best deal for their needs. This could mean taking up a new deal with their current provider, switching to a new provider or making an informed decision to stay on an existing deal.
- 2.3 There are typically good deals on offer, but the evidence we have, shows that all too often consumers do not take advantage of the choice available to them. Instead, many consumers continue with the same service and the same provider for a long period of time. Our recent *Pricing Trends for Communications Services* report (the “Pricing Trends report”) highlights that consumers who do not effectively engage with the choices available to them in the market typically pay higher prices than those who do.<sup>6</sup>
- 2.4 This is a trend that also concerns the UK Government, with the recent Green Paper, *Modernising Consumer Markets*, noting that it is often the most vulnerable consumers who are least likely to be on good deals.<sup>7</sup>
- 2.5 As we explain below, and in more detail in this document, we have identified that most providers do not notify their customers at an appropriate time, and some consumers do not know when their minimum contract period is due to end, or indeed that it has in fact ended. Most providers also do not notify their customers of price increases or other service changes that occur at the end of their minimum contract period.
- 2.6 We are concerned that this lack of information results in too many consumers allowing their existing contracts to roll-over onto ‘out-of-contract’ terms. This means that some consumers experience an unexpected increase in their price, or change to their services,

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<sup>4</sup> Ofcom, Annual Plan 2018/19: *Making communications work for everyone*:

[https://www.ofcom.org.uk/data/assets/pdf\\_file/0017/112427/Proposed-Annual-Plan-2018.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0017/112427/Proposed-Annual-Plan-2018.pdf).

<sup>5</sup> Ofcom, Making communication work for everyone: initial conclusions from the Strategic Review of Digital Communications, 25 February 2016: [https://www.ofcom.org.uk/data/assets/pdf\\_file/0016/50416/dcr-statement.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0016/50416/dcr-statement.pdf).

<sup>6</sup> Ofcom, *Pricing trends for communications services in the UK*, 17 May 2018:

[https://www.ofcom.org.uk/data/assets/pdf\\_file/0030/113898/pricing-report-2018.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0030/113898/pricing-report-2018.pdf).

<sup>7</sup> Department for Business, Energy & Industrial Strategy, *Modernising Consumer Markets: Consumer Green Paper*, 11 April 2018:

[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/699937/modernising-consumer-markets-green-paper.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/699937/modernising-consumer-markets-green-paper.pdf).

while others continue on the same price and service package and do not benefit from moving to a better package and saving money.

- 2.7 This consultation sets out proposals to ensure that consumers are equipped with the right information at the right time to make informed decisions about the communications services they buy.

## July 2017 Call for Inputs

- 2.8 In July 2017, we published a Call for Inputs (the “July 2017 CFI”), launching a programme of work to help us better understand why some consumers may face difficulties engaging in communications markets.<sup>8</sup>
- 2.9 We received 26 responses to our CFI, including from providers, consumer bodies and advocacy groups, industry bodies, other regulators and individual consumers. The non-confidential responses are published on our website.<sup>9</sup> The relevant responses are discussed in sections 3 and 4 of this consultation.

## We published an update on our work in April 2018

- 2.10 In April, we announced that the first phase of our work on consumer engagement would consider whether end-of-contract notifications – whereby providers would proactively inform their customers when they are approaching the end of their minimum contract period – might address some of the lack of consumer engagement that we had identified.<sup>10</sup>

## Our regulatory policy objectives

### Most providers do not remind consumers when their minimum contract period ends

- 2.11 Many landline, broadband, mobile and pay TV deals in the market today are offered on contracts with a minimum contract period of 12, 18 or 24 months, where customers are not able to leave until the end of their minimum contract period unless they pay an early termination charge. At the end of this minimum contract period, consumers are no longer tied into their existing deal and have different options available to them. Although practice differs across the sector, if the consumer does nothing at this point, their contract may

<sup>8</sup> Ofcom, *Helping consumers to engage in communications markets: Call for Inputs*, 14 July 2017:

[https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0014/104441/call-inputs-consumer-engagement-communications.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0014/104441/call-inputs-consumer-engagement-communications.pdf).

<sup>9</sup> Non-confidential responses can be found at: <https://www.ofcom.org.uk/consultations-and-statements/category-2/helping-consumers-engage-communications-markets>.

<sup>10</sup> Ofcom, *Helping consumers to engage in communications markets: Update on next steps*, 27 April 2018:

[https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0015/113451/Engagement-project-update\\_April-2018.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0015/113451/Engagement-project-update_April-2018.pdf).



continue on a monthly rolling basis<sup>11</sup> on existing terms, they may face a price increase, or they may find that elements of the deal they originally signed up to change.<sup>12</sup>

- 2.12 The evidence we have indicates that most providers, across landline, broadband, mobile and pay TV services, do not notify their customers when their minimum contract period is coming to an end, or has ended, and what that means for their service and price.<sup>13</sup> Without this information, consumers do not always know when they should be reviewing their existing deal and if they should shop around for a new one. Where notifications are sent by providers to customers who are approaching the end or have reached the end of their minimum contract period, many suggest that customers upgrade their services, but with important information missing.

### **Providers should inform their customers of important information at the appropriate time**

- 2.13 It is reasonable to expect that providers will treat their customers fairly in the provision of communications services. An essential aspect of fairness is that providers ensure their customers are informed at the appropriate time of important information about their services. This will enable consumers to make informed decisions and will protect them against unexpected and unwelcome changes to their service or price (such as a price increase at the end of their minimum contract period).
- 2.14 Current Ofcom rules require providers to provide consumers with certain information on request at the time they purchase a service, which includes the duration of the contract, and the conditions for renewal and termination, as well as details of prices and tariffs, and the services provided.<sup>14,15</sup>
- 2.15 However, as set out in Section 3, consumers lack awareness of when their minimum contract period ends and what this means for their price and the services they buy. They are also not clear about the options available to them, including that they could make savings by taking up a new deal.
- 2.16 In our view, this shows that consumers do not always remember information that was provided to them when they purchased their service, which could have been up to 24 months previously (or longer where the consumer is already beyond the minimum contract period end date). Indeed, consumers may not have been provided information about subsequent precise price increases at all when they entered into the contract.

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<sup>11</sup> Where the customer is not tied into a new minimum term but may have to give notice (potentially up to 30 days) to cancel their contract and/or switch provider.

<sup>12</sup> See Section 3, Figure 5: Proportion and number of customers on deals with an automatic price increase at the end of the minimum contract period.

<sup>13</sup> See Section 3.

<sup>14</sup> See GC 9.1 and 9.2 of the current General Conditions, which will be replaced by GC C1.2 as of 1 October 2018.

<sup>15</sup> Furthermore, providers are required to give all subscribers notice of any price changes that were not agreed at point of sale (see GC 9.6 of the current General Conditions and GCs C1.6 to C1.8 of the revised General Conditions to come into effect on 1 October 2018).

- 2.17 For consumers to be able to avoid price and service changes and make informed decisions about their existing package and whether they should find a new deal, we consider that it is necessary for them to be informed of:
- when they are no longer tied to their minimum contract period and are able to change their contract or switch to another provider without incurring a penalty; and
  - the implications if they do not engage and remain on their existing deal. In particular, consumers should be made aware of any changes to their price or service that take effect from the end of the minimum contract period.
- 2.18 Consumers should be informed of this information at an appropriate time to ensure that they can effectively act on receiving this information. This means that it should be sent to consumers near or at the end of the minimum contract period without them having to seek it out. Where consumers are already outside their minimum contract period but were not informed of this, this information is equally important for them and should be sent as soon as possible.

### Consumers may face paying higher prices as a consequence

- 2.19 As a result of being unaware of when their minimum contract period ends or of the fact that it has ended and the implications of this for their price or services, a significant number of consumers allow their contracts to ‘roll over’ after the expiry of their minimum contract period. As a result, many pay higher prices, and do not benefit from better deals or opportunities to improve their package, either with their existing provider or by switching to another provider. In all these cases, we are concerned that consumers pay much higher prices than they need to.<sup>16</sup>
- 2.20 Our recent Pricing Trends report highlights that consumers who do not shop around for better deals typically pay higher prices than those who do. This reflects the fact that providers tend to offer promotional discounts to new customers, or ‘retention’ or ‘loyalty’ discounts to existing customers who negotiate or threaten to leave.<sup>17</sup> Generous promotional discounts for bundles (typically between 10% and 20% of the non-discounted price of the service over its minimum contractual term) and growing take-up of bundles (our research shows that 79% of UK households purchased bundled services in 2018<sup>18</sup>) emphasise the importance of consumers being equipped with the right information at the right time so that they are able to make informed choices about their current deal and the offers available to them.

### Our policy objectives

- 2.21 In light of the concerns highlighted above, we consider that it is in the interests of consumers that they are given important information about the services they buy at an appropriate time to ensure they know when to exercise choice and take advantage of

<sup>16</sup> See Section 3 for evidence to indicate that there is often a financial penalty for customers who remain out of contract.

<sup>17</sup> Ofcom, *Pricing trends for communications services in the UK*, 17 May 2018.

<sup>18</sup> Ofcom, *Technology Tracker*, H1 2018: [https://www.ofcom.org.uk/data/assets/pdf\\_file/0021/113169/Technology-Tracker-H1-2018-data-tables.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0021/113169/Technology-Tracker-H1-2018-data-tables.pdf).

competition in communications markets. Reflecting our statutory duties to further the interests of consumers, we have two regulatory policy objectives:

- to ensure consumers are informed at an appropriate time when their minimum contract period is coming to an end, and of any changes to price or services that will occur as a result; and
- to ensure consumers are informed that their minimum contract period has already come to an end if they were not previously informed of this.

## Legal Framework

### Ofcom's general duties

- 2.22 Section 3(1) of the Communications Act 2003 (the “Act”) states that it shall be the principal duty of Ofcom, in carrying out its functions:
- a) to further the interests of citizens in relation to communication matters; and
  - b) to further the interests of consumers in relevant markets, where appropriate by promoting competition.<sup>19</sup>
- 2.23 In performing its duties under section 3(1) of the Act, Ofcom is required to have regard to the principles under which regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed, as well as any other principles appearing to Ofcom to represent best regulatory practice (section 3(3) of the Act).<sup>20</sup>
- 2.24 Section 3(4), provides that Ofcom must have regard, in performing its duties, to a number of matters<sup>21</sup> including the desirability of promoting competition in relevant markets; the desirability of promoting and facilitating the development and use of effective forms of self-regulation; the desirability of encouraging investment and innovation in relevant markets; the needs of persons with disabilities, of the elderly and of those on low incomes; the opinions of consumers in relevant markets and of members of the public generally; and the extent to which, in the circumstances of the case, the furthering or securing of the matters mentioned in section 3(1) is reasonably practicable.
- 2.25 In addition, section 3(5) of the Act requires that, when performing its duty to further the interests of consumers, Ofcom must have regard, in particular, to the interests of those consumers in respect of choice, price, quality of service and value for money.

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<sup>19</sup> Consumer is defined in section 405(5) of the Act and includes people acting in their personal capacity or for the purposes of, or in connection with, a business.

<sup>20</sup> Ofcom’s regulatory principles can be found at: <https://www.ofcom.org.uk/about-ofcom/what-is-ofcom>.

<sup>21</sup> As they appear to Ofcom to be relevant in the circumstances.

## Duties for the purpose of fulfilling EU obligations

2.26 As set out in Section 4 of the Act, when exercising certain functions<sup>22</sup> Ofcom must act in accordance with the six European Community requirements described there. The requirements of Section 4 of the Act are read in the light of Article 8 of the Framework Directive<sup>23</sup> which sets out the policy objectives of the Framework. It says national regulatory authorities shall ensure that, when they carry out the regulatory tasks set out in the Framework, they take all reasonable and proportionate measures aimed at achieving specific objectives.<sup>24</sup> Those objectives include:

- the promotion of competition in the provision of electronic communications services<sup>25</sup> by ensuring that users derive maximum benefit in terms of choice, price and quality and there is no distortion or restriction of competition in the electronic communications sector;<sup>26</sup> and
- the promotion of the interests of EU citizens by ensuring a high level of protection for consumers in their dealings with suppliers and promoting the provision of clear information (in particular, requiring transparency of tariffs and conditions for using publicly available electronic communications services).<sup>27</sup>

## Powers and duties in relation to general conditions

2.27 Alongside the Framework Directive, the Authorisation Directive provides for national regulatory authorities to set conditions of general authorisation for communications providers.<sup>28</sup> Under Article 6 and paragraph 8 of the Annex these include conditions containing “... consumer protection rules specific to the electronic communications sector, including<sup>29</sup> conditions in conformity with Directive 2002/22/EC (“Universal Service Directive”).” The over-arching principle is that such conditions shall be non-discriminatory, proportionate and transparent.<sup>30</sup>

2.28 These provisions are implemented into national law by the Act. In particular, Section 45 of the Act says that Ofcom may set general conditions which contain provisions authorised or required by one or more of sections 51, 52, 57, 58 or 64. Under Section 51(1)(a), the general conditions Ofcom may make include conditions making such provisions as Ofcom consider appropriate for the purpose of protecting the interests of end-users of public electronic communications services (“PECS”). Section 51(2) sets out a non-exhaustive list of the specific types of general conditions that Ofcom may set in pursuance of this purpose.

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<sup>22</sup> Including those we propose to exercise in this document.

<sup>23</sup> Directive 2002/21/EC of the European Parliament and of the Council (as amended by Directive 2009/140/EC), 7 March 2002. Available at: <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:32002L0021>

<sup>24</sup> Set out in paragraphs 2, 3 and 4 of Article 8.

<sup>25</sup> As well as electronic communications networks and associated facilities and services.

<sup>26</sup> Article 8(2)(a) and (b) of the Framework Directive.

<sup>27</sup> Article 8(4)(b) and (d) of the Framework Directive.

<sup>28</sup> Directive 2002/20/EC of the European Parliament and of the Council (as amended by Directive 2009/140/EC), paragraph 8 of Annex A. Available at: <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32002L0020&from=EN>

<sup>29</sup> And therefore, not limited to.

<sup>30</sup> Article 6(1) of the Authorisation Directive.

Section 51(2)(d) provides that Ofcom can, by general condition, “require the provision, free of charge, of specified information, or information of a specified kind, to end-users”. We are proposing to exercise these powers, in the manner set out in this consultation document, to further the interests of citizens and consumers in these markets.

- 2.29 Section 47(2) governs the circumstances in which Ofcom can set or modify a general condition. It states that a condition can be made or modified where doing so does not discriminate unduly against particular persons or against a particular description of persons and is proportionate to what the condition or modification is intended to achieve, and transparent in relation to what it is intended to achieve.<sup>31</sup>
- 2.30 We consider in Section 5 how the proposals set out in this document accord with our powers and duties.

## Impact Assessment

- 2.31 The analysis presented in this document constitutes an impact assessment as defined in Section 7 of the Act. Impact assessments provide a valuable way of assessing different options for regulation and showing why the preferred option was chosen. They form part of best practice policy-making. This is reflected in Section 7 of the Act, which means that generally Ofcom has to carry out impact assessments where its proposals would be likely to have a significant effect on businesses or the general public, or when there is a major change in Ofcom's activities. However, as a matter of policy Ofcom is committed to carrying out impact assessments in relation to the great majority of its policy decisions. For further information about Ofcom's approach to impact assessments, see the guidelines *Better policy-making: Ofcom's approach to impact assessment*, which are on Ofcom's website.<sup>32</sup>

## Equality Impact Assessment

- 2.32 Ofcom is also required to assess the potential impact of all its functions, policies, projects and practices on the equality of individuals to whom those policies will apply. An equality impact assessment (“EIA”) assists Ofcom in making sure that it is meeting its principal duty of furthering the interests of citizens and consumers regardless of their background or identity.
- 2.33 We have given careful consideration to whether or not the proposals contained in this document will have a particular impact on race, age, disability, gender, pregnancy and maternity, religion or sex equality. We do not envisage however, that our proposals would have a detrimental impact on any particular group of people.

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<sup>31</sup> In assessing whether a General Condition is proportionate or not Ofcom is likely to consider whether it is objectively justifiable in relation to the networks, services, facilities, apparatus or directories to which it relates.

<sup>32</sup> More information about Ofcom's approach to impact assessments are available at:

[http://stakeholders.ofcom.org.uk/binaries/consultations/better-policy-making/Better\\_Policy\\_Making.pdf](http://stakeholders.ofcom.org.uk/binaries/consultations/better-policy-making/Better_Policy_Making.pdf)

## Sources of evidence

2.34 In making the proposals set out in this consultation, we have taken into account evidence from a number of sources, including:

- responses to our July 2017 CFI;
- bespoke qualitative and quantitative consumer research undertaken in 2015, 2016, 2017 and 2018 (detailed below);
- the *Pricing Trends for Communications Services in the UK* report 2018;<sup>33</sup>
- the Ofcom 2017 Switching Tracker;<sup>34</sup> and
- input from stakeholders (including material obtained using our statutory information gathering powers) on providers' current practices and customer bases.<sup>35</sup>

## Consumer research

2.35 We have commissioned and published research exploring consumers' engagement with communications services, including awareness and expectations regarding the end of their minimum contract period. These are summarised below, with further methodological detail in their respective slide packs or reports:

- Qualitative consumer engagement research, conducted in July 2017 by Futuresight ("2017 qualitative consumer engagement research"). This study provided insights to better understand why consumers do not engage fully, or at all, with communications markets; what, if any, barriers exist; and what might encourage those who are less engaged to participate more.<sup>36</sup>
- Quantitative consumer engagement research, conducted in January to April 2018, by Critical Research ("2018 quantitative consumer engagement research"). This study quantified the extent of any difficulties with engagement that consumers had identified in our qualitative research; and explored consumer awareness and understanding of their contractual status.<sup>37</sup>
- Qualitative end-of-contract notification testing, conducted in May 2018, by Jigsaw ("2018 end-of-contract notification qualitative research"). This study tested various potential pieces of information for inclusion in an end-of-contract notification, seeking to understand attitudes towards the content and ordering, to test comprehension and

<sup>33</sup> Ofcom, Pricing trends for communications services in the UK report, May 2018.

<sup>34</sup> Our annual Switching Tracker monitors switching levels and the extent to which consumers engage with communications markets. Data tables are available on the Ofcom website here:

[https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0024/107178/Switching-Tracker-2017-Data-tables.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0024/107178/Switching-Tracker-2017-Data-tables.pdf)

<sup>35</sup> We collected information from: BT, EE, KCOM, O2, Plusnet, Post Office, Sky, TalkTalk, Tesco Mobile, Three, Verastar, Virgin Media, Vodafone and XLN.

<sup>36</sup> Ofcom's qualitative consumer engagement research 2017, conducted by Futuresight:

[https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0022/113458/Engagement-Qualitative-Research-Report,-2017.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0022/113458/Engagement-Qualitative-Research-Report,-2017.pdf)

<sup>37</sup> Ofcom's quantitative consumer engagement research 2018, conducted by Critical. Slide 15:

[https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0022/117076/Consumer-engagement-quantitative-research-2018-slide-pack.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0022/117076/Consumer-engagement-quantitative-research-2018-slide-pack.pdf)

to understand which pieces of information would be most useful and effective in a potential end-of-contract notification.<sup>38</sup>

- 2.36 We also rely on previous bespoke research on end-of-contract notifications, conducted in 2015 by Jigsaw (the “2015 end-of-contract notification research”).<sup>39</sup> This research explored knowledge of minimum contract period end dates across the triple play, dual play, standalone pay TV and mobile markets, awareness of contract issues, as well as interest in being informed of their minimum contract period end date and the usefulness of knowing this end date when considering switching.
- 2.37 We also use previous bespoke research on SMEs’ experience of communications services, conducted in 2016 by Jigsaw (“2016 SME research”).<sup>40</sup> This research looked at business customer experience of communications services, switching behaviour, usage and satisfaction.
- 2.38 All of this research is available on Ofcom’s website using the links provided in the footnotes.

### Information requested from providers

- 2.39 To inform our assessment, we collected data from providers using our statutory information gathering powers. The required information relevant to this consultation is set out below, with further detail in Annex 7.
- First information request (residential customers), January 2018: Providers were asked to provide information:
    - about current practices relating to end-of-contract notifications;
    - on any notifications of price or service changes that occur at the end of the minimum contract period; and
    - on how customers can access information about their minimum contract period themselves.
  - Second information request (residential customers), May 2018: Providers were asked to provide information about customers who are:
    - on contracts that will see an increase in price during, and/or at the end of, the minimum contract period; and
    - within and outside of their minimum contract period.
  - Information request to providers regarding small to medium enterprises (SMEs), May 2018: SME providers were asked to provide similar information as we requested from residential providers in our first information request.

<sup>38</sup> Ofcom’s end of contract notification qualitative research 2018, conducted by Jigsaw:

[https://www.ofcom.org.uk/data/assets/pdf\\_file/0020/117074/Qualitative-end-of-contract-notification-research-July-2018.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0020/117074/Qualitative-end-of-contract-notification-research-July-2018.pdf)

<sup>39</sup> Ofcom’s 2015 end of contract notification research, conducted by Jigsaw:

[https://www.ofcom.org.uk/data/assets/pdf\\_file/0024/74715/end-of-contract-notification-research.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0024/74715/end-of-contract-notification-research.pdf)

<sup>40</sup> Ofcom’s 2016 quantitative SME research, conducted by Jigsaw:

[https://www.ofcom.org.uk/data/assets/pdf\\_file/0030/96348/Ofcom-SME-consumer-experience-research-2016-Report.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0030/96348/Ofcom-SME-consumer-experience-research-2016-Report.pdf)

## This document

2.40 The rest of this document is set out as follows:

- Section 3 sets out the case for requiring end-of-contract and out-of-contract notifications.
- Section 4 sets out our proposals for making end-of-contract and out-of-contract notifications simple for consumers and practical to implement.
- Section 5 contains our provisional conclusions on the proportionality of our proposals.

2.41 The Annexes are set out as follows:

- Annex 1: Responding to this consultation
- Annex 2: Ofcom’s consultation principles
- Annex 3: Consultation response cover sheet
- Annex 4: Consultation questions
- Annex 5: Glossary
- Annex 6: Impact assessment for regulating end-of-contract and out-of-contract notifications for residential consumers
- Annex 7: Data and methodology used to assess consumer outcomes
- Annex 8: End-of-contract and out-of-contract notification process
- Annex 9: Notification of proposed new general condition and modification to the General Conditions under section 48A(3) of the Act.<sup>41</sup>

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<sup>41</sup> Annexes 6 to 9 can be found here: [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0017/117161/Annexes-6-to-9.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0017/117161/Annexes-6-to-9.pdf)



## 3. The case for requiring end-of-contract and out-of-contract notifications

### Introduction

- 3.1 Many deals in the communications market are offered on contracts with a minimum contract period of 12 to 24 months. Although practice differs across the sector, if the consumer does nothing at the end of their minimum contract period, their contract continues on a monthly rolling basis. As they go ‘out-of-contract’, consumers may face an automatic price increase, or they may find that elements of the deal they originally signed up to change.
- 3.2 In this section, we set out the evidence that we have gathered which shows that most providers do not notify their customers, at the appropriate time, of information about the services they buy. In particular, consumers are not notified that they are approaching the end of their minimum contract period; what this means for their price and the services they buy; and the options available to them after this point, including the potential for savings. We also describe the evidence which shows that some consumers lack awareness of this information.
- 3.3 We consider that this lack of information leads to a significant number of consumers staying out-of-contract for longer than they otherwise would. As a result, we are concerned that many consumers are paying higher prices, and are unable to benefit from better service packages:
- Many consumers experience automatic price increases, or service changes, at the end of the minimum contract period. Due to a lack of awareness, they are unable to avoid them.
  - More generally, consumers cannot make informed decisions on when and whether they should search for a better deal.
- 3.4 For those consumers that are aware of this information, they have to incur time and effort to retain, monitor and seek out this information.
- 3.5 Later in this section, we set out the options for intervening to protect consumers’ interests. We propose to require that providers send end-of-contract notifications and a one-off out-of-contract notification. We consider that this would be the most appropriate and effective approach to address the harms we have identified. We propose that these notifications be sent to all residential and Small Business customers.

### Most providers do not notify consumers of relevant information about the end of their minimum contract period, at an appropriate time

- 3.6 The evidence we have collected shows that most providers do not notify consumers at the appropriate time of important information about the services they buy. In particular,

consumers are not notified that they are approaching the end of their minimum contract period; what this means for their price and the services they buy; and the options available to them after this point.

3.7 We asked the largest landline, broadband, pay TV and mobile providers whether they send end-of-contract notifications to customers.<sup>42,43</sup> In relation to landline, broadband and pay TV:

- Four providers, Sky, Virgin Media, Post Office and KCOM, told us they do not send any notifications to customers as they approach the end of their minimum contract period informing them that they are reaching that point, or of any changes in service or price at the end of the minimum contract period.<sup>44,45</sup>
- Four providers, BT, TalkTalk, Plusnet and Vodafone, told us they do send notifications to customers as they approach the end of their minimum contract period;<sup>46</sup> however, our analysis of the examples these providers provided to us indicates that they do not clearly state that the customer is approaching the end of their minimum contract period, the date the minimum contract period ends, or provide information relating to early termination charges.
- In terms of pricing information, two providers, BT and TalkTalk, told us they send notifications that inform customers their ‘discount’ or ‘promotional’ price plan is ending.<sup>47</sup> Another provider, Vodafone, told us it sends notifications that include a possible price saving if the consumer upgrades relative to the customer’s current (in-contract) tariff price.

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<sup>42</sup> We contacted providers with a relative market share above [redacted]% for each service.

<sup>43</sup> We also asked providers what other notifications they send to customers to convey information about changes in prices payable or the scope of services to be received. In particular, we asked providers if they send notifications to customers when they are coming to the end of a discount or promotional period.

<sup>44</sup> KCOM told us there are no price or service changes when a customer’s contract reaches the end of the minimum contract period.

<sup>45</sup> Sky told us that it sends SMS notifications to customers informing them about their upcoming bill payment, including how much the customer will pay and the date the payment will be taken.

<sup>46</sup> One provider [redacted] told us it only sends notifications to dual and triple play customers, and not to those on standalone services.

<sup>47</sup> Some notifications from BT include details of the exact amount of the discount that will expire and the price change whereas TalkTalk only states that the customer may see an increase in their bill, without specifying the magnitude of the increase.

Figure 1: Notifications by Landline, Broadband and Pay TV providers

Provider	Is a notification sent?	Is the minimum contract period mentioned?	Does the provider send a notification when a price change occurs at the end of the minimum contract period?	Additional Comments
BT	✓	×	✓	<ul style="list-style-type: none"> <li>Customers are sent notifications which show the price change incurred, as well as the date the change will occur.</li> </ul>
KCOM	×	×	Not Applicable	<ul style="list-style-type: none"> <li>There are no price or service changes when a customer's contract reaches the end of the minimum contract period.</li> </ul>
Plusnet	✓	×	×	<ul style="list-style-type: none"> <li>This provider notifies customers they can re-contract, but no other information is provided.</li> </ul>
Post Office	×	×	×	<ul style="list-style-type: none"> <li>If there is a limited discount on a tariff and it ends, the customer's contract will revert to the standard price.</li> </ul>
Sky	×	×	×	
TalkTalk	✓	×	✓	<ul style="list-style-type: none"> <li>Customers are sent notifications near the end of the minimum contract period that their 'promotion' or 'offer' is coming to an end. These do not include what the price of the standard tariff will be.</li> </ul>
Virgin Media	×	×	×	<ul style="list-style-type: none"> <li>Any discounts on the tariff (which may run for the duration of the minimum contract period) are removed when the time-limited offer period ends.</li> </ul>
Vodafone	✓	×	×	<ul style="list-style-type: none"> <li>Customers may receive invitations to upgrade their contract close to the end of the minimum contract period. These include a possible price saving relative to the customer's current tariff price.</li> <li>Provider recently introduced discounted tariffs where the price changes at the end of the minimum contract period, and have not provided notification examples as customers have not yet reached the end of the minimum contract period.</li> </ul>

Source: Provider response to formal information request

3.8 In relation to mobile, almost all mobile providers said they send customers upgrade communications to encourage the customer to re-contract to secure a new handset.<sup>48</sup> However, at the time of our request, only some providers (O2, Virgin Mobile and Vodafone) told us they send notifications to customers specifying they are coming to the end of their minimum contract period – of these providers, only one (O2) told us they send notifications that included the exact minimum contract period end date, and only one

<sup>48</sup> We did not specifically ask providers for examples relating to upgrade or re-contracting practice – the information gathered on this is based on what has been provided additionally by providers in their responses.

(Vodafone) told us they informed consumers on handset contracts that they can switch to a SIM-only deal after the minimum contract period has expired.

- 3.9 A number of providers, BT Mobile, EE and Three, have told us that customers will see no changes in price at the end of the minimum contract period.<sup>49</sup> Other providers (O2, Sky Mobile, Tesco Mobile and Virgin Mobile) said that customers that have agreements with the provider to pay for the handset separately will see a change in their bill once the device plan is paid off, and only the airtime plan remains.<sup>50</sup>
- 3.10 More recently, EE has launched an SMS notification letting customers know they can upgrade after the minimum contract period. The notification does not state that the customer is approaching or has reached the end of their minimum contract period. However, for those customers who have not consented to receive marketing, it includes a link to a webpage which informs the customer of their options at the end of the minimum contract period, namely to upgrade to a new handset, move to a SIM-only contract, or leave the provider.

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<sup>49</sup> Sky Mobile has told us that this is the case for airtime contracts.

<sup>50</sup> We did not specifically ask providers whether they send notifications as a result of this change in our formal information request. However, based on provider responses, we know that at least two providers (Virgin Mobile and Sky Mobile) do send notification to customers that this change has occurred.

Figure 2: Notifications by mobile providers

Provider	Is a notification sent?	Is the minimum contract period mentioned?	Does the provider send a notification when a price change occurs at the end of the minimum contract period?	Additional Comments
BT Mobile†	×	×	Not Applicable	<ul style="list-style-type: none"> <li>There are no price changes when a customer's contract reaches the end of the minimum contract period.</li> </ul>
EE	✓	×	Not Applicable	<ul style="list-style-type: none"> <li>There are no price changes when a customer's contract reaches the end of the minimum contract period.</li> <li>Customers are sent notifications when they are nearing the end of the minimum contract period to inform them that they can 'upgrade' to a new deal.</li> </ul>
O2	✓	✓	×	<ul style="list-style-type: none"> <li>Customers with offers on their tariffs which are limited to during the minimum term have the discount end and the price revert to the full contract price at the end of the minimum contract period.</li> </ul>
Sky Mobile	×	×	Not Applicable	<ul style="list-style-type: none"> <li>There are no price changes when a customer's contract reaches the end of the minimum contract period.</li> </ul>
Tesco Mobile	✓	×	×	<ul style="list-style-type: none"> <li>There are no price <i>increases</i> when a customer's contract reaches the end of the minimum contract period.</li> <li>Provider sends notifications for customers to upgrade their plan or calls customers to discuss options with the provider.</li> </ul>
Three	×	×	Not Applicable	<ul style="list-style-type: none"> <li>Any recurring discounts that are part of the customer's chosen plan at point of sale or added during the contract will remain on the customer's account until the customer upgrades or terminates the contract.</li> </ul>
Virgin Mobile	✓	✓	×	<ul style="list-style-type: none"> <li>Provider sends notifications for customers to upgrade their plan.</li> </ul>
Vodafone	✓	✓	✓	

Source: Provider response to formal information request

† Since responding to our formal information request, BT has told us that it now sends notifications to BT Mobile customers with handset contracts (not SIM-only). These do not mention the minimum contract period.

## Some consumers do not have the information they require to make informed decisions

3.11 Current Ofcom rules require providers to provide consumers with certain information on request at the time they purchase a service, which includes the duration of the contract,

and the conditions for renewal and termination, as well as details of prices and tariffs, and the services provided.<sup>51,52</sup>

- 3.12 However, the evidence shows that some consumers lack awareness in respect of this information, which is fundamental to their ability to make informed decisions about the services they purchase. In particular, some consumers lack awareness of when their minimum contract period ends, and what this might mean for the price they pay and the services they buy. They are also not clear about the options available to them at this point, including that they could make savings by taking up a new deal.
- 3.13 In our view, this shows that consumers do not always remember information provided to them when they purchased their service, which could have been up to 24 months previously (or longer where the consumer is already beyond the minimum contract period end date). We also understand that consumers may lack awareness where providers only communicate in general terms what will happen to the price they pay at the end of the minimum contract period.

### **Some consumers are unaware of their minimum contract period end date**

- 3.14 In order to understand the extent to which consumers are aware of the end of their minimum contract period, we asked participants in our 2018 quantitative consumer engagement research<sup>53</sup> when they thought their contract with their service provider ended. The results of this research, as well as our 2017 Switching Tracker, indicated both a lack of awareness and confusion regarding consumers' contractual status.
- 3.15 In our quantitative research, up to 26% of dual play, triple play or standalone pay TV consumers and 15% of mobile consumers appeared to lack awareness or be confused about their contract status.<sup>54</sup> More specifically, some consumers said that:
- they do not know *if* their contract had ended (13%-14% of each standalone pay TV, dual play or triple play customers and 6% of mobile customers);<sup>55</sup> or
  - they are within their minimum contract period, but were not clear when this would end (11%-13% of each dual play, triple play and standalone pay TV customers and 9% of mobile customers – see Figure 3 below).

<sup>51</sup> See GC 9.1 and 9.2 of the current General Conditions, which will be replaced by GC C1.2 as of 1 October 2018.

<sup>52</sup> Furthermore, providers are required to give all subscribers notice of any price changes that were not agreed at point of sale (see GC 9.6 of the current General Conditions and GCs C1.6 to C1.8 of the revised General Conditions to come into effect on 1 October 2018).

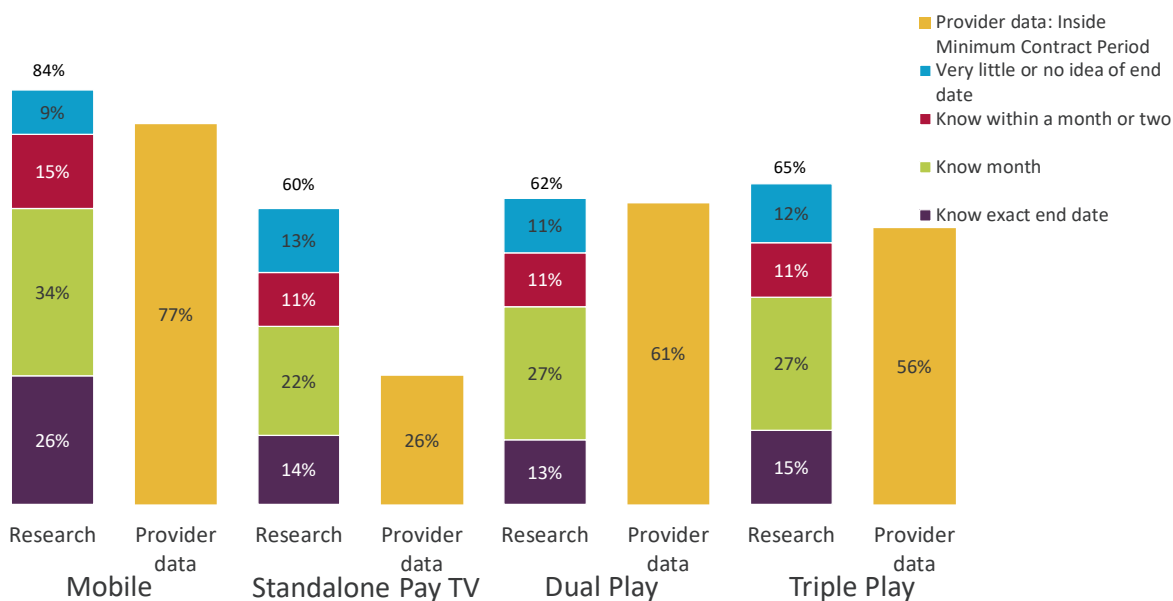
<sup>53</sup> Our research was focussed on services and bundles of services that have the largest subscriber numbers.

<sup>54</sup> Dual play – 25%; triple play – 26%; standalone pay TV – 26%. Ofcom's quantitative consumer engagement research 2018, conducted by Critical, slide 15. These percentage figures are the sum of the figures for "Unsure if in or out of contract" and "I have very little/no idea – but know I am still in contract".

<sup>55</sup> Ofcom's quantitative consumer engagement research 2018, conducted by Critical. Slide 15. Specifically, 13% of standalone pay TV, 14% of dual play and 14% of triple play customers reported that they do not know if their contract has ended.

- 3.16 Similarly, our switching tracker found that around one in ten (13%)<sup>56</sup> standalone landline customers did not know whether they were in-contract, and around one in five (19%) did not know when their contract ends.<sup>57</sup>
- 3.17 Separately, a comparison of our research and provider data illustrates that the proportion of consumers who reported being in-contract is higher than the proportion reported by providers to be within their minimum contract period, particularly in the standalone pay TV market (see Figure 3 below). This suggests some consumers incorrectly believe they are within their minimum contract period, when they are more likely not to be.<sup>58</sup>

**Figure 3: Consumers who reported being in-contract and consumers who providers reported to be in-contract**



Source: Ofcom's 2018 quantitative consumer engagement research, conducted by Critical. Slide 15; proportion of consumers who are within their minimum contract term from Pricing Trends report 2018, Fig 31, p.44 based on provider data. Mobile data is based on Ofcom analysis of provider data (see Annex 7 for further details). Note: Mobile base excludes SIM-only 30-day and Pay As You Go mobile.

### Some consumers are unaware of what happens after their minimum contract period ends

- 3.18 Our research suggests that some consumers are unaware of what happens after the end of their minimum contract period. In particular, we find that some consumers do not know that they (i) may face a price increase at the end of their minimum contract period; and (ii) do not need to pay a penalty or early termination charge after the end of their minimum

<sup>56</sup> Ofcom's switching tracker, 2017. The equivalent figure for standalone broadband was 8%.

<sup>57</sup> Ofcom's switching tracker, 2017. The equivalent figure for standalone broadband was 20%.

<sup>58</sup> If some consumers also reported being out of contract when they are in-contract, the extent of consumer confusion as implied by the data in Figure 3 is likely to be understated.

contract period. Some consumers thus lack an understanding of what will happen when they reach the end of their minimum contract period.

- 3.19 As shown in the first row of the table below, between 16%-18% of consumers (i.e. across each of mobile, standalone pay TV, dual play and triple play services) who said they are ‘in-contract’ do not know what will happen to their price at the end of their minimum contract period. This proportion is higher among those who lack awareness in relation to their contract status. In particular, the third row in the table shows how 23%-30% of consumers who have little idea as to when their minimum period contract ends, also do not know what will happen to the price they pay at that point.

**Figure 4: Proportion of consumers who do not know what will happen to the price they pay at the end of their minimum contract period**

<i>Group of consumers</i>	Mobile	Standalone Pay TV	Dual Play	Triple Play
<b>All in-contract consumers</b>	18%	16%	18%	17%
<b>In-contract consumers, who know their contract end date within a month or two</b>	16%	14%	16%	15%
<b>In-contract consumers, who have little/no idea as to when their contract ends</b>	30%*	24%	25%	23%

Source: Ofcom’s consumer engagement quantitative research 2018, conducted by Critical, slide 20 and bespoke analysis. Note: \* indicates low base so treat as indicative only.

- 3.20 In the 2015 end-of-contract notification research some participants were unaware that once their minimum contract period ends, they could switch to another provider without paying any additional charges<sup>59</sup> (9% of mobile, 12% of dual play, 11% of triple play and 15% of standalone pay TV).<sup>60</sup>

### **Some consumers are not clear about the options available to them after the minimum contract period and the savings that could be made**

- 3.21 Our research suggests that some consumers are unaware of the options available to them when their minimum contract period ends. In particular, we find that some consumers do not know that (i) they can switch to a different package or deal with their existing provider (including SIM-only deals for mobile), and (ii) that savings could be made by changing deal/package, either with their own or another provider. This means that some consumers fail to properly understand the options available to them as they come to the end of their minimum contract period.
- 3.22 In the 2015 end-of-contract notification research, we found that some participants were unaware that they could switch to a different package/deal with their current provider

<sup>59</sup> For example, early termination charges.

<sup>60</sup> Ofcom’s 2015 end-of-contract notification research. Slide 37.



once their contract ends (i.e. 7% of mobile, 11% of each of dual play and triple play and 13% of standalone pay TV).<sup>61</sup>

- 3.23 Our 2018 quantitative consumer engagement research found that a quarter of consumers on a mobile handset contract were unaware of the possibility of moving to a SIM-only deal at the end of their minimum contract period.<sup>62</sup> This lack of awareness was also evident in our qualitative research, where some participants on a mobile handset contract ‘discovered’ they could make substantial savings by switching to a SIM-only deal.<sup>63</sup>
- 3.24 Further, consumers who were unaware of the end of their minimum contract period (i.e. consumers who do not know if their minimum contract period has ended, or lack awareness of when their minimum contract period ends), were among those most likely to agree that ‘it is difficult to know whether any cost savings could be achieved from changing deal or provider’.<sup>64</sup> This was true across each of dual play, triple play and standalone pay TV services analysed in our 2018 quantitative consumer engagement research.<sup>65</sup> Ofcom’s Switching Tracker 2017 also found that three in five (60%) standalone landline customers agreed that ‘it is too hard to work out if I would save or not if I switched provider’.<sup>66</sup>
- 3.25 Similarly, there was a perception among consumers who said they were out-of-contract that signing up to a new deal with their existing or an alternative provider would not result in any savings. In particular, up to a quarter of out-of-contract consumers for each of the standalone pay TV (17%), dual play (24%), and triple play (24%) services did not think they could make any savings by signing up to a new contract.<sup>67</sup>
- 3.26 Communications markets are complex and the perception amongst some consumers that no savings can be made by signing up to a new deal at the end of their minimum contract period is likely to limit their ability to make informed decisions about their existing deal. While we cannot say with certainty that all of these consumers would achieve savings by doing so, our analysis (see below) suggests that: (i) consumers of dual play, triple play and standalone pay TV who are out-of-contract tend to spend more on average than those who are in-contract; and (ii) consumers who go out-of-contract when purchasing mobile services with a handset on average pay more than those on SIM-only deals

### Some consumers incur a penalty due to this lack of information

- 3.27 The evidence shows that many consumers are on a contract with an automatic change to the price after their minimum contract period ends. For those consumers who allow their contract to roll-over onto out-of-contract terms due to the lack of awareness we identify

<sup>61</sup> Ofcom’s 2015 end-of-contract Notification Research. Slide 37.

<sup>62</sup> Ofcom’s quantitative consumer engagement research 2018, conducted by Critical. Slide 29.

<sup>63</sup> Ofcom’s qualitative consumer engagement research 2017, conducted by Futuresight (p. 29).

<sup>64</sup> Ofcom’s quantitative consumer engagement research 2018, conducted by Critical. Slide 12.

<sup>65</sup> Base for mobile too low to report.

<sup>66</sup> Ofcom Switching Tracker 2017. The equivalent figure was 53% of standalone broadband customers. Standalone landline customers were significantly more likely than average (53%) to agree with this statement.

<sup>67</sup> Ofcom’s quantitative consumer engagement research 2018, conducted by Critical. Slide 53.

above, we are concerned that they are unable to avoid unexpected increases to the price they pay or reductions in the service they receive.

- 3.28 More generally, the evidence suggests that there is often a financial penalty for consumers who are out-of-contract. Moreover, the pace at which communication services and prices progress over time suggests that consumers who stay out-of-contract may not benefit from the best deals available. As such, we are concerned that consumers who lack awareness stay out-of-contract longer than they otherwise would, and thus pay higher prices and fail to benefit from better service packages.
- 3.29 Finally, we recognise that there are consumers who are aware of this information, but we note that they have to incur time and effort to monitor, retain and search for this information.

### **Some consumers are unable to avoid unexpected price and service changes**

- 3.30 The evidence suggests that a significant number of consumers are on contracts which have an automatic price increase at the end of the minimum contract period. We are concerned that consumers who lack information allow their contract to roll-over, and as a result they are not in a position to avoid such unexpected price increases.
- 3.31 We asked major providers to report information in relation to the number of customers<sup>68</sup> who are on contracts with automatic price increases,<sup>69</sup> both within and at the end of the minimum contract period.<sup>70</sup>
- 3.32 As shown below, this data suggests that a significant proportion of dual and triple play customers are on contracts where the price increases automatically at the end of the

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<sup>68</sup> For standalone landline, the total subscriber figure is taken from the [2017 Review of the market for standalone landline telephone services statement](#) (para. 2.5, p.7). For the other services, our estimates of the number of customers (either in total or by service) throughout this document are based on the data we collected for the purpose of this proposal. In order to arrive at these estimates, we gross-up the aggregate customer numbers for a given service as implied by the data we collected from providers using our formal powers so as to take into account customers using providers for a given service that did not submit data to us. The factor we use to gross-up these aggregate consumer figures for a given service is based on the market share estimates for these providers as implied by [3<]. We recognise that alternative methods may arrive at different estimates, particularly given the use of survey data to measure market shares. For example, to the extent that the market shares understate the size of the providers who responded to our formal request, our grossing-up factor would be too high and our estimates of the customer total would be overstated. For further details, see Annex 7.

<sup>69</sup> In our request, we asked providers to exclude from 'an automatic price increase' any RPI price changes.

<sup>70</sup> By an automatic price increase, we mean the occasions where the price increases either during or at the end of the minimum contract period, as per the agreement signed when the contract is taken out. Hence, a provider does not need to inform the consumer again at the time when such a price increase comes into effect. At Figure 1 and Figure 2 we include an overview of providers' practices in terms of price communication at the end of customers' minimum contract period.

minimum contract period. While this proportion is somewhat lower for standalone pay TV, [redacted].<sup>71</sup>

**Figure 5: Proportion and number of customers on deals with an automatic price increase at the end of the minimum contract period**

Service	Proportion of in-contract customers <sup>72</sup>	Number of customers (millions)
Dual Play	75%	c.5.4
Triple Play	57%	c.3.6
Standalone pay TV <sup>73</sup>	[redacted]%	[redacted]
Mobile with SIM-only	11%	c.1.0
Mobile with handset	3%	c.0.6

Source: Ofcom analysis of provider data (see Annex 7 for further details).

3.33 Some consumers may experience changes to services at the end of the minimum contract period. Similar to our concerns about price increases, we also have concerns that consumers who lack information about this may allow their contract to roll-over, and as a result they are not in a position to avoid such changes.

### There is often a financial penalty to staying out-of-contract

3.34 The evidence we collected confirms that out-of-contract consumers who purchase dual play, triple play and standalone pay TV on average spend more than consumers who are in-contract. Likewise, we find that consumers on a mobile handset contract who are out-of-contract spend more than in-contract consumers who are on a SIM-only deal. This would suggest that consumers often incur a financial penalty for staying out-of-contract. The evidence also shows that this affects a significant number of consumers, as provider data we collected implies that a considerable proportion of consumers are out-of-contract for each of the services we investigated.

### In-contract and out-of-contract spend

3.35 We asked providers to report the average spend for customers who are in and out-of-contract. As illustrated in the table below, the data shows that the average spend by consumers of dual play, triple play and standalone pay TV who are out-of-contract is substantially higher than the spend by corresponding customers who are in-contract. In particular, out-of-contract dual play customers spend on average 19% more than those who are in-contract, where this figure is 24% for triple play and [redacted]% for standalone pay TV. This is in contrast to mobile services and standalone landline, where we find that the

<sup>71</sup> [redacted]

<sup>72</sup> There are differences across individual providers in the proportion of customers who are on deals with a price increase at the end of the minimum contract period only. For Dual Play, the proportions across providers are: [redacted]. For Triple Play, the proportions across providers are: [redacted]. For Mobile with SIM-only, the proportions are [redacted] for other providers. For Mobile contracts with a handset, the proportions are [redacted] for other providers.

<sup>73</sup> [redacted]

average spend for in-contract customers is higher than the average spend of customers who are out-of-contract.

**Figure 6: Average spend of customers by contract status**<sup>74</sup>

Service	Average in-contract spend (£ per month)	Average out-of-contract spend (£ per month)	Out-of-contract relative to in-contract spend
Dual Play	£35	£41	19% higher
Triple Play	£52	£65	26% higher
Standalone Pay TV	£[<del>3</del>]	£[<del>3</del>]	[<del>3</del>]% higher
Standalone landline	£26	£24	6% lower
Mobile SIM-only	£17	£15	8% lower
Mobile handset	£31	£22	27% lower

Source: Ofcom analysis of provider data (see Annex 7 for further details). The average spend data for standalone landline is from the Pricing Trends report 2018.<sup>75</sup>

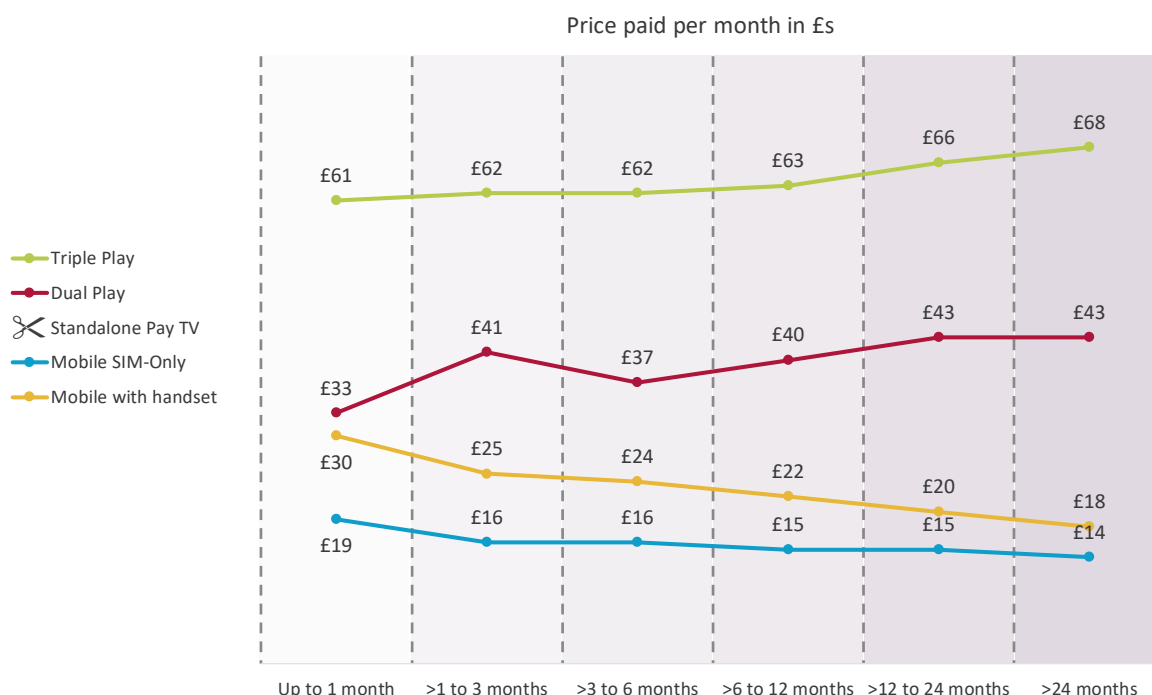
3.36 Further, we asked providers to report the average spend of out-of-contract customers according to the time elapsed since the end of their minimum contract period. As illustrated in Figure 7 below, the data suggests that on average consumers of dual play, triple play, standalone pay TV and mobile services spend more, the longer they have been

<sup>74</sup> The average spend of in-contract and out-of-contract customers implied by the provider data [<del>3</del>] is similar to the corresponding numbers in the 2018 Pricing Trends report for Q3 2017. The latter found an average monthly spend of £32 for customers in-contract and £39 for customers out-of-contract for dual play, £51 for customers in-contract and £63 for customers out-of-contract for triple play, and £36 for customers in-contract and £45 for customers out-of-contract for standalone pay TV.

<sup>75</sup> Figure 30: 'Average monthly spend for customers within the minimum contract period and outside the minimum contract period, by service type/combination: Q3 2017', p.44 in the Pricing Trends report.

out-of-contract. In contrast, mobile customers tend to spend less on average the longer they have been out-of-contract.

**Figure 7: Average spend of out-of-contract customers, by service and length of out-of-contract**



Source: Ofcom analysis of provider data (see Annex 7 for further details).

3.37 This evidence should be interpreted carefully, as the difference in the average spend of out-of-contract and in-contract customers may under or overstate the extent to which customers pay higher prices after the end of their minimum contract period. This is because of the potential distinction between the average spend and the average price. For example, the average spend for a service package could be higher in part because the group of out-of-contract customers is generally buying more services within that package compared with the corresponding group of in-contract customers. If so, at least part of the reported difference in average spend could be explained by this difference in the composition of the package, rather than solely reflecting that out-of-contract customers pay higher prices for the same package of services. Alternatively, if the group of out-of-contract customers is generally buying fewer services within a package than the corresponding group of in-contract customers, the difference in the average prices they pay for these services could be larger than the reported difference in average spend.

3.38 We recognise that differences may exist in the average packages purchased by in-contract and out-of-contract customers of dual play, triple play packages and standalone pay TV.<sup>76</sup> However, we consider that the difference between the average in-contract and out-of-contract spend reported in the table above could be as a result of out-of-contract consumers of these services: (i) being subject to a price increase at the end of their

<sup>76</sup> In dual and triple play, it is possible that a larger proportion of in-contract customers purchase bundles which include superfast broadband. If this is the case, this would imply that the difference between the average in-contract and out-of-contract spend may understate the extent to which customers pay higher prices when they go out-of-contract.

minimum contract period; and / or (ii) failing to secure promotional discounts providers offer to new customers, or ‘retention’ or ‘loyalty’ discounts their existing provider may offer to customers who negotiate or threaten to leave.<sup>77</sup>

- 3.39 The situation is different in the mobile market. In contrast to dual play, triple play and standalone pay TV, the spend of mobile customers who are out-of-contract is on average lower than that of mobile customers who are within their minimum contract period. This is likely to be the result of a number of factors. First, only a small proportion of mobile contracts are subject to an automatic price increase at the end of the minimum contract period (see Figure 5 above). In contrast, the monthly price for some mobile customers may fall at the end of the minimum contract period, if the charge for the handset contract is automatically removed at the end of the minimum contract period.<sup>78</sup> Second, the higher spend by in-contract customers could in part be due to a compositional effect, as providers offer deals with larger data packages and deals with more expensive phones over time. Mobile customers who are in-contract may have taken up recent contracts which are on average more expensive than older contracts (more likely to be used by customers who are out-of-contract).<sup>79</sup>
- 3.40 Separately, we note that consumers on combined airtime and handset deals pay a price that reflects the cost of the handset. When these consumers continue to pay the same price after the end of their minimum contract period, remaining out-of-contract means they pay a significantly higher price than if they switched to a SIM-only deal. As set out above, many mobile customers lack awareness of the options available to them, including moving to a cheaper SIM-only deal, and the savings or improved services that they could benefit from. This is consistent with the spend data reported in Figure 6, which shows that the average spend of out-of-contract customers who are on a mobile handset contract is higher than the average spend of SIM-only customers who are in-contract.
- 3.41 Finally, we also find that the average in-contract spend for standalone landline customers is higher than that of out-of-contract customers. It is not immediately clear why this difference occurs, but given the recent changes to prices in this market we do not consider it relevant to our analysis.<sup>80</sup>

### **A significant proportion of consumers are outside their minimum contract period**

- 3.42 The relevance of the difference in average spend between in-contract and out-of-contract consumers for dual play, triple play and standalone pay TV cannot be understated. Data

<sup>77</sup> This is also consistent with an analysis of actual offers available in the market, included at Annex 6.

<sup>78</sup> Particularly where there are separate contracts for the handset and airtime element of the mobile deal.

<sup>79</sup> This is suggested by the fact that the type of handset and inclusive data allowances are the most important factors in determining the price of pay-monthly mobile services. Also, there has been an increase in both handset functionality as well as the proportion of mobile tariffs offering large or unlimited data services over time. (See the 2018 Pricing Trends report, pp. 13-15.)

<sup>80</sup> BT has recently lowered the monthly price paid by its voice-only landline customers (customers that do not purchase broadband) by £7. Post Office has also lowered the price of its standalone voice product to new customers. This change means that voice-only consumers could make savings by signing up to a new deal with a different provider. Those consumers that do not bundle their voice and broadband services could make considerable savings by bundling their services.

collected from major providers<sup>81</sup> and our recent Pricing Trends report indicates that a significant proportion of consumers on dual play, triple play, standalone landline and standalone pay TV products are outside their minimum contract period.<sup>82</sup>

- 3.43 As illustrated in the table below, around 40% of dual play and triple play customers are currently out-of-contract, which we estimate equates to ~4.3 million and ~4.4 million customers respectively.<sup>83</sup> The proportion of standalone landline customers who are out-of-contract is 87%, which we estimate equates to ~2.3 million customers.<sup>84</sup> From our Pricing Trends report, the proportion of standalone pay TV customers who are out-of-contract is ~74%.<sup>85,86</sup>
- 3.44 In terms of mobile contracts, the picture is somewhat different depending on the type of contract taken. In particular, while 44% of SIM-only customers (or ~6.8 million) are out-of-

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<sup>81</sup> We have asked for information from the following providers. [X]

<sup>82</sup> The proportions of in-contract and out-of-contract consumers implied by the information request data [X] are similar to the proportions reported in the 2018 Pricing trends for communications services in the UK report for Q3 2017. In particular, the Pricing Trends report found that for: (i) dual play, 61% of customers are in-contract, and 39% are out-of-contract; (ii) for triple play, 56% of customers are in-contract, and 44% are out-of-contract; (iii) for standalone pay TV, 26% of customers are in-contract, and 74% are out-of-contract; and (iv) for standalone landline, 13% of customers are in-contract, and 87% are out-of-contract.

<sup>83</sup> Our analysis also indicates that ~2.6 million dual play customers (i.e. 23% of the total) and ~2.4 million triple play customers (i.e. 23% of the total) have been out-of-contract for more than one year.

<sup>84</sup> Ofcom. Pricing trends for communications services in the UK, May 2018.

<sup>85</sup> Ofcom. Pricing trends for communications services in the UK, May 2018.

<sup>86</sup> This reflects the data we gathered from providers' responses to our formal information requests. This data shows that the proportion of standalone pay TV customers who are out-of-contract is [X]%, which we estimate equates to [X] million customers. The proportion of customers who are out-of-contract for more than 2 years is [X]%, which accounts for [X] million customers.

contract, this proportion is substantially lower for customers on contracts that include a handset (we discuss the mobile market further below).

**Figure 8: Estimated number of customers, by contract status**

	Dual Play	Triple Play	Standalone Pay TV	Standalone landline	Mobile SIM-only	Mobile with handset
<b>Number of customers (in millions)</b>						
<b>Total</b>	c.11.5	c.10.6	[<del>]</del>	c.2.6	c.15.6	c.28.0
<b>Out-of-contract (any duration)</b>	c.4.3	c.4.4	[<del>]</del>	c.2.3	c.6.8	c.3.7
<b>Estimate of proportion (%) of customers who are out-of-contract</b>						
<b>Any duration</b>	37%	41%	[<del>]</del>%	87%	44%	13%
<b>Up to 1 month</b>	2%	3%	[<del>]</del>%		4%	1%
<b>1 month to 3 months</b>	3%	4%	[<del>]</del>%		5%	2%
<b>3 months to 6 months</b>	4%	4%	[<del>]</del>%		6%	2%
<b>6 months but to 12 months</b>	7%	8%	[<del>]</del>%		9%	3%
<b>12 months to 24 months</b>	9%	10%	[<del>]</del>%		10%	3%
<b>More than 24 months</b>	14%	13%	[<del>]</del>%		10%	3%

Source: Ofcom analysis of provider data (see Annex 7 for further details). The total number and proportion of out-of-contract customers for standalone landline are from the 2017 Review of the market for standalone landline telephone services statement and the Pricing Trends report 2018.<sup>87,88</sup> Note: Due to rounding, the percentage of customers who are out-of-contract for different durations does not necessarily add up to the overall percentage of customers who are out-of-contract. For standalone landline, we do not have information regarding the proportion of customers who are out-of-contract by duration.

### Some consumers do not benefit from improvements in services and price once their minimum contract period ends

- 3.45 In addition to the evidence that consumers who are out-of-contract are generally spending more, we are concerned that consumers who do not move to a new deal may not benefit from the continuing improvement in services and prices over time.
- 3.46 The communications market is constantly evolving and developing at a fast pace. Consumers who search for a new deal at the end of their minimum contract period can benefit from improvements in the choice and value available in the market. For example:
- **Many people could upgrade their broadband at no extra cost.** As superfast broadband coverage continues to increase,<sup>89</sup> the gap has narrowed between the price of superfast and standard broadband services.



- **Mobile users are getting more for their money.** Average data consumption per mobile subscription has grown significantly over time as mobile data service use has increased, however, average spend has declined. This is partly due to the availability of pay-monthly tariffs with larger inclusive data allowances.
- **There are improvements in the service and prices paid for pay TV.** Consumers signing up to the latest deals may benefit from the added functionality and improved user experience of higher-spec TV set-top boxes and/or packages which allow them greater flexibility in accessing and paying for what they want to view. Moreover, the price for pay TV purchased as part of a bundle has decreased. For example, it is notable that new customers purchasing triple play bundles rarely pay the standard price due to promotional discounting and gifts.<sup>90</sup>

3.47 In light of such developments, we are concerned that consumers that do not search for a new deal as they approach the end of their minimum contract period may not benefit from these developments. While it would be difficult to quantify this, the speed of developments and changes in the communications market means that consumers who remain out-of-contract are likely to be missing out on better deals. In particular, we note that [§<] % of standalone pay TV customers who are out-of-contract have been so for more than two years and therefore are more likely to be missing out from the benefits that new packages provide.

### Some consumers have to spend time and effort to proactively seek out contract status information

3.48 Even for those consumers that have some awareness of their contract status, these consumers have to incur time and effort to retain, monitor and seek out this information.

3.49 As set out above, consumers are made aware of contract terms at the point of sale. However, as contracts tend to have a minimum period of one to two years, consumers must expend effort to recall these details over a prolonged period of time. In addition, we understand that, when a customer purchases a service, providers may not always communicate the extent of the price increase that will occur at the end of the minimum contract period, and rather refer to it only in general terms.

3.50 In principle, consumers could aid their memory, or search for the information, by contacting their provider. Providers in response to our information requests told us that<sup>91</sup>:

- they provide minimum contract period information to customers in the ‘welcome letter’ or in the contractual terms of agreement;

<sup>87</sup> Paragraph 2.5, p.7.

<sup>88</sup> Figure 31: ‘Average customer tenure and proportion of customers outside the minimum contract period, by service’, p.44.

<sup>89</sup> It is now available to 93% (27.2m) of UK premises. Ofcom, *Connected Nations Update*, Spring 2018:

[https://www.ofcom.org.uk/data/assets/pdf\\_file/0017/113543/Connected-Nations-update-Spring-2018.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0017/113543/Connected-Nations-update-Spring-2018.pdf).

<sup>90</sup> Ofcom, *Pricing trends for communications services in the UK*, May 2018.

<sup>91</sup> We asked providers to tell us whether their customers can access information on whether they are within or outside of their minimum contract period, and if they are within this period, when that period ends. Providers’ responses indicate that this information is available in a number of cases, but not necessarily signposted or presented in a consistent way to

- they also provide access to end-of-contract information via an online platform (website or app) and/or via their customer call centres;<sup>92</sup> and
- with the exception of three providers, Sky Mobile, Tesco Mobile and Virgin Mobile, most mobile providers provide information on the minimum contract period end date via their smartphone application.

3.51 However, consumers incur time and effort to proactively search for this contract information, some of which may not be available without actually speaking to their provider (such as precise price increases). Moreover, in the absence of an external trigger, consumers need to set reminders to check their contract status against this information to be able to act on it in a timely manner.

3.52 As illustrated in the last row of the table below, we consider that the group of consumers who incur such time and hassle is likely to be sizeable – it aggregates to a rough estimate of more than 18 million customers across all services, and on the basis of our 2017 engagement index.<sup>93</sup>

**Figure 9: Estimated number of engaged customers, by service**

<i>Consumer base</i>	Dual Play	Triple Play	Mobile	Standalone Pay TV	Standalone landline
<b>Estimated number of customers (million)</b>	11.5	10.6	43.6	[X]	2.6
<b>2017 engagement index</b>	36%	41%	22%	26%	8%
<b>Number of customers who engaged (million)</b>	4.1	4.4	9.6	[X]	0.2

Source: Estimated number of subscribers, except for standalone landline, is from Ofcom analysis of provider data (see Annex 7 for further details) while that for standalone landline is from the [2017 Review of the market for standalone landline telephone services statement](#), p.7; the 2017 engagement index proportions are from Ofcom's Switching Tracker 2017.

Note: The number of subscribers who engaged in 2017 for any service is the product of the estimated number of subscribers and the engagement index proportion for that service.

3.53 The evidence we have indicates that 16% of consumers who said they were in-contract reported to have searched for their minimum contract period end date, or whether their minimum contract period has ended. Nearly all of these consumers said that they were able to locate this information<sup>94</sup> and 27% to 32% of in-contract consumers (depending on

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their customers. For example, the end date for the minimum contract period is often referred to as the point from which the customer can 'upgrade' (rather than when this period ends).

<sup>92</sup> Post Office do not provide this information online, but customers are able to call the customer contact team to access this information.

<sup>93</sup> Ofcom is in the process of reviewing the engagement index, as such the engagement statistics shown here may be subject to revision. The methodology of the current engagement index can be found on pages 165-167 of the following document: [https://www.ofcom.org.uk/data/assets/pdf\\_file/0029/98615/access-inclusion-research-annex.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0029/98615/access-inclusion-research-annex.pdf).

<sup>94</sup> Ofcom's quantitative consumer engagement research 2018, conducted by Critical, slide 17. Data is an average across markets.

the service) said they did not need to look for the end date, as they had already made a note of it.<sup>95</sup>

- 3.54 Even for these consumers we consider that there is time and effort required to keep track of the relevant contract information, and as set out above, they would need further effort to understand the implications of their contracting ending. This is consistent with the fact that across the services, 88%-92% of consumers who said they had at least some idea of when their contract would end, also said they would find it helpful to receive an end-of-contract notification.<sup>96</sup>

## Small Businesses

- 3.55 Our 2017 qualitative consumer engagement research included respondents who were sole traders and / or worked from home and found that they responded in a similar way to residential consumers.<sup>97</sup>
- 3.56 Our 2016 SME research found that for those on business contracts, a significant minority said they did not know how long their minimum contract period was (15% for landline, 12% for broadband, 9% for mobile), similar to our findings for residential consumers (as highlighted above).<sup>98</sup>
- 3.57 We also found from this research that many business respondents were on residential contracts. These participants thought their use of communications services was not high enough to warrant a more expensive business contract and residential contracts often offered a cheaper solution.<sup>99</sup> Small Businesses on residential contracts are already covered by our analysis of the residential market.
- 3.58 In our July 2017 CFI, we asked stakeholders to provide input into the possible scope for SMEs to be included in our consumer engagement work. In its response, Sky suggested that Ofcom seek a better understanding of the engagement levels and drivers of SME customers, while Moorhouse Consulting highlighted that the SME market is significantly different to the residential market. BT said that SME customers often have support options and will put effort into making informed decisions; however, it accepted that smaller businesses may not have as much support, but are likely to be very cost conscious, and may purchase consumer products. Virgin Media stated that Ofcom should keep the scope limited to consumers and micro businesses of up to 10 employees, in line with the General Conditions of Entitlement (GCEs). The Federation of Small Businesses, First Utility, and another respondent [X] highlighted that small businesses share some similarities with

<sup>95</sup> Ofcom's quantitative consumer engagement research 2018, conducted by Critical, slide 17.

<sup>96</sup> 88% for dual play, 92% for triple play, 88% for mobile phone and 89% for standalone pay TV. Base includes consumers who reported to be in-contract, and knew when their contract ends at least within a month or two. Source: Ofcom's consumer engagement quantitative research 2018, conducted by Critical, bespoke analysis.

<sup>97</sup> Ofcom's consumer engagement qualitative research 2017, conducted by Futuresight.

<sup>98</sup> Ofcom's 2016 quantitative SME research, bespoke analysis of small business customers (with between 1 and 9 employees) on a business contract for each service.

<sup>99</sup> Ofcom's 2016 quantitative SME research found that a significant proportion of small businesses were not on a business contract for one or more of their communications services. Among small businesses, 51% of those with a mobile service, 65% of those with an internet service, and 69% of those with a landline service were on a business contract.

residential consumers, including the way in which they interact with communications markets. The Communications Consumer Panel raised that this subset is particularly susceptible to the types of harm that affect domestic consumers.<sup>100</sup>

3.59 We also collected information from business landline, broadband and mobile providers about whether they currently send end-of-contract notifications to SME customers.<sup>101</sup>

3.60 Our analysis is summarised in Figure 10 below. This suggests that only one of the providers we asked (BT) sends end-of-contract notifications to SMEs for the services they offer which specifically reference the minimum contract period. Another provider (O2) stated that it sends end-of-contract notifications, but these do not mention the minimum contract period, instead telling the customer they are able to 'renew' their contract. None of the other providers we asked sent written notifications, but they did note the availability of this information to customers who are willing to proactively check their welcome information or engage via a customer contact centre.

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<sup>100</sup> Ofcom, *Call for inputs: Helping consumers to engage in communications markets*, July 2017.

<sup>101</sup> In our information request we defined SMEs as 'a business for which no more than 250 individuals work (whether as employees, volunteers or otherwise)'.

Figure 10: Information on SME notifications

Provider	Is a notification sent?	Is the minimum contract period mentioned?	Additional comments
BT	✓	✓*	<ul style="list-style-type: none"> <li>*The minimum contract period is <i>only</i> mentioned in notifications sent to customers who have <i>opted-out</i> of receiving marketing material.</li> <li>Customers who have <i>opted-in</i> to marketing receive information about what would happen if the customer did nothing (e.g. if their tariff would become more expensive)</li> </ul>
O2	✓	✗	<ul style="list-style-type: none"> <li>Customers receive upgrade and renew notifications which encourage them to call the provider and discuss their options.</li> </ul>
TalkTalk	✗	✗	<ul style="list-style-type: none"> <li>Minimum contract period information is available via the online portal and the provider's customer contact team.</li> </ul>
Verastar	✗	✗	<ul style="list-style-type: none"> <li>Customers with Unicom, Clear Business or Kinex are contacted by phone when they are approaching the end of the minimum contract period to discuss contract options.</li> <li>Minimum contract period information is available in the customer's contractual terms of agreement, the letter sent to customers upon activation of the service or via a call to their customer contact team.</li> </ul>
Virgin Media	✗	✗	<ul style="list-style-type: none"> <li>The provider runs campaign-driven proactive marketing to re-engage and re-contact customers.</li> <li>Minimum contract period information is available on the customer's contract agreement, or via their customer contact team.</li> </ul>
Vodafone	✗	✗	<ul style="list-style-type: none"> <li>Around [X] of customers (which have opted-in to marketing) receive a call to discuss their upgrade options, and if a customer cannot be reached, they will be contacted by email.</li> <li>Customers can access minimum contract period information in store, or by calling the customer contact team. Some customers can access this information through the provider's app.</li> </ul>
XLN	✗	✗	<ul style="list-style-type: none"> <li>Customers can find information about their minimum contract period by contacting the customer contact team by phone, email, social media, their online accounts, or in their welcome letter.</li> </ul>

Source: Provider response to formal information request.

- 3.61 Given our research and the previous approach taken by Ofcom in relation to Small Businesses (those with no more than ten individuals), we consider that these businesses are likely to behave in a similar way and raise similar concerns to residential consumers. This would mean that in addition to potentially not knowing when their minimum contract period ends, they are similarly unlikely to know what happens when it does, their options and that they could make savings (and/or find a better deal to suit their needs). Therefore, as with residential consumers, Small Businesses are likely to suffer harm from paying higher prices, not benefiting from improvements in services and price or from having to proactively seek out this information.
- 3.62 In the General Conditions of Entitlement, Small Businesses employing no more than ten individuals (whether as employees, volunteers or otherwise) often have the same

regulatory protections as residential customers. In contrast, larger businesses, while enjoying the same basic protections (such as the right to minimum information regarding their contracts, a minimum contract period of 12 months, and a minimum notice period of one month), do not need certain additional protections that the GCs extend to residential consumers and Small Businesses (such as the requirement for providers to seek consent for each new specific minimum contract period, before renewing a contract). As noted in our September 2017 statement on our review of the GCs, large businesses generally have greater bargaining power than Small Businesses and consumers, and are therefore less likely to experience harm in this area.<sup>102</sup> Within the scope and make-up of small and medium sized enterprises, recent government statistics showed that small businesses of 0-9 individuals made up 90% of SMEs.<sup>103</sup>

## Our assessment of consumer harm

- 3.63 We have set out our concerns above that most providers do not notify their customers, at the appropriate time, of important information about the services they buy. In particular, they are not notified that they are approaching the end of their minimum contract period; what this means for their price and the services they buy; and the options available to them after this point, including the potential to make savings.
- 3.64 While some providers communicate with their customers near the end of their minimum contract period, we consider that the extent of current communications is not sufficient to ensure that consumers have the right information at the right time to ensure they can make informed decisions. First, most providers do not send notifications to customers which make clear that customers have reached, or are about to reach, the end of their minimum contract period. Second, the content of this communication is not consistent across providers, and often excludes important information, such as the change in service and price at the end of the minimum contract period. Finally, communications do not make clear to customers what coming to the end of their minimum contract period means and the options that are available to them at this point.
- 3.65 The evidence shows that some consumers lack awareness in respect of certain information that is fundamental to their ability to make informed decisions about their services. In particular:
- **Many don't know the status of their contract.** Up to 26% of people taking landline, broadband and pay TV services (standalone or as a bundle) lack awareness or are confused about their contract status.<sup>104</sup> The same is true of 15% of mobile phone customers.

<sup>102</sup> Ofcom, *Review of the General Conditions of Entitlement*, September 2017:

[https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0026/106397/Statement-and-Consultation-Review-of-the-General-Conditions-of-Entitlement.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0026/106397/Statement-and-Consultation-Review-of-the-General-Conditions-of-Entitlement.pdf). Section 7.18.

<sup>103</sup> ONS UK Business Stats 2017; Table 10 - Number of VAT and/or PAYE based enterprises in districts, counties and unitary authorities within region and country by employment size bands

(<https://www.ons.gov.uk/businessindustryandtrade/business/activitysizeandlocation/datasets/ukbusinessactivitysizeandlocation>).

<sup>104</sup> The research did not cover standalone landline, standalone broadband, or quad play packages.

- **Some are unclear about future charges.** Around a quarter of people who do not know when their contract ends, also do not know what will happen to the price they pay when it does; and
- **People often don't understand their options.** Communications markets are complex by nature and some consumers do not understand what coming to the end of their minimum contract period means. They are also unaware of the options, savings or benefits available to them. Around one in ten are unaware that they could switch to a different deal with their current provider once their contract ends. One quarter of customers on a mobile handset contract are unaware of the possibility of moving to a SIM-only deal. And up to a quarter of out-of-contract customers do not think they could make any savings.

3.66 As most providers do not inform their customers at the appropriate time of important information about the services they buy, we consider that this lack of information leads to a significant number of consumers moving to rolling out-of-contract terms. The evidence we have gathered indicates that, as a result, many consumers pay higher prices than they need to, and do not benefit from improved service packages:

- Many consumers are subject to automatic price increases, or service changes, at the end of the minimum contract period. We estimate that more than 10 million customers are on deals with an automatic price increase at the end of the minimum contract period. Due to their lack of awareness, many consumers go out-of-contract and are unable to avoid these changes.
- More generally, consumers who lack awareness cannot make informed decisions on when and whether they should search for a better deal. We are concerned that some of these consumers are unable to make savings, or benefit from an improved service package, at the end of their minimum contract period. For example, customers taking a bundle of landline and broadband services spend, on average, around 20% more when they are out-of-contract. Also, certain mobile consumers continue to pay the same price (which includes the cost of handset) after the end of their minimum contract period, which could be significantly higher than the price they would pay if they switched to a SIM-only deal.

3.67 For those consumers that are aware of this information, we consider it unreasonable that they have to incur time and effort to retain, monitor and seek out this information.

3.68 Based on the evidence set out in this section<sup>105</sup>, our assessment is that consumers experience harm as a result of not being notified by their providers, at an appropriate time, of important information relevant to coming to the end of their minimum contract period.

## Intervening to protect consumers' interests

3.69 We consider below the options that would be effective at addressing the issues we have identified in order to achieve our policy objectives.

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<sup>105</sup> The evidence we rely on is specific to those services and bundles of services that have the largest subscriber numbers. We have no reason to believe that other combinations of services, e.g. quad play, would change our assessment.

- 3.70 As set out in Section 2, our policy objectives are to ensure that consumers are informed:
- at an appropriate time when their minimum contract period is coming to an end, and of any changes to price or services that will occur as a result; and
  - that their minimum contract period has already come to an end if they were not previously informed of this.
- 3.71 The two main options we evaluate below are: (1) Maintaining the status quo; and (2) Requiring providers to send end-of-contract notifications and a one-off out-of-contract notification to their residential and Small Business customers.

### **Option 1: Maintaining the status quo**

- 3.72 In accordance with our regulatory principles, we have considered whether maintaining the status quo is likely to fulfil our policy objectives.<sup>106</sup> We have set out above why we consider that residential consumers' and Small Businesses' interests are not currently being met by the existing regulatory measures in place and the practice of most providers. In our view, it is not reasonable that most providers do not notify customers of when their minimum contract period ends, what this means for their price and the services they buy, and the options available to them after this point.
- 3.73 We do not have evidence that the harms we have identified will reduce of their own accord or that providers will improve the information they provide to their customers in the absence of regulatory change. Therefore, we do not consider that our policy objectives will be achieved if the status quo is maintained.
- 3.74 Our provisional view is that, in order to ensure our policy objectives are met, and the respective harm areas, in terms of consumers paying higher prices and not benefiting from deals that could improve their package or save them money, are addressed, changes are likely to be necessary.

### **Option 2: Requiring providers to send end-of-contract notifications and a one-off out-of-contract notification**

- 3.75 Under this option, residential and Small Business customers nearing the end of their minimum contract period would receive a communication from their provider with information that we consider important in order to meet our policy objectives and address the harm we have identified (we discuss the precise information we consider appropriate in Section 4). Also under this option, residential and Small Business customers already beyond their minimum contract period would receive a one-off out-of-contract notification if they have not been informed previously of all of the information that we consider important.

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<sup>106</sup> See Ofcom's regulatory principles: <https://www.ofcom.org.uk/about-ofcom/what-is-ofcom>



- 3.76 This information would ensure consumers are informed of the status of their contract at an appropriate time so that they are able to make informed decisions about the services they buy. They would be aware of:
- when they are no longer tied to their minimum contract period and so can engage and change their contract or switch to another provider without penalty; and
  - the implications if they do not engage and remain on their existing deal. In particular, of any increase to their price, or a loss in the service they receive, that may occur from the end of that period. This would also include information to address lack of understanding of what coming to the end of their minimum contract period means in terms of the options available, and the possible savings they could achieve from moving to a new deal.
- 3.77 The end-of-contract notification would be sent to customers at an appropriate time, which would be when they are nearing the end of their minimum contract period. This ensures that consumers are able to act accordingly when it is most appropriate. It is also supported by our consumer research, with around nine out of ten consumers who reported being in-contract across each of the services saying they thought it would be useful to be contacted by their provider and told their contract is coming to an end (about 1 to 2 months before this happened).<sup>107</sup>
- 3.78 End-of-contract notifications were spontaneously suggested as a way to support informed decision making by participants in our 2017 qualitative consumer engagement research, who felt it had the potential to ‘awaken’ people to think about whether their current deal is the best one for their needs. This was evident among less engaged participants as well as those in a potentially vulnerable situation, where many did not feel confident to do something proactively. Those who were less engaged also felt they would be prompted to engage if notified of a price increase before it was imposed, with some feeling they could be ‘caught’ out by a price increase.
- 3.79 Given that those consumers who are already out-of-contract will not receive a notification advising them that their minimum contract period is ending and providers have not previously provided them with this information, it is equally important that this option addresses the harm we have identified in relation to these customers. A one-off out-of-contract notification would ensure these customers are appropriately informed that they are out-of-contract and of the relevant implications of remaining on their existing deal.
- 3.80 Stated interest in such notifications was strong among those who said they were out-of-contract. Our research found that many of these consumers across each of the services reported that they would find a notification useful.<sup>108</sup> In particular, standalone pay TV customers who were unsure of their contract status were significantly more likely than those who knew they were out-of-contract to find this type of notification useful (78%).

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<sup>107</sup> Ofcom’s quantitative consumer engagement research 2018, conducted by Critical. Slide 23. 87% for mobile, 87% for standalone pay TV, 89% for dual play, 90% for triple play.

<sup>108</sup> Ofcom’s quantitative consumer engagement research 2018, conducted by Critical, slide 24. 56% for standalone pay TV, 56% for dual play, 62% for triple play.

- 3.81 Given our assessment of harm evidenced in the landline, broadband, pay TV and mobile markets, we think it is appropriate for this option to apply more broadly to all providers of PECS. This is consistent with the application of our consumer protection conditions (part C in the revised General Conditions of Entitlement which come into force on 1 October 2018). This would build on the provisions in these conditions.
- 3.82 This means that this option would require notifications to be sent to all residential and Small Business customers who take PECS, which would include landline, broadband, pay TV and mobile services.<sup>109</sup>
- 3.83 Our research showed that a notification was of less interest to mobile consumers. In this market, we expect the interest or desire to upgrade handsets acts as a natural trigger for engagement. However, this was still viewed as a prompt for less engaged consumers to contact their provider about upgrade options, and for consumers on a mobile handset to consider switching to a SIM-only deal.
- 3.84 Around half of respondents to the July 2017 CFI were supportive of Ofcom considering end-of-contract notifications as a potential solution to consumers not engaging with the market. One respondent, [X], thought this could help consumers know when to engage as it removes uncertainty and should boost consumer confidence.<sup>110</sup> This was echoed by others who believed providers are not proactive enough in informing consumers that their promotional period is ending,<sup>111</sup> so that often the first time consumers know about a price increase is when they receive their bill.<sup>112</sup>
- 3.85 Some respondents raised concerns about the potential for end-of-contract notifications to annoy or overload consumers with information (e.g. Sky,<sup>113</sup> Communications Consumer Panel<sup>114</sup>). In addition, Citizens Advice, uSwitch and MoneySavingExpert highlighted that prompts may not have much impact on their own, for example if a consumer is not free to exit the contract or the notification does not also include information about the best tariffs available as seen in other sectors (e.g. energy market). We have taken these views into account in Section 4 in our proposed notifications design.
- 3.86 Our provisional judgement is that the option of providers sending end-of-contract and out-of-contract notifications is likely to effectively address the harms we have identified and thereby achieve our policy objectives. In particular, for both residential consumers and

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<sup>109</sup> In relation to standalone landline, we recognise that, following a review of the market for standalone landline telephone services, BT voluntarily committed to improve the information available to ensure its voice-only customers are aware of possible savings available to them in this market. BT has committed to investigate, using a reasonable number of trials, the form of communication which has the best prospect of success in increasing engagement for these customers. We note the potential overlap between this communication and a one-off out-of-contract notification and will consider this further once we know the outcome of the first trial. BT also voluntarily committed to provide its split purchase customers with an annual statement. We note there may be some overlap between the annual statement and the one-off out-of-contract notification and we consider that BT could amalgamate these communications if it wants.

<sup>110</sup> [X], July 2017 CFI response.

<sup>111</sup> This view was shared by BGL Group Limited, MoneySavingExpert, Moorhouse Consulting, First Utility, SSE, TalkTalk, Inclusion London, Citizens Advice, Communications Consumer Panel, Advertising Standards Authority, uSwitch, Centre for Competition Policy: University of East Anglia and one other provider, [X].

<sup>112</sup> Ofcom, *Call for inputs: Helping consumers to engage in communications markets*, July 2017.

<sup>113</sup> Sky, July 2017 CFI response: [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0023/108437/Sky.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0023/108437/Sky.pdf).

<sup>114</sup> Communications Consumer Panel, July 2017 CFI response: [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0023/108428/Communications-Consumer-Panel-and-ACOD.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0023/108428/Communications-Consumer-Panel-and-ACOD.pdf).

Small Businesses, they would increase awareness of their minimum contract period status, they would inform them of price and service changes, and they would also address their lack of understanding and awareness of the options available after that period ends and the savings that could potentially be made. This timely information would protect them against unexpected and unwelcome changes to their service and price and enable them to make informed decisions about their current deal and whether they need to consider alternatives. We consider that they would also more generally reduce the time and effort required for consumers and Small Businesses to monitor, and search for some of this information at the appropriate time.

## Other options we have considered

3.87 We have also considered some other potential options that could address our concerns and meet our policy objectives but for the reasons set out below we have not pursued them further in this consultation. These are:

- **Strengthening information given at the time services are purchased**, for example, by requiring providers to inform customers about what precisely will happen once the minimum contract period ends and the potential options available beyond this period.
- **Mandating provision of end-of-contract information online or via app**. We could require this information to be presented in a standardised way so that there is a consistent approach to how this information is presented that would be proactively accessed.

### Strengthening information given when the service is purchased

3.88 Our provisional view is that strengthening this information is unlikely to address the specific harms we have identified above and therefore will not achieve our policy objectives in relation to Small Business and residential consumers.

3.89 Our policy objectives are clear that we consider information should be provided at an appropriate time to ensure that consumers can effectively act on receiving this information. We consider this to be at the time the minimum contract period is ending, and, in the case of where this period has already passed, this information should be provided as soon as possible.

3.90 Providers are already required to provide a significant amount of information when a customer purchases a service, with our evidence indicating that some consumers are unable to recall this information. It is therefore unlikely that if more information is provided at this time consumers will recall this information differently. Increasing information requirements at the time a customer purchases a service may also increase the risk of information overload, which would undermine the purpose of increasing awareness of what happens at the end of the minimum contract period.

3.91 To the extent that consumers are focused on getting their new service, they may give limited weight to contract conditions which will usually only come into effect in 12 to 24 months' time when their minimum contract period ends. Moreover, some providers may not be able to provide precise price changes when the service is purchased.

### Mandating provision of end-of-contract information online or via app

- 3.92 Again, our provisional view is that this option is unlikely to address the harm we have previously identified and so achieve our policy objectives in relation to Small Business and residential consumers.
- 3.93 Our policy objectives are framed in terms of this information being provided to consumers at an appropriate time.
- 3.94 Our evidence highlights that customers already have multiple ways to access minimum contract period information, with online accounts being a common way that providers typically make this information available to consumers. However, the inclusion of this information in online accounts and apps would still rely on consumers taking proactive action to seek this information out, and the evidence gathered shows that some consumers do not appear to do this (as highlighted earlier in this section).
- 3.95 We also consider it important to reduce the time and effort of obtaining and monitoring this type of information for those consumers who may be more engaged.
- 3.96 Since both these alternative options require consumers to either recall or proactively seek out this information, we do not think these options would address the harm identified and thereby achieve our policy objectives.

### Our assessment on options for intervention

- 3.97 We are minded to regard maintaining the status quo, strengthening information provided when the service is purchased and mandating provision of end-of-contract information online or via app alone as unlikely to address the harms we have identified and secure our policy objectives.
- 3.98 We propose that requiring providers to send end-of-contract notifications and a one-off out-of-contract notification would be the most appropriate and effective approach for consumers faced with the harms identified above. Given the harms we have identified, we propose that these notifications be sent to all residential and Small Business customers who take PECS.
- 3.99 We have also considered ways to make such a solution less onerous for providers, as detailed in Section 4, where we set out our proposed notification design to be implemented by way of formal regulation.
- 3.100 In Section 5, we evaluate the benefits and costs of this approach before reaching a provisional conclusion on whether we consider that requiring providers to send end-of-contract notifications and a one-off out-of-contract notification to consumers is proportionate.

**Question 1:** Do you agree with our assessment of harm relating to residential consumers and Small Businesses?

**Question 2:** Do you agree that providers should send both end-of-contract and out-of-contract notifications?

**Question 3:** Do you agree with our proposal that notifications should be sent to all residential and Small Business customers who take Public Electronic Communications Services?

Please provide evidence in support of your views.

## 4. Making end-of-contract and out-of-contract notifications simple for consumers and practical to implement

### Introduction

- 4.1 As set out in Section 3, our provisional view is that the option of introducing end-of-contract notifications and out-of-contract notifications for both residential consumers and Small Businesses is most likely to achieve our policy objectives. Both notifications would be sent to all residential and Small Business customers who take PECS, that is landline, broadband, pay TV and mobile services, whether taken alone or in dual play, triple play, or quad play bundles. This section sets out our proposed design of such notifications to be implemented by way of formal regulation.
- 4.2 To ensure that these notifications are effective and easy for consumers and Small Businesses to understand, we set out proposals on the content and structure of the communications. To ensure that they are practical to implement and go no further than is necessary, we propose giving providers some flexibility over when they should be sent and the detailed drafting.

### Approach to remedy design

- 4.3 Taking into account our policy objectives in Section 2 and our assessment of harm in Section 3, we have sought to design notifications which are appropriate to the consumer harm identified in order to achieve our policy objectives. At the same time, we have been mindful of the need to ensure that providers have a degree of flexibility to communicate with their own customers.
- 4.4 We have identified the following key criteria against which we assess our proposals to ensure they are appropriate:
- They should be effective in addressing consumers' lack of awareness or lack of sufficient information about the end of their minimum contract period and the implications of this. This would help them to avoid unexpected and unwelcome changes to their service or price, make informed decisions about their existing deal and whether they should be shopping around for a new one, and/or avoid incurring time and effort in monitoring and seeking out this information.
  - The notification should be in a form that is understandable for consumers.
  - The notification should be timely so that when consumers receive the information they can act upon it appropriately.
  - They should as far as possible mitigate any unintended consequences for both consumers and providers.
- 4.5 Our consideration of remedy design is the same for residential consumers and Small Businesses. The evidence we rely on is largely based on consumer research, but as set out

in Section 3 we consider that Small Businesses are likely to behave in a similar way and raise similar concerns to residential consumers.

## Sources of evidence

4.6 We have considered a number of sources to help inform the proposals for notifications as set out in this section, including responses to our July 2017 Call for Inputs and consumer research, as described below. We have also reflected the views of providers in formulating our proposals, obtained during our discussion with them in the course of this review.

### Responses to our July 2017 Call for Inputs (CFI)

4.7 A number of respondents to our July 2017 CFI had specific views on the content, format and timing of end-of-contract notifications. These are set out in more detail in the relevant paragraphs below.

### Consumer Research

4.8 We carried out qualitative research (“2018 end-of-contract notification qualitative research”) to test consumer comprehension of potential notification messages and to identify any issues with the volume of information and/or any misleading or worrying information/messaging that may have a negative impact on consumers’ behaviour.

4.9 Our further aim from the research was to understand:

- which, if any, pieces of information were most relevant in terms of supporting next steps. Our starting point was that the notification should include three key pieces of information: a) the minimum contract period end date; b) that after that date the consumer is free to switch deal/provider without incurring an early termination charge; and c) any monthly price or service change if the consumer takes no action;
- which combinations of information participants said would be the most effective in ensuring the notification supported respondents’ decisions on whether to engage and importantly, whether any particular pieces, or combinations of, information would detract from recalling and understanding the key messages – e.g. whether offers from a customer’s current provider would overshadow messaging around their ability to find a better deal or switch; and
- whether views differ according to the method of communication (e.g. SMS, letter or email).

4.10 Taking all our evidence into account, we have set out proposed requirements for notifications which in our view achieve our policy objectives by seeking to address the concerns detailed in Section 3, while seeking to avoid any unintended consequences.

## Proposed content of end-of-contract notifications

4.11 We propose that an end-of-contract notification should include the following information:

- The date on which the customer’s minimum contract period ends, including that early termination charges no longer apply at that point.<sup>115</sup> It should also include details of any applicable notice periods;
- The services which the provider currently provides to the customer under that contract, including additional benefits that accompany the contract, such as free subscriptions to other services (e.g. Netflix, Spotify); the monthly subscription price currently paid by the customer for those services (including any historical discounts); and any changes to the services provided and/or monthly subscription price paid by the customer upon the minimum contract period ending. This should include a list of other services taken with the same provider pursuant to other contracts; and
- The options available to the customer after the minimum contract period has ended, including a message that the customer may be able to make savings by exploring the available options. The notification to customers of mobile services must include SIM-only as one of the options.

**Proposed content:**

**(i) The date on which the customer’s minimum contract period ends, including that early termination charges no longer apply at that point. It should also include details of any applicable notice periods.**

- 4.12 Participants in our 2018 end-of-contract notification qualitative research were generally supportive of a notification. They thought that such notifications would be useful and would save them from having to proactively find information about their minimum contract period end date. They considered this end date to be an **essential** piece of information in a notification. The participants considered it to be a core message which should be clear and prominent, such that it sets the context for the rest of the notification.<sup>116</sup>
- 4.13 Participants were generally in favour of the notification informing them that they would not have to pay **early termination charges** after the end of their minimum contract period if they wanted to end their subscription. Overall, they thought that the inclusion of this information helped to clarify the conditions they would be subject to.<sup>117</sup>
- 4.14 In general, participants understood relatively little about **notice periods**, including that consumers may be required to give notice to their provider beyond the end of their minimum contract period.<sup>118</sup> They considered this to be essential information, as well as the length of the notice period so as to time their decisions accordingly.<sup>119</sup>
- 4.15 First Utility commented in its July 2017 CFI response that consumers should be notified ahead of their minimum contract period end date and that the expiry date of any

<sup>115</sup> The minimum contract period is referred to in the General Conditions of Entitlement as the fixed commitment period.

<sup>116</sup> Ofcom’s end of contract notification qualitative research 2018, conducted by Jigsaw. Slides 15, 49.

<sup>117</sup> Ofcom’s end of contract notification qualitative research 2018, conducted by Jigsaw. Slide 28.

<sup>118</sup> Ofcom’s end of contract notification quantitative research, 2015, conducted by Jigsaw. Slide 37: at least 25% of consumers in each of the dual play, triple play, pay TV and mobile markets were not aware that they were required to give notice outside of their minimum contract period.

<sup>119</sup> Ofcom’s end of contract notification qualitative research 2018, conducted by Jigsaw. Slides 15 and 24.



promotional discount, in particular, should be made clear. MoneySavingExpert also commented that consumers should be made aware of when it is a good time for them to engage in the market through prompts.

## Our assessment

- 4.16 For our proposed remedy to be effective in addressing the harms that we have identified, we consider that consumers should be informed, at the appropriate time, of the **date their minimum contract period ends**.<sup>120</sup> In Section 3, we set out that a material number of customers do not know if their minimum contract period has come to an end or when it is due to come to an end, or incur costs to monitor and seek out this information. Our research shows that up to 26% of people taking landline, broadband and pay TV services (standalone or as a bundle) lack awareness or are confused about their contract status. The same is true of 15% of mobile phone customers.
- 4.17 Our proposal addresses this by ensuring that this information is provided to them in a clear and understandable way, meaning they do not have to proactively seek it out.
- 4.18 To assist consumers in understanding the implications of reaching the end of their minimum contract period, we consider it important for the notification to make clear that **early termination charges** will not apply after the end of the minimum contract period if the consumer decides to move to a new deal or switch provider.
- 4.19 This information would address the concerns identified in our research (see paragraph 3.18) that consumers may be put off moving to new deal if they believe they may be subject to early termination charges. It also helps to avoid unintended consequences that may arise where notifications are sent in advance of the end of the minimum contract period (see below), such that consumers are aware that early termination charges will be payable up to the date the minimum contract period ends.
- 4.20 We consider that providing guidance on the length of **notice periods** in the end-of-contract notification will ensure that consumers understand that even when they are outside their minimum contract period, they will still need to give notice to their provider if they decide to change deals and can therefore plan on the basis of this. It also helps to avoid unintended consequences, such as switching provider before the end of the notice period and potentially having to pay for both old and new services at the same time.

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<sup>120</sup> In our assessment sections and analysis below (not where we report research results), references to ‘consumers’ covers both residential and Small Business customers.

**Proposed content:**

**(ii) The services which the provider currently provides to the customer under that contract, including additional benefits that accompany the contract, such as free subscriptions to other services (e.g. Netflix, Spotify); the monthly subscription price currently paid by the customer for those services (including any historical discounts); and any changes to the services provided and/or monthly subscription price paid by the customer upon the minimum contract period ending. This should include a list of other services taken with the same provider pursuant to other contracts.**

- 4.21 Participants in our 2018 end-of-contract notification qualitative research identified **monthly price changes** at the end of the minimum contract period as essential information in a notification, which could help them determine whether they wanted or needed to take any action. Most thought that if the amount they were paying was going to change after the end of the minimum contract period then it should be incumbent on the provider to let the customer know this.<sup>121</sup> This was a view echoed by respondents to our July 2017 CFI who suggested various pieces of information that should be provided in a notification including current, as well as future, pricing and service information.<sup>122</sup>
- 4.22 In general, participants preferred price information to be presented as a monthly rather than an annual figure as this would be more helpful to them in terms of budgeting. They were also keen to understand the scale of any price increase (i.e. from £X to £Y), and thought it was reassuring and straightforward to include both the current and future amounts (even for those who already knew what they were paying each month). They also considered it important for the notification to include the current monthly subscription price even where the price does not change, for clarity around what they will pay going forward.<sup>123</sup>
- 4.23 Our research also tested reactions to the inclusion of information about **price discounts** that applied earlier in the contract. This was considered most useful where no price increase occurred at the end of the minimum term and acted as a reminder that they may be offered a discount if they were to sign up to a new deal. Generally, a lot of price information was considered too complex for a single notification and so a simple reminder that a discount had been applied previously (if relevant) was considered sufficient.<sup>124</sup>
- 4.24 Participants also thought that including a **breakdown of current service/contract** and any changes was essential to the end-of-contract notification. In particular, it would act as a reminder of the services they currently take and would allow them to review what they are paying for and consider whether they still require those services.<sup>125</sup>

<sup>121</sup> Ofcom's end of contract notification qualitative research 2018, conducted by Jigsaw. Slides 15, 26, 52.

<sup>122</sup> Suggestions of this nature were made by respondents including Citizens Advice, BGL Group, SSE, First Utility and MoneySavingExpert. Ofcom, *Helping consumers to engage in communications markets: Call for Inputs*, July 2017.

<sup>123</sup> Ofcom's end of contract notification qualitative research 2018, conducted by Jigsaw. Slides 26 and 29.

<sup>124</sup> Ofcom's end of contract notification qualitative research 2018, conducted by Jigsaw. Slide 15, 26, 53. Earlier discounted pricing was unfamiliar to some participants and the seeming irrelevance may have impacted their attitudes.

<sup>125</sup> Ofcom's end of contract notification qualitative research 2018, conducted by Jigsaw. Slides 15, 27, 55.

4.25 Participants preferred this information to be presented to them in a clear and easy to absorb format, and particularly liked the idea of being able to easily and visually compare current and future services and price in a simple table format. They considered the presentation of information in this way would be transparent. Below is an example of a breakdown of services and price (where price changes exist) used in the research which was well-received by participants.

**Figure 11: Example of breakdown table for a dual play contract**

Current deal	After [day] [month] 2018
Broadband and Talk	Broadband and Talk
Line Rental - £X	Line Rental - £Y
Caller display - FREE	Caller display - £Y
Broadband unlimited - £X	Broadband unlimited - £Y
WiFi Hotspots - FREE	WiFi Hotspots - £Y
Pay as you talk - FREE	Pay as you talk - £Y
Monthly price - £X	Monthly price - £Y

4.26 The participants additionally thought that being told about the implications for any other contracts taken with the same provider was essential if applicable to them, i.e. if other services taken from the same provider did not end on the same date.

4.27 A number of respondents to our July 2017 CFI agreed that pricing information – either highlighting the differences between the current and out-of-contract tariffs or informing customers that a discount or promotional offer is ending – would be important in an end-of-contract notification.<sup>126</sup>

## Our assessment

4.28 We consider that reminding consumers of details of their **current package and monthly price paid** is important in helping them understand which services the minimum contract period relates to and assists them in: making an informed decision about whether to remain on their existing deal and assessing their options once the minimum contract period ends. Service details should include additional benefits that accompany the contract, such as free subscriptions to other services (e.g. Netflix, Spotify) as this is relevant information for consumers to be aware of in making an informed decision.

4.29 We propose that the information about the package/service details and monthly price to be provided should be those that are applicable at the time of the notification. This would

<sup>126</sup> Citizens Advice, First Utility, SSE and BGL Group. Ofcom, *Helping consumers to engage in communications markets: Call for Inputs*, July 2017.

ensure that customers are given the most relevant and recent pricing and service information. It would also avoid the risk of confusion with different prices paid during the minimum term of the contract, particularly where consumers could add or remove additional services from month to month. However, we consider it important to inform consumers whether any discounts had been applied to the prices they paid during their minimum contract period, without providing the actual price paid or the value of the discount, as this fact is relevant to a consumer's understanding of the overall price of the contract over the minimum contract period.

- 4.30 Being informed of **any change in cost and service(s)** that will occur once the minimum contract period comes to an end is essential for consumers to be able to avoid any unexpected and unwelcome changes, and, furthermore, allow them to make an informed decision about whether to remain on their existing deal and make an assessment of their options. This is particularly significant given that we have identified this as a significant source of harm (see Section 3).
- 4.31 Listing the **other services taken with the same provider pursuant to other contracts** is important so that consumers are given complete information in terms of the services they currently take with that provider. This aims to help consumers avoid unintended consequences and make an informed decision about next steps as there could be implications for them if they were to change deal or switch provider.

**Proposed content:**

**(iii) The options available to the customer after the minimum contract period has ended, including a message that the customer may be able to make savings by exploring the available options. The notification to customers of mobile services should inform them of the availability of SIM-only deals as one of the options.**

- 4.32 Some participants in our 2018 end-of-contract notification qualitative research considered that giving consumers additional information regarding their options (such as the fact they could shop around for a new deal or switch to a new provider) alongside the contract end date gives a more complete picture of their options. Indeed, among the less engaged participants being provided with all the relevant information in a single communication was considered essential.
- 4.33 Some participants who had a mobile contract that included a handset were unaware of SIM-only options. Of these, some continued to pay the higher price for their mobile service even when their minimum term had ended. These participants expressed concern at not being notified about SIM-only options and considered it important for this information to be included in an end-of-contract notification, in order for consumers to avoid 'paying over the odds' for their mobile.<sup>127</sup>
- 4.34 This was also supported in responses to our July 2017 CFI, with MoneySavingExpert stating that consumers often do not engage due to not knowing how much they could save, and therefore a prompt informing consumers that they could make savings would be useful.

<sup>127</sup> Ofcom's end of contract notification qualitative research 2018, conducted by Jigsaw. Slides 15, 35, 60.

Participants in our 2018 end-of-contract notification qualitative research also noted that a message informing them that they could ‘save money’ was a good reminder that they could be paying less.<sup>128</sup>

- 4.35 The Communications Consumer Panel’s response to our July 2017 CFI reflected our consumer research findings and highlighted that it would be useful for providers to give their customers clear advice on what new deals are available.

## Our assessment

- 4.36 In order to ensure the effectiveness of the end-of contract notifications, our view is that consumers’ interests will be best served if the recipients understand the implications of coming to the end of their minimum contract period, including the options that are available to them. Communications markets are complex and without that information, consumers may be confused as to what, if anything, they can do next. In order to make these options tangible, we consider that consumers should be informed that these options could enable them to find an improved deal and/or that there is the possibility of making savings.
- 4.37 This is aimed at ensuring that consumers are fully aware of what it means to come to the end of their minimum contract period, such that they are able to make an informed decision about their existing deal. By not being informed of what their options are and the possibility of savings, there is a risk that consumers will make an assumption that their existing deal is the best available, without exploring other available options. This, in turn, would undermine the effectiveness of end-of-contract notifications in addressing the higher prices paid by some out-of-contract consumers.
- 4.38 In Section 3, we have explained that consumers often do not understand or lack awareness of the options available to them once their minimum contract period ends and the savings they could make. Therefore, we consider it appropriate for this information to be provided in the end-of-contract notification to ensure the effectiveness of the communication and enable consumers to make an informed decision about whether to stay on their current deal or seek an alternative deal.
- 4.39 We propose that the notification to customers of **mobile** services should also include that the customer can use their existing handset and take a SIM-only deal as one of the options available to them at the end of the minimum contract period. In particular, these deals are likely to enable a number of out-of-contract mobile consumers to move to a better deal and save money. Alerting customers to the existence of SIM-only deals would address the lack of awareness of some mobile customers of SIM-only deals.<sup>129</sup>
- 4.40 We do not propose to prohibit providers from including offers in the end-of-contract notification. The inclusion of provider offers would not be out of place alongside the other options available and we consider that it is appropriate that consumers consider a provider

<sup>128</sup> Ofcom’s end of contract notification qualitative research 2018, conducted by Jigsaw. Slides 15, 43, 56.

<sup>129</sup> Our 2018 quantitative consumer engagement research found that a quarter of customers on a mobile handset contract were unaware of the possibility of moving to a SIM-only deal at the end of their minimum contract period. Ofcom’s quantitative consumer engagement research 2018, conducted by Critical. Slide 29.

offer when assessing whether to remain on their existing deal or switching to another provider.

## Content we are not proposing to be in an end-of-contract notification

4.41 Our 2018 end-of-contract notification qualitative research also tested additional content to be included in the notifications. We have decided not to include this additional content in our proposed notifications for the reasons set out below:

- **Total price paid over the term of the contract.** Our research sought participant views on how useful it would be for the notification to include a figure for the total price paid for the services taken by the customer over the minimum term of the contract. Most participants did not consider this information to be essential to them. Our findings suggest that the total price paid over the term of the contract is not something that consumers calculate or would use to make decisions about their contract. Given we are proposing the current monthly subscription price is included in the notification, an additional price point could risk information overload, which could undermine the effectiveness of the notification. Our view is that it is not appropriate to include the total price paid over the term of the contract in our proposed content for the notification.
- **Detailed information about other contracts taken with the same provider.** Our research also sought views on different messages regarding other contracts that consumers may have with the same provider. When these messages were tested in our research, they were only relevant to a few participants. Where the information was relevant, participants deemed this information essential, and the preferred message was to be told the end date of the minimum contract period for their other services. We are proposing that the notification should include a list of other services taken with the same provider, however, in our assessment, we do not consider that it would be proportionate to require providers to give more detailed information. The list of services should be sufficient for consumers to seek out further information if required.
- **A link to the mobile provider's webpage on handset unlocking, where relevant.** Participants in our research felt that information about how to unlock their handset was largely irrelevant in an end-of-contract notification. While participants thought the information was important, they did not consider that it was required at the point the notification is sent. We therefore do not propose to require providers to include information about handset unlocking in the notification. In particular, we consider that this information is likely to be more relevant at the point that a customer decides to switch provider.
- **A link to information about mobile coverage, where relevant.** Participants in our research also felt that a reference to find more information about mobile coverage was irrelevant in such a notification. We do not propose to include this information in the end-of-contract notification. As with handset unlocking, we consider that information about mobile coverage is likely to be more relevant when customers decide to shop around for mobile services.

- **A link to switching information on Ofcom’s website.** Participants in our research considered the inclusion of a link to advice on how to switch on Ofcom’s website to be desirable rather than essential. The more confident and engaged did not feel that they needed advice on how to switch, while others considered this to be a good or responsible thing to be included in the communication. In our assessment, we do not consider this information essential and it is likely to be more relevant at the point that a customer decides to switch provider. We also note that information/advice about switching can be found elsewhere, such as on providers’ and consumer groups’ websites.

## Structure of the end-of-contract notification

- 4.42 One of the objectives of our 2018 end-of-contract notification qualitative research was to explore the optimal content and flow for an end-of-contract notification in terms of delivering the core messages in the most effective way.
- 4.43 Our research tested example notifications of various lengths with participants.<sup>130</sup> In general, the longer versions were thought to be more informative, provided important information that supported decision making and appeared more honest and helpful. The longer versions were, in particular, preferred by the less engaged and less confident consumers. Although the more confident/engaged tended to prefer shorter notifications, they did not reject the longer version.
- 4.44 As mentioned above, our starting point was that the end-of-contract notification should include three key pieces of information:
- the actual end date of the minimum contract period;
  - the fact that after that date the consumer is free to end their subscription without incurring an early termination charge; and
  - the monthly price (change) if the consumer takes no action.
- 4.45 Evidence from our research suggests that participants considered it essential that the end-of-contract notification should lead with the date their minimum contract period ends, as this sets the context for the rest of the communication. Participants also thought that it was ‘crucial’ to be told about any price change, as this would inform a decision on whether to engage.<sup>131</sup> Other aspects considered crucial or essential by participants were: the ability to cancel or switch without charge (as this highlighted their options), notice periods (given the general lack of understanding), and end dates for other contracts with the same provider (if applicable).
- 4.46 Participants largely accepted the inclusion of provider offers in the notification and felt it was quite useful and would save them time and effort to look for a new deal. However, they highlighted that an end-of-contract notification that led with an ‘offer’ may be

<sup>130</sup> Ofcom’s end of contract notification qualitative research 2018, conducted by Jigsaw. Slide 16.

<sup>131</sup> Ofcom’s end of contract notification qualitative research 2018, conducted by Jigsaw. Slides 15, 19, 42, 52-53.

discarded/overlooked because it would be perceived as marketing information.<sup>132</sup>

Participants regarded a provider's offer as 'desirable' but considered it better placed after the 'essential' pieces of information.<sup>133</sup>

## Proposals for structure

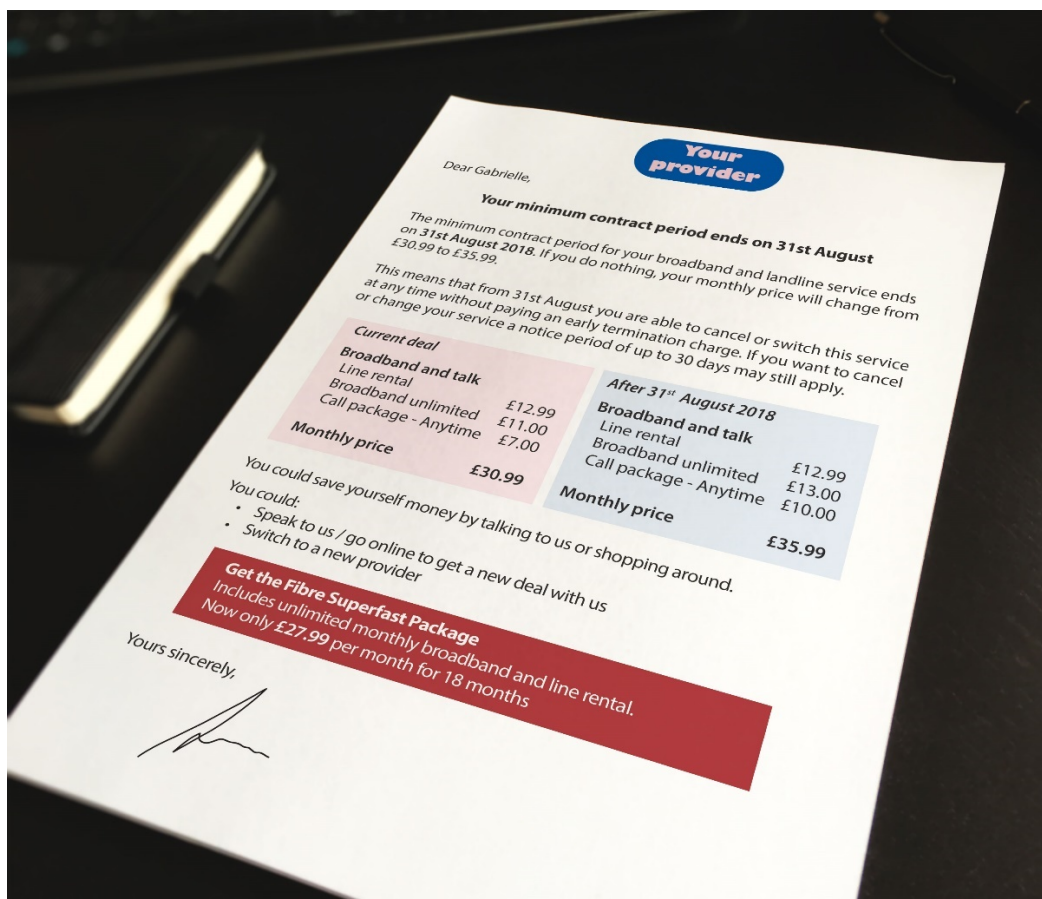
- 4.47 In order to ensure that the end-of-contract notification is effective and not mistaken for general marketing information, we propose that the end date of the minimum contract period and any resulting price changes should appear upfront in the notification. We consider that placing this information upfront is important to make consumers aware of the purpose of the communication and highlight information essential to their decision-making.
- 4.48 As set out above, we do not propose prohibiting providers from including offers in their end-of-contract notification. However, where an offer is included, we consider it important that this information appears **at the end of the notification**, as one of the options available to the customer at the end of the minimum contract period. This is to ensure that providers do not include an upfront marketing message that could mean the entire communication is mistaken as marketing and disregarded as a result.
- 4.49 We do not propose specifying the structure of the remaining content. As set out above, we recognise that some providers adopt a particular style when communicating with their customers and we would not want our proposals to limit their ability to communicate with their customers in the most effective way.
- 4.50 The following is an illustration of how the proposed information could be set out in an end-of-contract notification letter:

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<sup>132</sup> Similarly, in our 2017 qualitative consumer engagement research, some participants felt that it was important for the notification to stand out and apart from sales and marketing they receive, so that it would not be discarded by accident. Ofcom qualitative consumer engagement research, 2017, conducted by Futuresight (p.51).

<sup>133</sup> Ofcom's end of contract notification qualitative research 2018, conducted by Jigsaw. Slides 15, 25, 44.





## Method of sending the end-of-contract notification

- 4.51 Our evidence suggests that different customers have different contact preferences. For example, participants in our 2017 qualitative consumer engagement research wanted to choose which method to receive the notification. Text was the most common method called for across all services, and after that, a choice of email or post (i.e. letter) was requested.<sup>134</sup>
- 4.52 In contrast, participants in our 2018 end-of-contract notification qualitative research preferred longer communications with more information, suggesting a letter or email would be more effective. They considered that a letter or email could contain more messages and information relevant to their decision making, where such information would not be conducive to a text. However, some noted that people always read a text message which suggests this could potentially be an effective channel for key facts.
- 4.53 Most respondents to our July 2017 CFI did not state whether an end-of-contract notification should be sent in a specific format, but MoneySavingExpert said that it should be a distinct communication and separate from any bills. This echoes the views of the majority of participants in our 2015 end-of-contract notification research who preferred

<sup>134</sup> Ofcom's qualitative consumer engagement research 2017, conducted by Futuresight (p.51).

the idea of a standalone communication from the provider to receiving the information with a bill.<sup>135</sup>

## Proposals for method of sending the end-of-contract notification

- 4.54 We are aware that most providers collect information from their customers about their preferred channels of communication and are able to tailor their communication methods accordingly. Using customers' preferred method of contact is likely to be the most appropriate way of ensuring that the end-of-contract notification reaches consumers.
- 4.55 Therefore, we propose that providers should send the end-of-contract notification in a durable medium using the individual customers' preferred method of contact. By durable medium we mean paper, email or SMS, or any other medium that:
- allows information to be addressed personally to the recipient;
  - enables the recipient to store the information so that it is accessible for future reference for a period that is long enough for the purposes of the information; and
  - allows the unchanged reproduction of the information to be stored.<sup>136</sup>
- 4.56 We recognise that in some cases, the provider may not know the customer's preferred contact channel. In such cases, we propose that the end-of-contract notification should be sent in a durable medium using the same contact channel for providing or notifying the customer of available bills.
- 4.57 We also propose that the end-of-contract notification should be a standalone communication which is sent separately from their bill or other service message from their provider. This is to ensure that the consumer does not mistake, overlook or dismiss the end-of-contract notification with other messages from their provider.

## End-of-contract notifications sent by SMS

- 4.58 We note that some providers communicate with their customers mainly via SMS either because that is their standard method of communication and/or because they are aware that their customers prefer this particular contact channel.
- 4.59 In our 2018 qualitative research, we tested end-of-contract notifications using SMS with mobile customers. For the group discussions, participants were sent example notifications via text message to their mobile phones. While this format was acceptable to all, it was presented as the only option, and there was agreement that text was better suited to shorter communication (i.e. the 'basic version' that was tested). But some noted that the 'basic version' lacked information that was considered 'essential' e.g. price change information or notice periods. As such, participants suggested multiple texts may be a solution.<sup>137</sup>

<sup>135</sup> Ofcom 2015 end of contract notification research. Slide 28. However, over 55s were happier to receive the notification by standalone letter or along with their paper bill (under 35s preferred online methods, i.e. email).

<sup>136</sup> We do not consider that a push notification from a provider's app would meet the definition of durable medium.

<sup>137</sup> Ofcom's end of contract notification qualitative research 2018, conducted by Jigsaw. Slides 31-36.

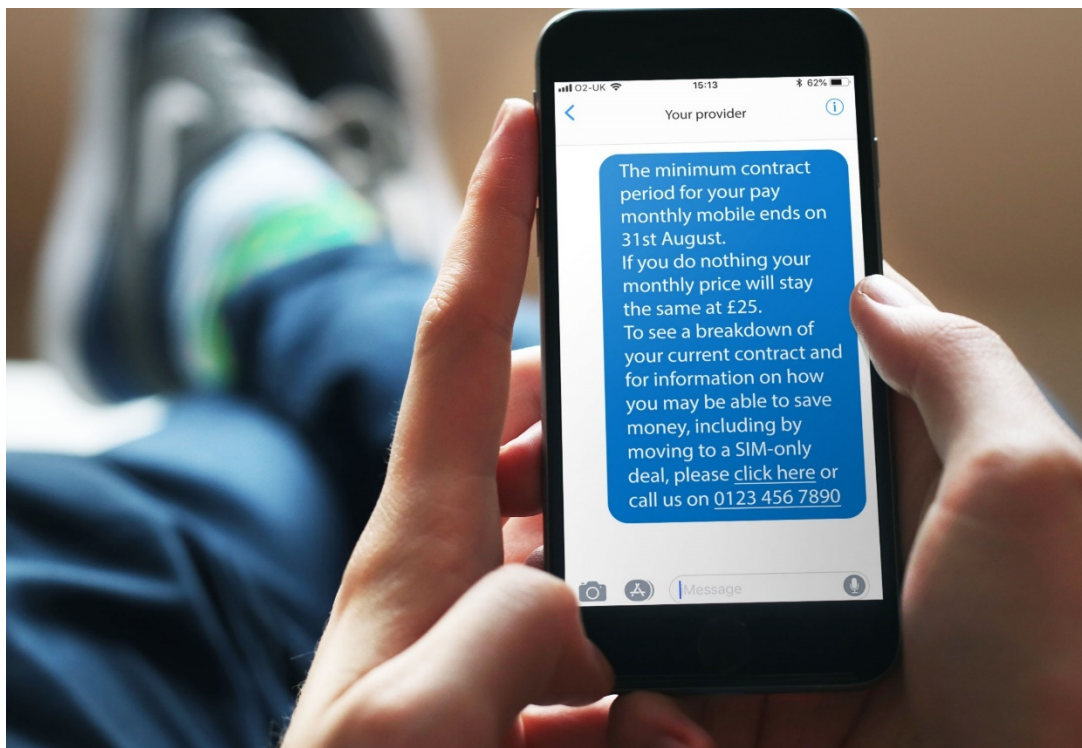
4.60 Given the need to keep SMS (text messages) relatively simple and concise in the interest of effective messaging, we consider that there is certain core information which the provider must include in the main body of an end-of-contract notification sent via SMS. However, the provider would also be required to provide the other details in either another durable medium (SMS, letter or email), or via a link in the SMS which should take the consumer to their online account. Providers need to be clear in the SMS where the other information will be available.

4.61 We therefore propose the following for end-of-contract notifications sent by SMS:

<b>Core information which must be included in the main body of the SMS</b>	<b>Information that can be included in either another durable medium or via a link in the SMS to the customer's online account</b>
The date on which the customer's minimum contract period ends.	The fact that early termination charges no longer apply after the end of the minimum contract period, but noting any applicable notice periods if the customer wants to cancel or switch.
The monthly subscription price currently paid by the customer and any changes to this upon the minimum contract period ending.	The services which the provider currently provides to the customer under that contract, including additional benefits that accompany the contract, such as free subscriptions to other services (e.g. Netflix, Spotify) and, if applicable, any changes to the services provided upon the minimum contract period ending. This should include a list of other services taken with the same providers pursuant to other contracts.
That SIM-only is an available option (mobile only)	If applicable, a reminder that a discount did apply during the minimum contract period.
How the information in the next column will be provided (e.g. the online link or other durable medium).	If applicable, a list of other services taken with the same provider pursuant to other contracts.
	Options available after the minimum contract period has ended, including a message that the customer may be

	able to make savings by exploring the available options.
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- 4.62 The following is an illustration of a possible end-of-contract notification for a mobile contract sent via SMS:



- 4.63 We note from our research that the core messages in the end-of-contract notification better supported decision making if they are embedded in a wider communication which is especially important for the less engaged/confident consumer. Therefore, one of the key disadvantages of sending an end-of-contract notification by SMS is that it could be less effective at supporting those who are less engaged/confident.
- 4.64 However, our proposal will ensure that even with SMS notifications, all the proposed content will be either be in the main body of the message, a link which will be included in the actual message or another durable medium. This ensures that customers would have access to all the information we deem important and relevant to them even if it is not provided in the SMS message itself.

### End-of-contract notifications in accessible formats

- 4.65 Vulnerable consumers and/or consumers with disabilities should get comparable access to end-of-contract notifications. This view is supported by responses to our July 2017 CFI from

the Communications Consumer Panel and Inclusion London who said that it is important to have accessible formats available for vulnerable consumers.<sup>138</sup>

- 4.66 We are, therefore, proposing to require providers to send end-of-contract notifications in a format such as electronic, braille or large print, where customers have registered to receive bills in an alternative format and/or the provider is aware that the customer requires communications to be sent in an alternative format.
- 4.67 This requirement on providers to send such notifications in accessible formats to those who they have identified as requiring communications in such formats, will ensure that customers receive these notifications in a form that is most suitable for them.

## Timing and frequency of the end-of-contract notification

- 4.68 In order to be effective, an end-of-contract notification would need to give consumers enough time to consider their options once their minimum contract period has ended and enough notice in case they choose to change their service. Therefore, we consider that an end-of-contract notification would likely need to be sent at least 1-2 months before the minimum contract period end date, taking into account that providers tend to have around 30-day notice periods (although this can vary, including by service).<sup>139</sup>
- 4.69 This was reflected in our 2017 qualitative consumer engagement research, with many participants saying they wanted to receive an end-of-contract notification **at least a month before the end of their minimum contract period**. Some (potentially those more informed about notice periods) wanted to receive the notification **two months prior**, to ensure that they had time to review their arrangements before the need to provide notice (often around 30 days), in the event that they chose to leave. There was also a universal preference for the notification to be sent towards the end of their minimum contract period, rather than at the end. Some consumers wanted two notifications – one in advance and a second closer to the end as a reminder, to reduce the chances of the original notification being missed.<sup>140</sup>
- 4.70 This was echoed by participants in our 2018 qualitative research, who ideally wanted to receive an end-of-contract notification a month or so before the end of the minimum contract period as this was close enough that it seems relevant, but far enough in advance to allow time to have a think and/or look around.<sup>141</sup>

<sup>138</sup> Communications Consumer Panel, July 2017 CFI response: [https://www.ofcom.org.uk/data/assets/pdf\\_file/0023/108428/Communications-Consumer-Panel-and-ACOD.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0023/108428/Communications-Consumer-Panel-and-ACOD.pdf), p.3; Inclusion London, July 2017 CFI response: [https://www.ofcom.org.uk/data/assets/pdf\\_file/0017/108431/Inclusion-London.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0017/108431/Inclusion-London.pdf), p.2.

<sup>139</sup> The length of any existing notification period may vary by provider, service and/or whether the customer is switching. E.g. for services switched within the Openreach network, the notice period tends to be aligned with the transfer period, i.e. minimum of 10 working days.

<sup>140</sup> Ofcom qualitative consumer engagement qualitative research, 2017, conducted by Futuresight. Page 51.

<sup>141</sup> Ofcom's end of contract notification qualitative research 2018, conducted by Jigsaw, Slides 10, 24. Note: there was a general lack of awareness in the sample with regards to notice periods, which may have impacted stated desired timing for an end of contract notification.

- 4.71 The July 2017 CFI responses that supported end-of-contract notifications were in favour of consumers receiving such notifications before the end date of their minimum contract period, where timing was mentioned.<sup>142</sup> The main reason cited for this is to give consumers enough time to consider engagement and look at available offers before any changes or price rises due to the expiry of the minimum contract period occur. First Utility's response was the most specific, stating that around 30 days before the end of the minimum contract period would be the most appropriate point.
- 4.72 As set out in Section 3, while most providers do not currently send end-of-contract notifications as we think of them,<sup>143</sup> many send promotional notifications to customers towards the end of their minimum contract period to say that their “discount period” is coming to an end and the customer’s contract price will soon increase, and/or that they can re-contract/upgrade without paying an early termination charge.
- 4.73 Where notifications are currently sent to consumers, these usually go out multiple times before and after the end of the minimum contract period. Responses to our January 2018 information request suggest that most providers that send some form of notification do so at least two times before the end of the minimum contract period.

### Proposal on timing and frequency of the end-of-contract notification

- 4.74 We propose to require providers to send **one** end-of-contract notification to customers approaching the end of their minimum contract period. We do not propose to require the sending of multiple end-of-contract notifications, e.g. one before the end of the minimum contract period and then again at the end of the minimum contract period.
- 4.75 We consider that notifying consumers of this information once addresses our key concerns set out in Section 3, that most providers are not informing consumers at the appropriate time of important information about the services they buy. This does not preclude providers from sending additional notifications if they so choose, e.g. at the end of the minimum contract period.
- 4.76 We propose that end-of-contract notifications should be sent to customers **between 40 to 70 days before the end of the minimum contract period**. This reflects our evidence that customers want to be notified nearer to the time they are required to take action but sufficiently in advance so that they have time to take action, particularly if they want to avoid any automatic price increases or service changes. We have also taken into account that in general, customers may have to give their provider up to 30 days’ notice before they can cancel their subscription. Therefore, our proposal should mean that notifications are sent in advance of any applicable notice period.
- 4.77 This also gives providers some flexibility regarding when to send the end-of-contract notification and should enable providers to stagger their customers’ communications accordingly, for example, so that the end-of-contract notification is not sent out at the

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<sup>142</sup> Including First Utility, SSE, MoneySavingExpert and BGL Group.

<sup>143</sup> I.e. A written or verbal notification which is made to a customer to inform them when they are approaching, are at, or have passed the end of their minimum contractual period.

same time as another campaign. This should help to avoid any consumer confusion on what each communication is telling them.

## Proposal on length of contracts to be covered

- 4.78 We propose that our rules should require providers to send end-of-contract notifications for any contracts that have a minimum contract period of **six months or more**. We do not consider that customers who take out monthly rolling (30-day) contracts should be included given the short minimum term for these contracts.
- 4.79 We note that typically the current deals in the market have minimum contract periods of 12, 18 or 24 months for consumer contracts. It is customers who are on these contracts that we think would most benefit from end-of-contract notifications. We are aware that some providers currently offer contracts with a shorter minimum contract period, such as 9 months, which we think is still sufficiently long to warrant an end of contract notification. In our proposals, we have sought to target contracts that have a significant period of time between the point the customer purchases services and the end of the minimum contract period.

## Assessment of design proposals for an end-of-contract notification

- 4.80 We have assessed whether our design proposal for an end-of-contract notification satisfies the criteria set out at the beginning of this chapter.

### The notification should be effective in addressing the harm we have identified

- 4.81 We consider that our proposed content would address the harm identified in Section 3 and thereby achieve our policy objectives. The notification would provide consumers with key information about their minimum contract end date, help consumers avoid unexpected and unwelcome changes to their service or price, help consumers to make informed decisions about their existing deal and whether they should be shopping around for a new one, and/or ensure they do not incur time and effort in monitoring and seeking out this information.
- 4.82 For this reason, we propose that the content of the notification should include the end date of the minimum contract period. To help them understand what this means, we propose that the notification should inform them that early termination charges are not payable after that date.
- 4.83 We consider that including information about current services and price, and any changes would make it clear to the customer which service(s) the notification is for and what will happen to service/price at the end of the minimum contract period. This would help them to make an informed decision about whether to take any action and avoid these changes if they want to.
- 4.84 The proposal to include the options available to the customer, including the possibility of making savings, will ensure they understand what, if anything, they can do next to find an

improved deal. To ensure that the notification is effective, we have proposed that certain core information is placed upfront so that the context of the communication is made clear to consumers while any provider offers should go at the end to avoid the risk of consumers dismissing the notification as general marketing information.

### **The notification should be in a form that is understandable for consumers**

- 4.85 We consider that the information we propose to be included in a single end-of-contract notification, and sent in accordance with a consumer’s chosen or normal method of communication, will ensure that consumers are more likely to understand the information it contains and the implications of coming to the end of their minimum contract period. This will enable them to make informed decisions on whether and when to act.
- 4.86 We have varied the information set out in the main body of the notification depending on the communication channel used in order to ensure the messages are understandable in different formats. We have also sought to ensure that certain core information is placed upfront so customers understand the context of the message regardless of the communication channel used.
- 4.87 The requirement for providers to make such notifications available in accessible formats should ensure that customers who have specific communication needs are able to receive the notification in a form that is most suitable for them.

### **The notification should be timely so that when consumers receive the information they can act upon it appropriately**

- 4.88 Requiring the proposed information to be sent when the customer is nearing the end of their minimum contract period ensures that customers are informed at a time when they are able to make decisions on how they want to proceed, and, if appropriate, take necessary steps in a timely manner. This may include shopping around for other offers and giving required notice if they want to cancel or switch.

### **The notification should as far as possible mitigate any unintended consequences for both consumers and providers**

- 4.89 As we are proposing that the notification is sent 40-70 days before the end of the minimum contract period, there is a risk that some consumers may cancel their contract before their actual contract end date and then have to pay early termination charges. Our proposal for the notification to inform consumers that early termination charges no longer apply after the minimum contract period will help to mitigate this risk.
- 4.90 The proposal to include information about applicable notice periods will help to avoid the unintended consequence of the customer switching provider before the end of their notice period and/or having to pay for old and new services at the same time.
- 4.91 The proposed requirement for the notification to list the other services taken with the same provider aims to help consumers avoid unintended consequences and make an



informed decision about next steps as there could be implications for them if they were to change deal.

- 4.92 We have sought to design our proposal in a clear, simple and achievable way, which minimises the risk of confusion as to what providers must include in the notification while also giving them flexibility in their communications with their customers. While we are proposing for specific content to be included, we do not propose to prescribe the actual words or language to be used in the notification. We note that some providers adopt a particular tone/style when communicating with their customers and we would not want our proposals to limit their ability to communicate with their customers in the most effective way.

## **Our proposal for a one-off “out-of-contract notification” at implementation**

- 4.93 As set out in Section 3, many consumers who are already out-of-contract will not have been informed at the appropriate time that their minimum contract period is ending or that it has ended. Where providers have not previously provided their customers with this information, it is equally important that our proposals address the harm we have identified in relation to these customers.
- 4.94 A one-off out-of-contract notification would ensure these customers are appropriately informed that they are out-of-contract and of the relevant implications of remaining on their existing deal.
- 4.95 We propose that providers should be required to send a one-off “out-of-contract notification<sup>144</sup>” to all residential and Small Business customers that are already outside of their minimum contract period if they have not previously been informed of the information proposed in the end-of-contract notification.

### **Content of the out-of-contract notification**

- 4.96 In our 2018 end-of-contract notification qualitative research, out-of-contract customers did not differ markedly from the other consumers in their responses to the end-of-contract notification content tested. Participants considered a notification would raise their awareness of being out-of-contract, what that meant and the options available to them. The notification would also act as a reminder of the details of their existing contract which would facilitate a decision on whether to engage or not.<sup>145</sup>
- 4.97 We propose that a potential out-of-contract notification would differ slightly in content from an end-of-contract notification, given it would be sent after the minimum contract period has expired. We propose that the notification for those already beyond their minimum contract period would inform the customer of:

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<sup>144</sup> By this, we mean a notification to customers who are already outside of their minimum contract period and therefore considered to be “out of contract”.

<sup>145</sup> Ofcom’s end of contract notification qualitative research 2018, conducted by Jigsaw. Slides 38-39.

- The date the customer’s minimum contract period ended and the fact that early termination charges no longer apply, but noting any applicable notice periods;
- The services which the provider currently provides to the customer under that contract, including additional benefits that accompany the contract, such as free subscriptions to other services (e.g. Netflix, Spotify) and the monthly subscription price currently paid by the customer for those services. This should include a list of other services taken with the same provider pursuant to other contracts; and
- The options available to the customer, including a message that the customer may be able to make savings by exploring the available options. The notification to customers of mobile services must include SIM-only as one of the options.

4.98 We consider our proposed content for out-of-contract notifications to be appropriate as it will ensure that consumers are provided with the same information as we have provisionally concluded as necessary for end-of-contract notifications, where this remains relevant.

4.99 The notification will tell them that they are no longer in their minimum contract period and the proposed information on early termination charges, available options and possible savings will help them to understand what it means to be out-of-contract. Providing information on applicable notice periods helps to ensure that consumers are informed that they still need to give their provider notice if they want to cancel or switch even if their minimum contract period has ended.

4.100 There are unlikely to be any service or price changes relevant to an out-of-contract notification and we do not consider that it would be relevant or effective to include historical service or pricing information (e.g. services or prices paid before the minimum contract period end date and/or any offers or discounts applied during the minimum contract period).

### **Structure of the out-of-contract notification**

4.101 In order to be effective, we propose that the structure of the out-of-contract notification should follow that proposed for end-of-contract notifications, for the same reasons. That is, for the date the customer’s minimum contract period ended to be presented upfront in the notification and for any provider offers to appear towards the end of the notification.

### **Method of sending the out-of-contract notification**

4.102 We propose that this one-off out-of-contract notification would be sent to consumers using the same method and principles set out for end-of-contract notifications, for the same reasons. That is, we propose that providers be required to send the notification in a durable medium using the customer's preferred method of contact (if known). If the customer's contact preference is unknown, the provider should use the durable medium by which it notifies the consumer of any available bills.

4.103 Consistent with our position on end-of-contract notifications sent via SMS above, we recognise the need to keep out-of-contract notifications by SMS (text messages) relatively simple and concise in the interest of effective messaging. Therefore, we consider there is

certain core information which should be included in the main body of the SMS. The provider would also be required to provide the other details in either another durable medium (SMS, letter or email), or via a link in the SMS which should take the consumer to their online account. Providers need to be clear in the SMS where the other information will be available.

4.104 We propose the following for out-of-contract notifications sent by SMS:

<b>Core information which must be included in the main body of the SMS</b>	<b>Information that can be included in either another durable medium or via a link in the SMS to the customer's online account</b>
The date the customer's minimum contract period ended.	The fact that early termination charges no longer apply, but noting any applicable notice periods if the customer wants to cancel or switch.
The monthly subscription price currently paid by the customer.	The services which the provider currently provides to the customer and if applicable, a list of other services taken with the same provider pursuant to other contracts.
That SIM-only is an available option (mobile only)	Options available after the minimum contract period has ended, including a message that the customer may be able to make savings by exploring the available options.
How the information in the next column will be provided (e.g. the online link or other durable medium).	

4.105 We also propose, similarly to end-of-contract notifications, to require providers to send out-of-contract notifications in a format such as electronic, braille or large print, where customers have registered to receive bills in these types of ways/requested this and/or where the provider is aware that the customer requires communications in alternative formats.

### **Proposal on length of contracts to be covered**

4.106 As with the proposed end-of-contract notification, we propose that the requirement to send a one-off out-of-contract notification should apply with respect to consumers that were previously subject to a minimum contract period of **six months or more**, where that

minimum contract period has since ended and the consumer remains on ‘rolled over’ or ‘out-of-contract’ terms.

- 4.107 This takes into account that some providers currently offer contracts that have a minimum contract period of 9 months as well as the more typical 12, 18 or 24 months.

### **Assessment of proposal for out-of-contract notification**

- 4.108 We have assessed whether our proposal for a one-off notification to customers who are already outside of their minimum contract period satisfies the criteria set out at the beginning of this chapter:

#### **The notification should be effective in addressing consumers’ lack of awareness or lack of sufficient information about the end of their minimum contract period and the implications of this**

- 4.109 As set out in Section 3, consumers who are already out-of-contract will not receive an end-of-contract notification advising them that their minimum contract period is ending. Where providers have not previously provided their customers with all of the information that we are proposing for the end-of-contract notification, it is equally important an out-of-contract notification addresses the harm we have identified in relation to these customers.
- 4.110 A one-off out-of-contract notification would ensure these customers are appropriately informed that they are out-of-contract and the relevant implications of remaining on their existing deal. For these reasons, we propose that the content of the notification should inform the customer that their minimum contract period has already ended. To help consumers to understand what this means, we propose that the notification should inform them that early termination charges no longer apply.
- 4.111 Including information about current services and price would make it clear to the customer which service(s) the notification is for. The proposal to include the options available to the customer, including the possibility of making savings, will ensure they understand what, if anything, they can do next to find an improved deal.
- 4.112 To ensure that the notification is effective, we have proposed that certain core information is placed upfront so that the context of the communication is made clear to consumers while any provider offers should go at the end to avoid the risk of consumers dismissing the notification as general marketing information.

#### **The notification should be in a form that is understandable for consumers**

- 4.113 We consider that the information we propose to be included in the one-off out-of-contract notification, and sent in accordance with a consumer’s chosen or normal method of communication, will ensure that consumers are more likely to understand the information sent and the implications of having reached the end of their minimum contract period. This will enable them to make informed decisions on whether and when to act.

- 4.114 We have varied the information set out in the main body of the notification depending on the communication channel used in order to ensure the messages are understandable in different formats. We have also sought to ensure that certain core information is placed upfront so customers understand the context of the message regardless of the communication channel used.
- 4.115 The requirement for providers to make such notifications available in accessible formats should ensure that customers who have specific communication needs are able to receive the notification in a form that is most suitable for them.

### **The notification should be timely so that when consumers receive the information they can act upon it effectively**

- 4.116 We propose that providers should send a one-off notification to customers who are already outside of their minimum contract period **within nine months of our decision statement** (we address our proposed implementation timescales further in Section 5). As the customer is already out-of-contract, the proposed information about the options available to them is particularly relevant as they are able to take immediate action subject to any notice periods, which they will be made aware of.

### **The notification should as far as possible mitigate unintended consequences for both consumers and providers**

- 4.117 We are proposing that this notification should make clear that the customer has already reached the end of their minimum contract period and of any applicable notice periods to ensure that customers who cancel their subscription understand that they still have to pay for services with their current provider until the end of any notice period. This will also help to avoid the unintended consequence of the customer switching provider before the end of their period and/or having to pay for old and new services at the same time.
- 4.118 The proposed requirement for the notification to list the other services taken with the same provider aims to help consumers avoid unintended consequences and make an informed decision about next steps as there could be implications for them if they were to change deal.
- 4.119 We have sought to design our proposal in a clear, simple and achievable way, which minimises the risk of confusion as to what providers must include in the notification while also giving them flexibility in their communications with their customers. While we are proposing for specific content to be included, we do not propose to prescribe the actual words or language to be used in the notification. We note that some providers adopt a particular tone/style when communicating with their customers and we would not want our proposals to limit their ability to communicate with their customers in the most effective way.

### **Provisional conclusion**

- 4.120 We are proposing to require all providers to send two types of notification:

- an end-of-contract notification to be sent before the customer reaches the end of their minimum contract period; and
- an out-of-contract notification to those customers who are already out of contract and who have not previously been informed of the information proposed in the end-of-contract notification.

4.121 Our proposals for the notifications are summarised below:

End-of-contract notification	Out-of-contract notification
<p>Proposed content:</p> <ul style="list-style-type: none"> <li>• The date on which the customer’s minimum contract period ends, including that early termination charges no longer apply at that point. It should also include details of any applicable notice periods.</li> <li>• The services which the provider currently provides to the customer under that contract, including additional benefits that accompany the contract, such as free subscriptions to other services (e.g. Netflix, Spotify); the monthly subscription price currently paid by the customer for those services (including any historical discounts); and any changes to the services provided and/or monthly subscription price paid by the customer upon the minimum contract period ending. This should include a list of other services taken with the same provider pursuant to other contracts.</li> <li>• The options available to the customer after the minimum contract period has ended, including a message that the customer may be able to make savings by exploring the available options. The notification to customers of mobile services must include SIM-only as one of the options.</li> </ul>	<p>Proposed content:</p> <ul style="list-style-type: none"> <li>• The date the customer’s minimum contract period ended and the fact that early termination charges no longer apply, but noting any applicable notice periods.</li> <li>• The services which the provider currently provides to the customer under that contract, including additional benefits that accompany the contract, such as free subscriptions to other services (e.g. Netflix, Spotify); the monthly subscription price currently paid by the customer for those services; and a list of other services taken with the same provider pursuant to other contracts.</li> <li>• The options available to the customer, including a message that the customer may be able to make savings by exploring the available options. The notification to customers of mobile services must include SIM-only as one of the options.</li> </ul>

<p>Proposals for structure:</p> <ul style="list-style-type: none"> <li>• The minimum contract period end date and any resulting price changes should appear upfront.</li> <li>• If providers choose to include an offer for the customer then that information should go at the end of the notification.</li> </ul>	<p>Proposals for structure:</p> <ul style="list-style-type: none"> <li>• The date the customer’s minimum contract period ended should appear upfront.</li> <li>• If providers choose to include an offer for the customer then that information should go at the end of the notification.</li> </ul>
<p>Proposals for sending:</p> <ul style="list-style-type: none"> <li>• The notification should be sent in a durable medium using the customer’s preferred communication channel.</li> <li>• The end-of-contract notification should be sent to consumers between 40-70 days before the end of their minimum contract period.</li> </ul>	<p>Proposals for sending:</p> <ul style="list-style-type: none"> <li>• The notification should be sent in a durable medium using the customer’s preferred communication channel.</li> <li>• The one-off out-of-contract notification will be sent to customers who are already out of their minimum contract period at the time of implementation and have not previously been informed of all the information proposed for the end-of-contract notification.</li> </ul>

4.122 We have assessed our proposals against set criteria as noted throughout this section to ensure that:

- They are effective in addressing consumers’ lack of awareness and lack of sufficient information about the end of their minimum contract period and the implications of this, so that they can avoid unexpected and unwelcome changes to their service or price, make informed decisions and/or avoid incurring time and effort in monitoring and seeking out this information.
- They are in a form that is understandable for consumers.
- They are timely so that when consumers receive the information they can act upon it effectively.
- They should as far as possible mitigate any unintended consequences for both consumers and providers.

4.123 In our judgement, we consider our remedy design to be appropriate to address the consumer harm identified in Section 3 and to achieve our policy objectives. We discuss the overall proportionality of our proposals in the next section.



## Consultation questions

4.124 We welcome stakeholder comments on the following questions in relation to our proposed remedy as set out in this section:

**Question 4:** Do you agree with our proposals on the content of the end-of-contract notification?

**Question 5:** Do you agree with our proposals on the structure, method, timing and frequency of the end-of-contract notification?

**Question 6:** Do you agree with our proposals on the content of the out-of-contract notification?

**Question 7:** Do you agree with our proposals on the structure, method and frequency of the out-of-contract notification?

Please provide evidence to support your views.

## 5. Provisional conclusions on the proportionality of our proposals

5.1 In this section we set out our assessment of the likely impact of our proposals. In doing so, we explain why we consider that our proposals are proportionate, are an effective means of achieving our objectives, and why we consider that they do not give rise to adverse effects which are disproportionate to the achievement of those objectives.

### Assessing the proportionality of our proposals

- 5.2 As set out in Section 2, section 3(1) of the Act states that it shall be the principal duty of Ofcom to further the interests of citizens in relation to communications matters and to further the interests of consumers in relevant markets, where appropriate by promoting competition.
- 5.3 In Section 3, we set out our concerns that some consumers are not notified by their providers at an appropriate time, and are unaware of important information about the end of their minimum contract period, what this means for their service and price, or the options available to them at this point.
- 5.4 We also set out our concerns for those who go out-of-contract and move onto rolling contract terms. Many consumers pay more as a result of higher prices and many miss out on deals that could improve their package or save them money.
- 5.5 In the light of those concerns, we have explained that we consider it reasonable that consumers are notified of this information at an appropriate time to ensure they can avoid price increases and service changes and can make informed decisions about their existing deal and when and how to exercise choice. It is not reasonable that providers do not currently provide their customers with this information and do not give them an opportunity to do this.
- 5.6 Under our regulatory principles we operate with a bias against intervention, which is derived from our duty in section 3(3) of the Act to have regard to the principles under which regulatory activities should be (among other things) proportionate and targeted only at cases in which action is needed.<sup>146</sup>
- 5.7 We have set out in Section 4 why we propose that action, in the form of requiring providers to send their customers end-of-contract notifications and a one-off out-of-contract notification in the manner described, is required in order to address the harms we have identified. We have also considered ways to make these notifications less onerous for providers, in how we have designed these notifications, as set out in that section.
- 5.8 In assessing proportionality, we consider:

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<sup>146</sup> See Ofcom's regulatory principles: <https://www.ofcom.org.uk/about-ofcom/what-is-ofcom>

- whether a proposed measure is an effective means of achieving our objectives;<sup>147</sup>
- whether the proposed measure is necessary to achieve those objectives, or whether those objectives could be achieved by a less onerous approach; and
- whether the proposed measure gives rise to adverse effects which are disproportionate to the aims pursued.

## Effective means of achieving our objectives

- 5.9 As set out in Section 2, our policy objectives are to ensure that:
- consumers are informed at an appropriate time when their minimum contract period is coming to an end, and of any changes to price or services that will occur as a result; and
  - consumers are informed that their minimum contract period has already come to an end if they were not previously informed of this.
- 5.10 It is reasonable to expect that providers will treat their customers fairly in the provision of communications services. An essential aspect of fairness is that providers ensure their customers are informed, at the appropriate time, of important information about the services they buy. This will enable consumers to make informed decisions and will protect them against unexpected and unwelcome changes to their service or price (such as a price increase at the end of their minimum contract period). In addition, consumers will be able to make informed decisions about whether to take up a new deal with their current provider, move to a new deal with a different provider or make an active decision to stay on an existing deal.
- 5.11 In Section 3, we set out our concerns that most providers do not notify their customers, and some consumers are not aware of, when their minimum contract period is coming to an end, as well as price increases and service changes that may apply at the end of that period. In addition, given the complex nature of communications markets, some consumers do not understand what coming to the end of their minimum contract period means and lack awareness of the options available, and the possible savings they could achieve from moving to a new deal.
- 5.12 We also set out that we consider that this lack of information leads to a significant number of consumers moving to rolling out-of-contract terms. As a result, we are concerned that many consumers pay higher prices than they need to, and do not benefit from improved service packages:
- Many consumers are subject to automatic price increases, or service changes, at the end of the minimum contract period. We estimate that more than 10 million customers are on deals with an automatic price increase at the end of the minimum contract

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<sup>147</sup> In order for an intervention to be proportionate, the objectives pursued must also be legitimate. We consider that our objectives are legitimate in light of our statutory powers and duties. In particular, and as set out in Section 2, one of our principal duties is to further the interests of consumers (section 3(1) of the Act). In performing this duty, we must have regard to the interests of those consumers in respect of choice, price, quality of service and value for money (section 3(5) of the Act).

period. Due to their lack of awareness, some consumers go out-of-contract and are unable to avoid these changes.

- More generally, consumers who lack awareness cannot make informed decisions on when and whether they should search for a better deal. We are concerned that some of these consumers are unable to make savings, or benefit from an improved service package, at the end of their minimum contract period. For example, customers taking a bundle of landline and broadband services spend, on average, around 20% more when they are out-of-contract. Also, certain mobile consumers continue to pay the same price (which includes the cost of handset) after the end of their minimum contract period, which could be significantly higher than the price they would pay if they switched to a SIM-only deal.

5.13 For those consumers that are aware of this information, we consider it unreasonable that they have to incur time and effort to retain, monitor and seek out this information.

5.14 Section 3 also sets out our view that Small Businesses are likely to experience similar harm to residential consumers, in terms of (i) not being notified and aware of this information, (ii) paying higher prices or not benefitting from improved service packages, and (iii) having to proactively seek out the relevant information. We consider that Small Businesses are likely to behave in a similar way and raise similar concerns to residential consumers.

5.15 To meet our policy objectives, and address the harms we have identified, we consider it reasonable that providers inform their customers at an appropriate time of important information about their minimum contract period. We have identified proposals in Section 3 and 4 which would require providers of PECS to send end-of-contract notifications and a one-off out-of-contract notification to all their residential and Small Business customers. The notifications would include specific information, including:

- the date on which the customer's minimum contract period will end, or has ended;
- the services currently provided to the customer and the price paid;
- changes to the service and price at the end of the minimum contract period, where relevant; and
- that the customer has options available to them (such as SIM-only deals for mobile) and may be able to make savings.

5.16 Our assessment is that these notifications will be an effective means of addressing the harms we have identified and achieving our policy objectives because they:

- inform consumers of the date on which their minimum contract period ends/ended (as well as what happens at the end of that period for relevant consumers), which will signal to consumers when they should be assessing their existing deal and other available options;
- where relevant, will help consumers to avoid unexpected and unwelcome changes to their service and price;
- will help consumers to make informed decisions about their existing deal and whether they should be shopping around for a new one, and
- more generally ensure consumers do not incur time and effort in monitoring and seeking out this information.

5.17 In Section 4, we have also assessed the structure, format, timing and frequency of our proposed notifications and provisionally conclude that in this regard our proposed notifications would be effective for the following reasons:

- they are in a form that is understandable for consumers as certain core information will be placed upfront so that the context of the communication is made clear to consumers, while any provider offers should go at the end to avoid the risk of consumers dismissing the notification as general marketing information. We have also varied the information set out in the main body of the notification depending on the communication channel used in order to ensure the messages are understandable in different formats. Notifications will be sent in accessible formats to those with specific communication needs;
- they are sent in accordance with the customer’s chosen or normal method of communication and in a durable medium so that the customer has a record of the information and can refer back to it when needed<sup>148</sup>;
- they will be sent at an appropriate time – 40 to 70 days before the end of the minimum contract period for those that are in-contract and within 9 months of Ofcom issuing a final statement for those that are out-of-contract, so that when consumers receive the information they can act upon it appropriately;
- they should as far as possible mitigate any unintended consequences for both consumers and providers. In particular, we have sought to design our proposal in a clear, simple and achievable way to minimise the risk of confusion as to what providers must include in the notification while also giving them the flexibility in their communications with their customers.

5.18 Overall, we provisionally conclude that our proposals will be effective at addressing the consumer harm we have identified and meeting our policy objectives.

## Necessary to achieve our policy objectives

5.19 We consider that imposing a requirement for providers to send end-of-contract notifications and, where applicable, a one-off out-of-contract notification to residential consumers and Small Businesses are necessary to address the harm that we have identified and to achieve our policy objectives. We have considered whether there is a potentially less onerous approach, such as maintaining the status quo, strengthening information provided when the service is purchased, or mandating provision of end-of-contract information online or via app. We do not consider that any of these options would achieve our policy objectives for the reasons set out in Section 3.

5.20 We have also considered whether the content, structure, format, timing and frequency of our proposed notifications are necessary to achieve our policy objectives. We have explained in Section 4 and above, why we consider that these aspects are necessary in order to make our notifications effective. Taking into account the need to ensure our

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<sup>148</sup> For notifications sent via SMS, we propose that certain core information must be included in the main body of the SMS. Other details can be provided in either another durable medium (SMS, letter or email), or via a link in the SMS which should take the consumer to their online account.

proposals are the least onerous to achieve our objectives, there are aspects of the design of the notifications which we have considered but which do not form part of our proposals:

- Being more prescriptive in terms of the actual words and language to be used in the notifications. We have decided against this as we would not want our proposals to limit providers' ability to communicate with their customers in the most effective way.
- Requiring the inclusion of the following content, which we do not consider would be appropriate and/or proportionate to include given our research findings:
  - Total price paid by the customer over the term of the contract;
  - Detailed information about other contracts with the same provider;
  - A link to the mobile provider's webpage on handset unlocking, where relevant;
  - A link to information about mobile coverage, where relevant;
  - A link to switching information on Ofcom's website.
- Prohibiting providers from including their own offers in the notifications. We have decided not to propose this; however, we are proposing to require that this type of information does not precede the mandatory information that we have proposed.
- Requiring the sending of multiple end-of-contract notifications, e.g. one before the end of the minimum contract period and one at the end of the period. We consider that one notification would be enough to address our key concern that most providers are not (or not consistently) informing consumers at the appropriate time of certain key information.
- Requiring a more specific and shorter timeframe for sending end-of-contract notifications to consumers. We recognise that a range of 40 to 70 days before the end of the minimum contract period gives providers some flexibility for sending these and should help stagger their customers' communications accordingly.
- Requiring the inclusion of historical pricing information in the one-off out-of-contract notification (e.g. prices paid before the minimum contract period end date). We do not think this would be as relevant or effective as these customers are already beyond their minimum contract period.

## **Consideration of any adverse effects which are disproportionate to our policy objectives**

- 5.21 We have considered whether our proposals to require providers to send end-of-contract and out-of-contract notifications would produce adverse effects, and in particular generate costs to industry, which are disproportionate to the policy objectives we are pursuing, in light of our statutory duties.
- 5.22 We summarise below our assessment of the impact of our proposals on providers and consumers. Our detailed assessment is set out in Annex 6 and Annex 7.

## Impact assessment of our proposals

- 5.23 We have considered the costs and benefits for those stakeholders that are likely to be impacted by our proposals. Some of these factors can be quantified, and where that is possible we have looked at these in order to inform our assessment. While other factors are less susceptible to meaningful quantification, they are important in our overall assessment of the costs and benefits associated with our proposals.
- 5.24 We are of the view that the costs of implementing the proposed notifications should be limited, given our proposals would require providers to send a single communication to their customers and that it would include information that is available from a customer's account. Providers communicate with their customers regularly, including as they approach the end of their contract, and we have designed our notifications to ensure that they can fit easily with how providers already communicate with their customers. We have also provided flexibility in terms of when the notifications are sent, in order to allow the notifications to be sent in batches and thus limit costs.

### Residential consumers

- 5.25 We met with a number of providers to discuss the processes required to introduce the proposed end-of-contract and out-of-contract notifications. We also received indicative cost estimates for these processes from some providers. On the basis of this input, we identified three types of costs: one-off implementation costs, ongoing costs to send end-of-contract notifications and one-off costs to send out-of-contract notifications. Our indicative cost estimates focus on the costs to residential consumers (as does our illustrative quantified assessment of benefits).
- 5.26 Providers would need to incur one-off implementation costs so that their systems can accommodate the extraction of information from customer accounts and distribute end-of-contract notifications to customers.<sup>149</sup> Using the providers' cost estimates and other information we have received, our indicative estimates of one-off implementation costs across industry suggest they are of the order of c.£4 million for mobile services and c.£4-6 million for landline, broadband and pay TV services combined. These estimates support our view that implementation costs are likely to be limited.
- 5.27 Second, providers would incur ongoing costs associated with sending the proposed end-of-contract notifications. Our indicative estimates, based on information from providers, suggest that these costs would be negligible for mobile providers, as we anticipate that the end-of-contract notifications would be sent via SMS at no material cost. These costs are likely to be higher for landline, broadband and pay TV customers (including standalone, dual play and triple play) service providers, as they are likely to communicate with some of their customer base via letter. Nonetheless, based on indicative estimates received from some providers, these costs are also relatively limited, of the order of c.£8-15 million NPV over ten years for residential customers.

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<sup>149</sup> See Annex 8.

- 5.28 Third, providers would also incur one-off costs to send notifications to customers currently out-of-contract, which we estimate to be c.£2m for residential customers.
- 5.29 Overall, based on the evidence outlined above and described in more detail in Annex 6, our provisional view is that the cost for industry to implement our proposed notifications is about £4 million for mobile operators and £14-23 million for landline, broadband and TV operators over a 10-year time horizon.
- 5.30 In relation to benefits, we expect that some consumers will avoid higher prices by seeking out a new deal and exercising choice as a result of our proposals. We consider that the savings that could be made by these consumers are potentially material. As we set out in Section 3, out-of-contract customers spend on average ~20% more than in-contract customers for dual play, triple play and standalone pay TV.<sup>150</sup> Similarly, we find that mobile handset customers who are out-of-contract spend on average ~34% more than mobile SIM-only customers who are in-contract. Separately, we consider that some consumers will be able to change to a product which is more suited to their needs. This could involve a reduction in the price they pay for the same or a better service, or an improvement in the service they receive for no (or only a limited) increase in the price they pay.
- 5.31 We recognise that some of this benefit may be offset, if providers have the incentive to raise in-contract prices in response to losing revenue from out-of-contract customers. However, this does not lead us to change our provisional conclusion that our proposals would result in a net benefit to consumers. First, there are reasons why providers might not have this incentive; in particular, where the level of in-contract prices is set independently from out-of-contract revenues, or where greater engagement by consumers would create pressure for providers to lower in-contract prices. Second, even where they might, providers are unlikely to pass on in full their loss of out-of-contract revenues into higher in-contract prices. Third, we also expect our proposals to generate additional benefits by:
- reducing the time and effort incurred by a second group of consumers, those who currently have to seek out this information; and
  - lowering prices and encouraging choice and innovation by increasing the level of competition in the market.
- 5.32 While the scale of the net benefits of our proposals are inherently uncertain, we have a reasonable basis to believe that the benefits of this intervention will exceed the costs. In particular, we have conducted an illustrative analysis of the balance between benefits and costs, making a number of simplifying assumptions and abstracting from a number of effects.<sup>151</sup> This analysis illustrates that only a limited proportion of consumers would have

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<sup>150</sup> We note that we do not find a similar comparison for mobile customers – consistent with the provider data that only a relatively limited fraction of their subscribers are on contracts which have an automatic price increase at the end of the minimum contract period.

<sup>151</sup> Such as benefits in terms of enhanced competition, savings in time and effort for consumers who are aware of the relevant information, and potential partial offsetting effects by providers.



to avoid going out-of-contract in order for the benefits to be larger than the indicative cost estimates we have produced:<sup>152</sup>

- For residential mobile, benefits would exceed a cost estimate of c.£4 million if end-of-contract notifications led to c.23,000 consumers exercising choice at the end of their minimum contract period, and saving £6 per month for the years they would avoid being out-of-contract.<sup>153</sup> This equates to less than 1% of consumers on a mobile handset contract who are in-contract, but lack awareness of their contract end date.<sup>154</sup>
- For landline, broadband and pay TV services, benefits would exceed the higher boundary of our cost estimate of c.£23 million if our proposal led to c.75,000 customers exercising choice earlier, and saving between £6 and £13 per month (depending on service) for the years they would avoid being out-of-contract.<sup>155</sup> This was derived as c.5,000 out-of-contract consumers signing up to a new deal as a result of out-of-contract notifications (this equates to a negligible fraction of out-of-contract customers),<sup>156</sup> and c.70,000 in-contract consumers avoiding going out-of-contract as a result of our end-of-contract notifications (this equates to c.2% of in-contract consumers who lack awareness on their contract end date).<sup>157</sup>

### Small Businesses

- 5.33 While we recognise that there are additional providers who would incur implementation costs to send notifications to Small Businesses, the residential analysis suggests that these costs are relatively limited. Moreover, some of these implementation costs may be lowered further, to the extent that they can be shared with the introduction of notifications to residential consumers.
- 5.34 In relation to the distribution costs, we expect the average incremental cost for sending one-off out-of-contract notifications and end-of-contract notifications to be similar to the cost for residential consumers. These costs would therefore be negligible for Small Business consumers who purchase mobile services. While more substantial for other services, they will reflect the number of notifications sent, and thus scale in line with the size of the Small Business base.

<sup>152</sup> These illustrations are only one combination of the minimum number of out-of-contract and in-contract consumers who would have to re-contract or avoid going out-of-contract for the benefits to exceed the indicative cost estimates. Benefits could also exceed the cost with many other combinations, such as a smaller number of in-contract consumers combined with a larger number of out-of-contract consumers.

<sup>153</sup> £6 is the difference between the average spend of mobile handset customers who are out-of-contract and SIM-only customers who are in-contract. We describe our approach in greater detail at Annex 6.

<sup>154</sup> Our analysis determines the number of out-of-contract consumers who would have to re-contract in order for benefits to exceed the one-off cost of sending out-of-contract notifications. Since we estimate that this cost is negligible for mobile customers who are out-of-contract, equally we consider that only a negligible number of out-of-contract consumers would have to re-contract in order for benefits to exceed these costs.

<sup>155</sup> These savings are the difference between the average spend of in-contract customers and out-of-contract customers for each of these services (dual play, triple play and standalone pay TV).

<sup>156</sup> This is calculated as the number of out-of-contract consumers who would have to re-contract in order for the benefits to exceed the one-off cost of sending out-of-contract notifications. We describe this approach in greater detail in Annex 6.

<sup>157</sup> This is calculated as the number of consumers who are currently in-contract, and who would have to avoid going out-of-contract in order for the benefits to exceed the implementation and ongoing costs for end-of-contract notifications. We describe this approach in greater detail in Annex 6.

- 5.35 In terms of benefits, there are similarities between Small Businesses and residential consumers. We therefore expect that the benefit to a Small Business from exercising choice could be similar. In any case, the illustrative analysis for residential consumers suggests that only a limited fraction of consumers would have to avoid being out-of-contract and paying higher prices to ensure the benefits exceed the costs, even at lower levels of the benefit for a given consumer.
- 5.36 Overall, we have a reasonable basis to believe that the benefits of the proposed notifications to Small Business will exceed the costs.

### **Provisional view on adverse effects which are disproportionate to our policy objectives**

- 5.37 Having considered the impact of our proposals on providers and consumers, we do not consider they would produce adverse effects which are disproportionate to our policy objectives. We consider that the objectives we are pursuing, and the benefits that would be secured by our proposed reforms, are important and legitimate in light of our statutory duties. Indeed, we consider achieving this outcome is a priority in our work on ensuring that consumers are able to gain the benefits of competition by being able to engage with the market and make informed decisions.

### **Provisional conclusions on proportionality**

- 5.38 On the basis of the assessment above, our provisional view is that our proposals are both effective and the minimum necessary to achieve our policy objectives. We consider that end-of-contract notifications and a one-off out-of-contract notification will deliver benefits to residential consumers and Small Businesses, and our initial assessment of the potential costs for providers are not disproportionate to the benefits that are likely to be secured.
- 5.39 In our view, our proposals would address the harms we have identified and achieve our policy objectives. Our policy objectives are clear in terms of ensuring that providers treat their customers fairly in the provision of communications services. We consider it entirely reasonable that providers inform their customers at an appropriate time of important information about their minimum contract period.
- 5.40 In our view, our proposed notifications will address the harms we have identified and achieve our policy objectives, in summary, by:
- **Ensuring consumers know when to review their existing deal**  
Consumers will be told when their minimum contract period ends/ended, which will signal to consumers when they should be assessing their existing deal and other available options;
  - **Ensuring consumers can avoid unexpected price and service changes**  
Where relevant, consumers will be advised of price and service changes that will ensure they are able to avoid them by moving to a deal that allows them to save money or benefit from a better service package.

- **Ensuring consumers are informed about the options available to them at end of the minimum contract period**

Consumers will be informed of what it means to be out-of-contract, particularly that no early termination charges apply and that they are able to move to a better deal that could save them money. This ensures that they are able to make an informed decision and exercise choice, whether that means moving to a better deal with their existing provider, switching provider or deciding to remain on their current deal.

- 5.41 Our assessment of impacts shows that the costs of implementing our proposals are likely to be limited and exceeded by the benefits to consumers. We therefore provisionally judge that our proposals are proportionate in order to achieve our policy objectives.

## Implementation

- 5.42 At this stage, we estimate that our proposals would take six months to implement between the date of our final statement and the introduction of end-of-contract notifications. Most providers already have systems in place that allow them to communicate with customers on a regular basis; however, we recognise that this is not done in a consistent way between providers and that it is appropriate to give providers a period of time to implement our proposals. This period will be particularly relevant to ensuring that the notifications include personalised information, such as pricing and service information. Following the implementation period, the sending of end-of-contract notifications will naturally be staggered over time by customers' contract end dates.
- 5.43 In respect of out-of-contract notifications, while these are likely to require a similar implementation period, we recognise that may be a large volume of these to be sent and do not consider it appropriate to require providers to send all of them at the same time. Therefore, we propose allowing an additional period of time in order for providers to manage this process and stagger the sending out of these notifications. We consider that an additional period of 3 months would be appropriate to allow for this. This would mean that all relevant customers should receive an out-of-contract notification from their provider within 9 months of the date of our final statement.

## Proposed general conditions

- 5.44 Annex 9 sets out our Notification of the draft general conditions we are proposing to introduce to implement our proposals. We propose to include the new general conditions under Part C1 of the General Conditions. It also sets out proposed amendments to an existing General Condition and additions to the definitions section of the General Conditions, which support the proposed draft new conditions.
- 5.45 It is important to note that in September 2017, Ofcom published a statement about changes that we have decided to make to the general conditions of entitlement (the "GC Review Statement"), in order to ensure the general conditions are up to date and reflect

Ofcom's current priorities.<sup>158</sup> The revised general conditions will come into force on 1 October 2018, and the current conditions will be revoked on the same date.

- 5.46 For this reason, the proposed new condition set out in Annex 9 should be read alongside the revised general conditions that will come into force on 1 October 2018.

## Legal tests and statutory duties

- 5.47 Section 2 of this document sets out our general statutory powers and duties as well as the powers, duties and requirements relevant to the setting of general conditions. In this subsection we explain why the introduction of our proposed general condition accords with these provisions of the Act.

### Ofcom's general duties

- 5.48 As explained in this consultation, our provisional judgment is that the introduction of a requirement to send end-of-contract notifications and a one-off out-of-contract notification in the proposed draft general conditions fulfils our duty to further the interests of citizens and consumers by ensuring that they are informed at an appropriate time of when their minimum contract period is coming to an end or has come to an end, as well as the implications (if any) for the services they receive and the price they pay, and their options. These proposed conditions will therefore address the harm to consumers that we have identified in this document.
- 5.49 This objective is in line with our principal duty set out in section 3(1) of the Act, as well as our duty to have regard to: the interest of consumers in respect of choice, price, quality of service and value for money (section 3(5) of the Act); the desirability of encouraging investment in relevant markets (section 3(4)(d) of the Act); the needs of persons with disabilities, of the elderly and those with low incomes (section 3(4)(i) of the Act); and the opinions of consumers in relevant markets (section 3(4)(k) of the Act), insofar as our proposals have been informed by research into consumers' expectations of the information they should receive.
- 5.50 We also assess that the introduction of the proposed regulation is in line with our obligation to ensure that our regulatory activities are proportionate and targeted only at cases in which action is needed (section 3(3) of the Act). We have sought to design our proposed intervention in a manner that minimises implementation costs for industry, with a view to ensuring that our proposed intervention is proportionate (as described above).

### Duties for the purpose of fulfilling EU obligations

- 5.51 We also provisionally assess that, by proposing to introduce draft general condition C[x], we are acting in accordance with the six European Community requirements in section 4 of the Act, read in light of Article 8 of the Framework Directive. Article 8 sets out the policy objectives of the Framework. These include:

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<sup>158</sup> Ofcom, *Review of the General Conditions of Entitlement*, September 2017.

- the promotion of competition in the provision of electronic communications services<sup>159</sup> by ensuring that users derive maximum benefit in terms of choice, price and quality and there is no distortion or restriction of competition in the electronic communications sector,<sup>160</sup> and
- the promotion of the interests of EU citizens by ensuring a high level of protection for consumers in their dealings with suppliers and promoting the provision of clear information (in particular, requiring transparency of tariffs and conditions for using publicly available electronic communications services).<sup>161</sup>

5.52 For the reasons set out in this document, our assessment is that introducing the proposed requirements regarding end-of-contract notifications and a one-off out-of-contract notification would be in line with the objectives of Article 8 of the Framework Directive as described above. In particular, it would increase protection for consumers by ensuring that they are informed at an appropriate time of when their minimum contract period is coming to an end or has come to an end, as well as the implications (if any) for the services they receive and the price they pay.

### **Power to set general conditions under section 51**

- 5.53 As set out in Section 2, we have the power under section 51(1)(a) of the Act to set conditions as we consider appropriate for the purpose of protecting the interests of end-users of PECS.
- 5.54 As noted in Section 3, the evidence we have gathered shows that many consumers don't know the status of the contract, some are unclear about future charges and some don't understand their options. Moreover, we have identified that there is often a financial penalty associated with remaining out-of-contract, either directly in terms of higher prices or being unable to benefit from better service packages, while for other consumers there are costs associated with the time and effort involved in seeking out contractual status information. Our proposed condition seeks to address these issues and we therefore consider that it falls within the current scope of our powers under section 51(1)(a).
- 5.55 As explained in Section 2, section 51(2) contains a non-exhaustive list of the types of condition that may be set under section 51(1)(a). Section 51(2)(d) provides that Ofcom can, by general condition, "*require the provision, free of charge, of specified information, or information of a specified kind, to end-users*". We are proposing to exercise this power.

### **Scope of proposed general conditions**

- 5.56 As stated above, we propose to include the new general conditions under Part C1 of the General Conditions. Part C1 falls under the consumer protection conditions and applies to all providers of Public Electronic Communications Networks and/or Public Electronic Communications Services. Section 46(2)(a) of the Act states that general conditions may

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<sup>159</sup> As well as electronic communications networks and associated facilities and services.

<sup>160</sup> Article 8(2)(a) and (b) of the Framework Directive.

<sup>161</sup> Article 8(4)(b) and (d) of the Framework Directive.

be applied generally to every person providing an electronic communications network or electronic communications service.

- 5.57 The term “electronic communications service” is defined in section 32(2) of the Act as: “... a service consisting in, or having as its principal feature, the conveyance by means of an electronic communications network of signals, except in so far as it is a content service.”
- 5.58 Article 2(c) of the Framework Directive contains a similar definition: “‘electronic communications service’ means a service normally provided for remuneration which consists wholly or mainly in the conveyance of signals on electronic communications networks, including telecommunications services and transmission services in networks used for broadcasting, but exclude services providing, or exercising editorial control over, content transmitted using electronic communications networks and services; it does not include information society services, as defined in Article 1 of Directive 98/34/EC, which do not consist wholly or mainly in the conveyance of signals on electronic communications networks.” So far as the General Conditions are concerned, the definition of “Electronic Communications Service” which applies is that set out in section 32(2) of the Act, which remains unchanged.
- 5.59 As we noted in our GC Review Statement and the consultation document of 29 July 2016 concerning cross-platform switching,<sup>162</sup> in the “UPC/Hilversum” case<sup>163</sup> and the “UPC/Hungary” case,<sup>164</sup> the Court of Justice of the European Union considered the application of the Framework Directive’s definition of an electronic communications service to pay TV services. The effect of these judgements is that the provision of such services falls within the definition in so far as they include the conveyance of signals on an electronic communications network. In the “UPC/Hilversum” case, the court said that is so even if:
- a) those services are also provided with other services, such as content services, that fall outside the definition;
  - b) the costs charged to consumers incorporate payments made in respect of programme content.<sup>165</sup>
- 5.60 Accordingly, the proposed new general condition that we propose will apply to providers of landline, broadband, mobile and pay TV services.

### Test for setting general conditions

- 5.61 As set out in Section 2, the test in section 47(2) of the Act must be met before we can set the proposed condition.
- 5.62 We are minded to consider that the setting of the proposed condition is:

<sup>162</sup> Ofcom, *Making switching easier and more reliable for consumers. Proposals to reform landline, broadband and pay TV switching between different platforms*, July 2016: [https://www.ofcom.org.uk/data/assets/pdf\\_file/0030/58845/making-switching-easier.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0030/58845/making-switching-easier.pdf). Paragraph 2.28

<sup>163</sup> Case C-518/11 *UPC Nederland BV v Gemeente Hilversum*, Judgment of 7 November 2013.

<sup>164</sup> Case C-475/12 *UPC v Hungary*, Judgment of 30 April 2014.

<sup>165</sup> See, in particular, paragraphs 35 – 47 and 65 of the court’s judgment in the “UPC/Hilversum” case. See also paragraphs 37 – 39 in the “UPC/Hungary” case.

- not unduly discriminatory as it would apply equally to all providers providing services to residential consumers and to those providing services to Small Businesses;
- proportionate in relation to our proposed end-of-contract and out-of-contract notifications that, as set out in section 4 and 5, taking account of our policy objectives, together with our assessment of the possible impacts, it would secure our objectives and the costs would be proportionate to the benefits that would be secured;
- transparent in that the proposed condition is set out in full in Annex 9 and explained in detail in this document. The proposed condition would also increase transparency by setting out a clear framework for the content, structure, format, timing and frequency for end-of-contract notifications and the one-off notification to customers who, on implementation, are already outside their minimum contract period;
- Finally, as part of our assessment of whether the proposed condition is proportionate, we also consider that it is objectively justifiable in that, for the reasons set out in sections 3 to 5 it seeks to address our concerns:

5.63 that providers do not inform their customers, at an appropriate time, when their minimum contract period is coming to an end and of any changes to price or services that will occur as a result, or that their minimum contract period has ended; and

5.64 about consumers' lack of awareness and/or uncertainty of contract status and the unexpected practices, including financial harm, that customers may face when they reach the end of their minimum contract period.

5.65 We welcome stakeholder comments on the following:

**Question 8:** Do you agree that our proposals are both effective and the minimum necessary to achieve our policy objectives?

**Question 9:** Do you agree with the impacts we identify, and the approach we take to quantify these impacts, in our assessment in Annex 6?

**Question 10:** Do you agree with our provisional assessment that the potential costs for providers are not disproportionate in order to achieve our policy objectives?

**Question 11:** Do you agree with our proposed implementation timescale for end-of-contract notifications and for the one-off notification to customers who are already outside of their minimum contract period?

**Question 12:** Do you have any comments on the draft condition set out in Annex 9 to this document?

Please provide evidence to support your views.

# A1. Responding to this consultation

## How to respond

- A1.1 Ofcom would like to receive views and comments on the issues raised in this document, **by 5pm on 9 October 2018.**
- A1.2 You can download a response form from <https://www.ofcom.org.uk/consultations-and-statements/category-2/end-of-contract-notifications>. You can return this by email or post to the address provided in the response form.
- A1.3 If your response is a large file, or has supporting charts, tables or other data, please email it to [improving.engagement@ofcom.org.uk](mailto:improving.engagement@ofcom.org.uk), as an attachment in Microsoft Word format, together with the cover sheet (<https://www.ofcom.org.uk/consultations-and-statements/consultation-response-coversheet>).
- A1.4 Responses may alternatively be posted to the address below, marked with the title of the consultation:
- Carmen To  
Ofcom  
Riverside House  
2A Southwark Bridge Road  
London SE1 9HA
- A1.5 We welcome responses in formats other than print, for example an audio recording or a British Sign Language video. To respond in BSL:
- Send us a recording of you signing your response. This should be no longer than 5 minutes. Suitable file formats are DVDs, wmv or QuickTime files. Or
  - Upload a video of you signing your response directly to YouTube (or another hosting site) and send us the link.
- A1.6 We will publish a transcript of any audio or video responses we receive (unless your response is confidential)
- A1.7 We do not need a paper copy of your response as well as an electronic version. We will acknowledge receipt if your response is submitted via the online web form, but not otherwise.
- A1.8 You do not have to answer all the questions in the consultation if you do not have a view; a short response on just one point is fine. We also welcome joint responses.
- A1.9 It would be helpful if your response could include direct answers to the questions asked in the consultation document. The questions are listed at Annex 4. It would also help if you could explain why you hold your views, and what you think the effect of Ofcom's proposals would be.
- A1.10 If you want to discuss the issues and questions raised in this consultation, please contact Carmen To on 020 7981 3538, or by email to [improving.engagement@ofcom.org.uk](mailto:improving.engagement@ofcom.org.uk).



## Confidentiality

- A1.11 Consultations are more effective if we publish the responses before the consultation period closes. In particular, this can help people and organisations with limited resources or familiarity with the issues to respond in a more informed way. So, in the interests of transparency and good regulatory practice, and because we believe it is important that everyone who is interested in an issue can see other respondents' views, we usually publish all responses on our website, [www.ofcom.org.uk](http://www.ofcom.org.uk), as soon as we receive them.
- A1.12 If you think your response should be kept confidential, please specify which part(s) this applies to, and explain why. Please send any confidential sections as a separate annex. If you want your name, address, other contact details or job title to remain confidential, please provide them only in the cover sheet, so that we don't have to edit your response.
- A1.13 If someone asks us to keep part or all of a response confidential, we will treat this request seriously and try to respect it. But sometimes we will need to publish all responses, including those that are marked as confidential, in order to meet legal obligations.
- A1.14 Please also note that copyright and all other intellectual property in responses will be assumed to be licensed to Ofcom to use. Ofcom's intellectual property rights are explained further at <https://www.ofcom.org.uk/about-ofcom/website/terms-of-use>.

## Next steps

- A1.15 Following this consultation period, Ofcom plans to publish a statement by March 2019.
- A1.16 If you wish, you can register to receive mail updates alerting you to new Ofcom publications; for more details please see <https://www.ofcom.org.uk/about-ofcom/latest/email-updates>

## Ofcom's consultation processes

- A1.17 Ofcom aims to make responding to a consultation as easy as possible. For more information, please see our consultation principles in Annex 2.
- A1.18 If you have any comments or suggestions on how we manage our consultations, please email us at [consult@ofcom.org.uk](mailto:consult@ofcom.org.uk). We particularly welcome ideas on how Ofcom could more effectively seek the views of groups or individuals, such as small businesses and residential consumers, who are less likely to give their opinions through a formal consultation.
- A1.19 If you would like to discuss these issues, or Ofcom's consultation processes more generally, please contact:

Corporation Secretary  
Ofcom  
Riverside House  
2a Southwark Bridge Road  
London SE1 9HA  
Email: [corporationsecretary@ofcom.org.uk](mailto:corporationsecretary@ofcom.org.uk)

## A2. Ofcom's consultation principles

### Ofcom has seven principles that it follows for every public written consultation:

#### Before the consultation

A2.1 Wherever possible, we will hold informal talks with people and organisations before announcing a big consultation, to find out whether we are thinking along the right lines. If we do not have enough time to do this, we will hold an open meeting to explain our proposals, shortly after announcing the consultation.

#### During the consultation

A2.2 We will be clear about whom we are consulting, why, on what questions and for how long.

A2.3 We will make the consultation document as short and simple as possible, with a summary of no more than two pages. We will try to make it as easy as possible for people to give us a written response. If the consultation is complicated, we may provide a short Plain English / Cymraeg Clir guide, to help smaller organisations or individuals who would not otherwise be able to spare the time to share their views.

A2.4 We will consult for up to ten weeks, depending on the potential impact of our proposals.

A2.5 A person within Ofcom will be in charge of making sure we follow our own guidelines and aim to reach the largest possible number of people and organisations who may be interested in the outcome of our decisions. Ofcom's Consultation Champion is the main person to contact if you have views on the way we run our consultations.

A2.6 If we are not able to follow any of these seven principles, we will explain why.

#### After the consultation

A2.7 We think it is important that everyone who is interested in an issue can see other people's views, so we usually publish all the responses on our website as soon as we receive them. After the consultation we will make our decisions and publish a statement explaining what we are going to do, and why, showing how respondents' views helped to shape these decisions.

## A3. Consultation cover sheet

### BASIC DETAILS

Consultation title:

To (Ofcom contact):

Name of respondent:

Representing (self or organisation/s):

Address (if not received by email):

### CONFIDENTIALITY

Please tick below what part of your response you consider is confidential, giving your reasons why

Nothing

Name/contact details/job title

Whole response

Organisation

Part of the response

If there is no separate annex, which parts? \_\_\_\_\_

If you want part of your response, your name or your organisation not to be published, can Ofcom still publish a reference to the contents of your response (including, for any confidential parts, a general summary that does not disclose the specific information or enable you to be identified)?

### DECLARATION

I confirm that the correspondence supplied with this cover sheet is a formal consultation response that Ofcom can publish. However, in supplying this response, I understand that Ofcom may need to publish all responses, including those which are marked as confidential, in order to meet legal obligations. If I have sent my response by email, Ofcom can disregard any standard e-mail text about not disclosing email contents and attachments.

Ofcom seeks to publish responses on receipt. If your response is non-confidential (in whole or in part), and you would prefer us to publish your response only once the consultation has ended, please tick here.

Name

Signed (if hard copy)

## A4. Consultation questions

A4.1 This Annex lists the questions that we are consulting on.

**Question 1:** Do you agree with our assessment of harm relating to residential consumers and Small Businesses?

**Question 2:** Do you agree that providers should send both end-of-contract and out-of-contract notifications?

**Question 3:** Do you agree with our proposal that notifications should be sent to all residential and Small Business customers who take Public Electronic Communications Services?

**Question 4:** Do you agree with our proposals on the content of the end-of-contract notification?

**Question 5:** Do you agree with our proposals on the structure, method, timing and frequency of the end-of-contract notification?

**Question 6:** Do you agree with our proposals on the content of the out-of-contract notification?

**Question 7:** Do you agree with our proposals on the structure, method and frequency of the out-of-contract notification?

**Question 8:** Do you agree that our proposals are both effective and the minimum necessary to achieve our policy objectives?

**Question 9:** Do you agree with the impacts we identify, and the approach we take to quantify these impacts, in our assessment in Annex 6?

**Question 10:** Do you agree with our provisional assessment that the potential costs for providers are not disproportionate in order to achieve our policy objectives?

**Question 11:** Do you agree with our proposed implementation timescale for end-of-contract notifications and for the one-off notification to customers who are already outside of their minimum contract period?

**Question 12:** Do you have any comments on the draft condition set out in Annex 9 to this document?

**Please provide evidence in support of your views.**

## A5. Glossary and abbreviations

**Act:** The Communications Act 2003

**Billing system:** A software tool that manages the billing of a customer’s services.

**Bundle:** A combination of more than one service (e.g. broadband and landline, or pay TV and broadband) which is provided by a single communications provider.

**Customer relationship marketing (CRM) tool:** A software tool that allows marketing departments to see information relating to the customer’s proposition.

**Customer service agent (CSA) tool:** A software tool that allows call centre agents to review customer account information.

**Communications provider (or provider):** A person who provides an electronic communications network or provides an electronic communications service, as defined in the Communications Act 2003. The terms ‘communications provider’ and ‘provider’ are used interchangeably throughout this document.

**Dual play:** Landline and broadband services provided by a single communications provider.

**Early termination charge:** A charge that may be payable by a consumer for the termination of a contract before the end of any minimum contract period (or subsequent minimum contract period).

**General Condition (‘GC’):** A general condition imposed by Ofcom under section 45(2)(a) of the Act.

**In-contract** refers to customers who are within the minimum contract period for any service provided by the communications provider.

**Mbit/s:** Megabits per second (1 Megabit = 1 million bits). A measure of bandwidth in a digital system.

**Minimum contract period:** The fixed period of time over which the communications provider and a customer have entered into an agreement for communications services and for which an early termination charge may be payable by the customer if they cancel their contract during this period.

**Mobile:** A mobile telephony subscription, i.e. a service including the provision of a SIM, which enables a customer to make and receive mobile voice calls and SMS, and/or use data services through a mobile handset.

**Out-of-contract** refers to customers who are outside of the minimum contract period but are still paying for a service (e.g. broadband, mobile, landline) provided by the provider (e.g. via a rolling monthly contract).

**Pay TV:** A subscription-based television service, usually charged at a monthly fee, offering multichannel television channels beyond those available free-to-air. It can be delivered through cable, satellite, digital terrestrial and/or the internet (IPTV).

**Post-pay contract:** A type of contract whereby customers are billed for their use of the provider’s services on a monthly basis, based on either the terms of a contract or on the amount of services they have used.

**Public electronic communications service (PECS):** Any electronic communications service that is provided so as to be available for use by members of the public.

**Quad play:** Landline, broadband, pay TV and mobile provided by a single communications provider.

**SIM-only:** A contract between a mobile network provider and a customer whereby the customer is only paying for the monthly network service and not a handset.

**Small business customer:** A customer who carries on an undertaking for which no more than ten individuals work (whether as employees or volunteers or otherwise), but who is not himself a communications provider.

**SMEs:** Small and medium sized enterprises are businesses with 249 or fewer employees.

**Standalone:** Where customers take only a single service from a communications provider and not a bundled service. E.g. standalone mobile refers to where a customer only takes a mobile service from their communications provider.

**Standard broadband:** Broadband services that deliver download speeds of less than 30Mbit/s, typically over a copper telephone line.

**Superfast broadband:** Broadband services that deliver download speeds of 30Mbit/s or higher, typically over fibre-to-the cabinet connection or coaxial cable (on Virgin Media's network).

**Triple play:** landline, broadband and pay TV services provided by a single communications provider.

**Upgrade / Downgrade:** Where customers change the service(s) received from their communications provider, or the terms on which they do so, but do not switch to another provider.

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**ANNEX 13**

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BT's response to Ofcom's consultation document: *"The review of the market for standalone landline telephone services: provisional conclusions"*

19 May 2017

## Contents

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## 1. Executive Summary

1. Ofcom has positioned its standalone landline telephone services market review as necessary to address concerns that customers who buy telephone services in a standalone contract (who Ofcom indicates are primarily older or vulnerable) have not benefited from competition in the same way as those buying bundles.
2. Ignoring that the concerns it has identified (to the extent they exist) extend beyond BT<sup>1</sup>, Ofcom inappropriately proposes to address its concerns by re-introducing and imposing retrograde SMP regulation on BT alone, in particular by imposing a price cut to BT's line rental charge. Ofcom further seeks to stimulate competition for SFV customers by imposing on BT an SMP condition to trial and, if appropriate, deliver behavioural "*communication*" type measures.
3. BT takes its responsibilities to older or more vulnerable customers very seriously. This is demonstrated by: the tailored products we have developed for these customers (services unique to BT); the introduction of new products that particularly aid these customers; our efforts to encourage take up of broadband amongst this group; and our work with consumer organisations to better understand customer needs and how to reach them. We continue to develop and invest in initiatives to serve and increase value for these customers.
4. For the reasons set out in this response, it is not justifiable on evidential, legal or economic bases for Ofcom to impose SMP conditions on BT in the manner proposed. The theory of harm that Ofcom has identified (but which Ofcom has not substantiated) is not a market power issue, but instead a question around whether certain customer groups (those who are relatively less engaged) are benefitting as much from the highly competitive retail voice market as groups who are relatively more engaged. To the extent there is an issue of this nature, this is a market wide issue; it is not caused by the actions or behaviours of a specific operator exercising market power.
5. BT is committed to helping its customers identify the best deal whatever their circumstances or level of engagement. BT has frozen its line rental charges and continues to review its approach to pricing.<sup>2</sup> Initiatives such as Virgin Media's Talk Protected proposition targeted at SFV customers<sup>3</sup> and active

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<sup>1</sup> Ofcom has expressed concern about the trend "observable across all major providers of landline services – not just BT" [emphasis added] that retail line rental prices have increased in the last 3 years, whilst the underlying wholesale costs have decreased. Paragraph 1.1 of Ofcom's 'Provisional Conclusions Consultation'.

<sup>2</sup> In response to changes in the market, developing policy positions and changes to rules, for example the ASA's changes to rules on broadband advertising in October 2016. <https://www.asa.org.uk/news/changes-to-broadband-price-claims-in-ads-comes-into-force-today.html>

<sup>3</sup> In December 2016, Virgin Media introduced "Talk Protected" plan for customers who are over the age of 65 or have additional accessibility needs including hearing, sight, speech and mobility issues. For £17.99 per month rental this plan offers £5 off of other Virgin Phone plans, such as Talk More Anytime and Talk More International Anytime, and includes free evening and weekend calls to UK landlines and mobiles, free 0845 and 0870 numbers and directory enquires (118 180) and paper billing and caller display at no extra cost. <http://www.virginmedia.com/corporate/media-centre/press-releases/virgin-media-freezes-line-rental-for-elderly-and-disabled-landline-customers.html>

marketing by the Post Office of a low price landline only offer, demonstrate that the market is not in need of intervention to address engagement issues.

6. Market players are competing for this segment in an effective manner, and the partial “remedy” proposed by Ofcom on only one market player, in circumstances where the issues Ofcom have identified are market-wide, is inappropriate, unnecessary and may have unintended consequences in discouraging migration to bundles, and are contrary to switching and digital inclusion objectives.

#### **Ofcom’s approach to market definition is flawed**

7. BT does not agree that there are separate markets for SFV services, whether for access or calls; rather there is a wider market for voice services in which BT does not hold SMP.
8. Within this wider market there are pro-competitive explanations for the pricing structure which Ofcom is concerned about. The incremental broadband price has historically been the focus of competitive activity reflecting the significant uptake of bundles and the advantages of bundled pricing in expanding consumption, promoting competition between firms and delivering benefits to consumers. As Ofcom acknowledges, in the *“past decade the landscape for fixed line telecommunications in the United Kingdom has been transformed. Competition has brought new services, increased choice and delivered real benefits to consumers.”*<sup>4</sup>
9. Firms have therefore prioritised keeping the incremental broadband prices low in order to be able to compete effectively for customers of bundles (which, at 90%, is by far the largest customer segment) rather than using line rental reductions as a means of competing for voice-only customers (which are a much smaller and dwindling group). Competition for voice-only customers has focused, instead, on product innovation (e.g. the creation of fixed price products such as Home Phone Saver) and discounts from headline call plan prices.
10. These broader competitive dynamics, which Ofcom fails to properly assess, have delivered strong competition and good consumer outcomes including for the SFV customers that have (in vast numbers) chosen to switch. There has been a [X] decline in the SFV customer base over the past 4 years or so driven primarily by switching to bundles (which Ofcom accepts), driven by low incremental broadband prices, and this is likely to continue.<sup>5</sup> Those who have not switched have seen new products, greater value and supplier choice, including from entrants such as the Post Office.
11. In this context, Ofcom has not shown that the necessary conditions are met to define markets for specific customer groups; indeed the past and predicted future migration of SFV customer to bundles indicates that the boundaries of the markets which Ofcom has identified are not stable. Far from discouraging diversion (as one would expect of a firm with market power), bundled pricing structures have encouraged further take up of dual play broadband by customers, consistent with pro-competitive and migration objectives, and not the objective or effect of segmentation and exploitation of market power.

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<sup>4</sup> Paragraph 1.1 of Ofcom’s Provisional Conclusions Consultation.

<sup>5</sup> Paragraph 4.4–4.6 and A8.15 of Ofcom’s Provisional Conclusions Consultation.

12. Going forward, the ASA's intervention<sup>6</sup> (which prevents broadband providers from advertising the price of broadband and line rental separately) is likely to change these dynamics by reducing incentives to raise the line rental price. Firms may, therefore, consider line rental reduction as a further means of competing for voice-only customers alongside product innovation and discounts (although dual play providers may still balance this with promoting further uptake of bundles by keeping implicit broadband prices low).
13. Even if it were correct for Ofcom to find separate SFV retail markets, so-called 'split purchase' customers clearly do not form part of that market and should not be subject to the same proposed remedies. Ofcom has not demonstrated that these customers are acting irrationally or that they are otherwise less engaged than other dual play customers, with whom they share very similar characteristics.
14. Split purchasers show higher levels of engagement, have historically switched in large numbers to bundles and are highly attractive to the larger CPs who can use a range of channels to reach these customers (as they do for customers across the dual play base). Split purchase customers should be viewed as dual play customers (albeit purchasing dual play products on an unbundled basis).
15. The three criteria test is not met; Ofcom has not demonstrated that the markets it identifies are susceptible to *ex-ante* regulation. Ofcom has not sufficiently discharged its legal burdens to re-impose retail level SMP regulation on BT. This is a retrograde and disproportionate step, which unduly discriminates against BT, which will not further the interests of citizens and which is out of line with the policy direction towards removing retail regulation that the European Commission is taking.

**BT does not hold significant market power**

16. BT faces significant competitive pressure in a rapidly changing environment. Our Consumer business is facing challenging headwinds, with falling volumes, calls usage and competition in the SFV segment from entities with a strong brand presence and channel advantages such as the Post Office (which targets BT's line rental customers with low priced offers) and from mobile substitution.
17. [REDACTED]<sup>7</sup>
18. BT is not, therefore, able to set the terms and conditions of sales for SFV services without facing competitive constraints from other providers, as suggested by Ofcom. Relevant competition parameters in the SFV segment encompass product choice, quality of service and value. We have responded to competition by investing to improve our products and customer service as well as introducing attractive offers, for example Home Phone Saver, which continue to perform well as we improve them.
19. [REDACTED]. This [REDACTED] as well as the [REDACTED], indicates a higher degree of engagement than Ofcom has found.
20. There is no material difference between split purchasers and dual play customers in their propensity to switch and levels of engagement more generally, and therefore no indication of an issue with customer engagement for this group. Split purchasers are also generally younger and more affluent, reflecting the demographics of BT's dual-play customers.

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<sup>6</sup> See section 1, paragraph 5 of this Response.

<sup>7</sup> A8.17 of Ofcom' Provisional Conclusions Consultation

21. Ofcom’s survey evidence shows that SFV customers indicate very high levels of satisfaction. To highlight loyalty to the BT brand as a facet of market power is inappropriate in this context and Ofcom should not penalise BT for successfully building brand value or for being trusted where this is attributable to high levels of customer satisfaction with the service provided.<sup>8</sup>
22. [§<]. Margins have also narrowed as our cost to serve the base have increased reflecting the additional value that we have offered (i.e. BT Call Protect, fixing faults at least 24 hours faster by upgrading to Openreach’s Care Level 2 and bringing back calls to the UK<sup>9</sup>). In any event measuring profit in a narrow market segment is not meaningful given the broader competitive dynamics described above; overall margins in the voice market reflect these competitive dynamics and are cited by Ofcom as a competitive benchmark.
23. In short, a quickly declining SFV base of customers is increasingly served by options to take broadband and other ways to save.

### Remedies

24. No SMP conditions are justified or necessary on BT; Ofcom has not adequately supported the need for SMP regulation either legally or substantively and its proposed intervention is not targeted at where action is needed.
25. In particular, there is no case for intervention in relation to split purchasers in the absence of any compelling evidence of either competition or consumer protection issues. Ofcom’s proposed remedies for this group are not only inappropriate and unnecessary but would be ineffective because they do not also address the charges for standalone broadband, in relation to which BT only has a small [§<] share.
26. For voice-only customers, Ofcom has underestimated the degree of engagement that these customers currently exhibit. If engagement is assessed correctly and future trends are properly taken into account, Ofcom’s proposed remedies are clearly disproportionate.
27. Ofcom’s proposed conditions could have serious and unintended consequences for voice only customers, for competition and for digital inclusion. For example, the proposed price reduction will make competition more difficult, even when coupled with behavioural remedies, and likely hinder the achievement of the UK’s digital inclusion objectives.
28. If Ofcom continues to seek to impose regulation in line with its provisional conclusions these adverse consequences must be minimised and the remedies implemented limited to those required to objectively address the problem they are seeking to address. More specifically, remedies should: (i) be limited to proportionate, specific and transparent behavioural “communication” remedies; and alternatively (ii) keep any price cut to a minimum, to provide maximum room for competition.
29. [§<].

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<sup>8</sup> This is especially true given Ofcom’s wider concerns about the low levels of trust in the industry that it perceives. Delivering for consumers and citizens, speech, 12 April 2017. <https://www.ofcom.org.uk/about-ofcom/latest/media/speeches/2017/delivering-consumers-citizens-sharon-white>

<sup>9</sup> [§<].



## 2. Context

### A. The market context for Ofcom's review

30. A proper consideration of the wider landscape in which standalone fixed voice services are provided is essential to understanding the SFV segment, [38] and why, therefore, this is not a segment in relation to which SMP regulation is appropriate or proportionate on a forward looking basis having regard to Ofcom's duties.

***The UK fixed telecommunications landscape is highly competitive and dynamic and delivers excellent consumer outcomes.***

31. Ofcom highlights that the fixed telecommunications market landscape has transformed in recent years and that vigorous competition has led to new services, increased choice and has delivered a range of benefits to customers.<sup>10</sup> Demand for fixed access lines is increasingly driven by demand for fixed broadband, which has made possible a vast choice of other means of communications that are of huge benefit to consumers. This trend is set to continue in the future.
32. Consumers have a wide choice of suppliers for their fixed line telecommunications needs (whether in a bundle or on a standalone basis) including BT, Sky, Virgin Media, TalkTalk, the Post Office, SSE, and Direct Save Telecom. This competition has been so effective that BT has one of the lowest retail market shares of any ex-incumbent operator in Europe. BT lines are currently at a share of 37% of total UK lines.<sup>11</sup>
33. LLU-based providers such as Sky and TalkTalk have been particularly successful in winning market share from BT, and this form of competition now accounts for 36%<sup>12</sup> of all Openreach access lines (see Chart 1). Ofcom encouraged this type of competition in order that customers would benefit from investment and innovation by competitors to BT who offer genuine differentiation.

<sup>10</sup> Paragraph 1.1 of Ofcom's Provisional Conclusions Consultation.

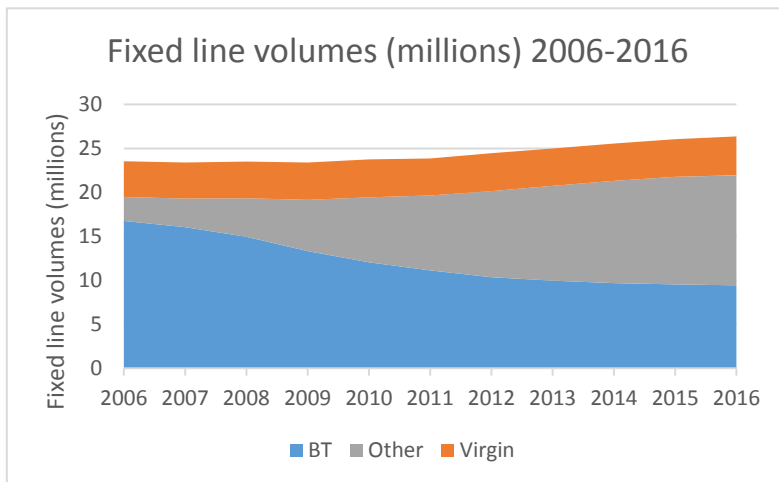
<sup>11</sup> [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0014/101408/telecoms-data-update-q4-2016.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0014/101408/telecoms-data-update-q4-2016.pdf) Table 2, page 5 – data excludes EE.

<sup>12</sup> Openreach Key Performance Indicators Q3 2016/17.

<http://btplc.com/Sharesandperformance/Quarterlyresults/2016-2017/Q3/Downloads/KPIs/q317KPIs.pdf>

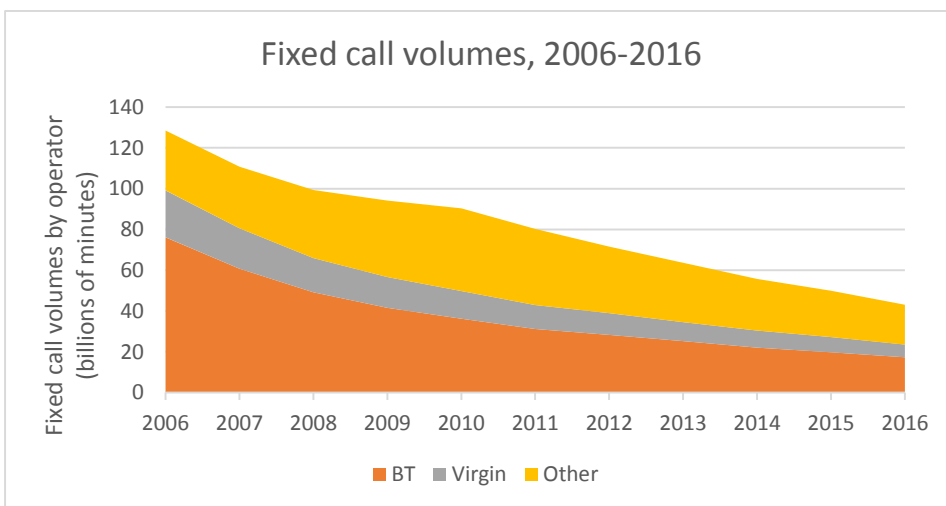


**Chart 1 – Increasing line competition since 2006<sup>13</sup>**



34. Demand for fixed line calls has also declined steeply, as Ofcom has recognised and as shown in Chart 2 below. In parallel, there has been continued growth in mobile calls (as to which see Chart 3 below) and increasing use of internet-based voice services, particularly ‘over-the-top’ services (such as WhatsApp; Skype; Apple’s Facetime; and Google Talk<sup>14</sup>).

**Chart 2 – Decline in fixed call volumes since 2006 (by provider)<sup>15</sup>**



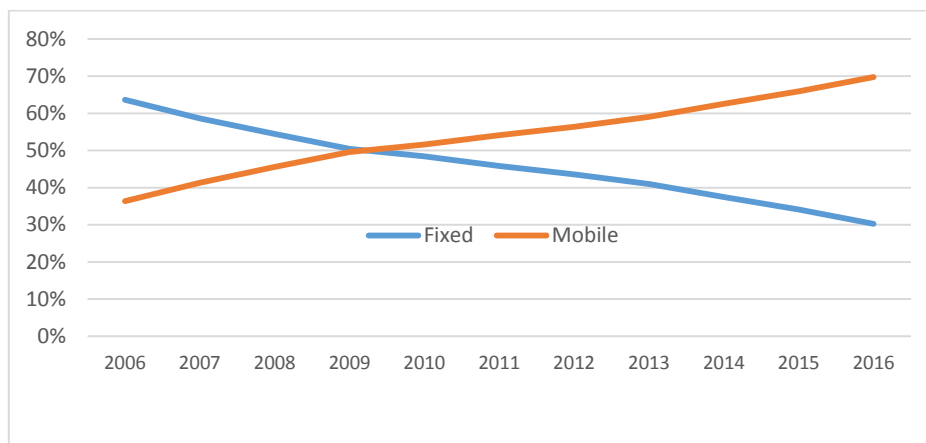
<sup>13</sup> Source: Ofcom data telecoms updates: <https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates>

<sup>14</sup> See for example Figure 4.37 of Ofcom’s 2016 Communications Market Report, 4 August 2016: [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0026/26648/uk\\_telecoms.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0026/26648/uk_telecoms.pdf)

<sup>15</sup> Source: Ofcom data telecoms updates: <https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates>

35. The trend of migration of calls from fixed line to mobile has continued to grow in the last decade.

**Chart 3 – Continuing migration of calls from fixed line to mobile since 2006<sup>16</sup>**



36. Put simply, the world of telecommunications is dynamic and rapidly changing and SFV customers are not exempted from many of these changes. As discussed further below, SFV customers have switched to bundles in droves. Equally, the vast majority (70%<sup>17</sup>) of SFV customers also have mobile phones and Ofcom accepts that *“there is scope for these customers to make more calls on their mobile phones instead of their fixed lines”*.<sup>18, 19</sup>

***There has been an increase in competition for bundles, which has delivered real consumer benefits, and a focus on competitive pricing of broadband***

37. Ofcom highlights the migration of customers to bundles and that people who have bundled are getting excellent value for their money in light of increased average speeds<sup>20</sup>, increased data packages and additional on-demand television and content services for little or no extra cost.<sup>21</sup>
38. In line with these market developments and competitive pressures, BT has transformed in the last decade. It has developed its propositions to provide voice services alongside access to high speed fixed broadband

<sup>16</sup> Source: Ofcom data telecoms updates: <https://www.ofcom.org.uk/research-and-data/telecoms-research/data-updates>

<sup>17</sup> Footnote 9 and paragraph 3.17 of Ofcom’s Provisional Conclusions Consultation – see also paragraph 129 of this Response which sets out, of these, that 95% of split purchase customers have access to mobile phones as compared to 58% for voice-only customers.

<sup>18</sup> Paragraph 3.17 of Ofcom’s Provisional Conclusions Consultation.

<sup>19</sup> Sections 4 and 5 of this Response set out the implications of these changes for Ofcom’s analysis of the relevant market and BT’s market power.

<sup>20</sup> As Ofcom noted in 2015: *Ten years ago fixed broadband services were widely available, but a service only had to deliver a speed of 128 Kbit/s to qualify as ‘broadband’. Now, superfast broadband (capable of delivering speeds of 30Mbit/s) is available to 83% of UK premises. This increase is primarily due to the Government’s BDUK investment programme, building on the commercial rollouts of Openreach’s fibre-to-the-cabinet (FTTC) network as well as Virgin Media’s DOCSIS 3.0 technology. Superfast availability is expected to reach 95% by 2017.* Strategic Review of Digital Communications, Discussion document, Ofcom 16 July 2015 paragraph 4.5.

<sup>21</sup> Paragraph 1.23 of Ofcom’s Provisional Conclusions Consultation.

connections, as well as moving into the provision of quad play services. BT has invested in migrating customers to fibre speeds, improved home hubs, developed BT's YouView platform, and built a pay TV content business and launched BT Mobile.

39. 9 out of 10 customers<sup>22</sup> now purchase fixed voice as part of a bundle and this has led all providers of bundles to devise pricing strategies which reflect bundled purchasing. In particular, the incremental broadband price has (historically) been the focus of competitive offers and price competition has been fierce. As a result, the incremental price of broadband has fallen significantly<sup>23</sup> and packages are now available that are close to or below landline-only packages – e.g. Sky's ADSL broadband for free for a year.<sup>24</sup><sup>25</sup> The Oxera report explains how bundled pricing strategies such as this can expand consumption and promote competition between firms as well as delivering benefits for customers.<sup>26</sup>
40. Line rental price increases must be understood in this context. As the market has evolved to almost ubiquitous take up of bundles, incremental broadband prices have been forced down by competitive pressure. All providers have chosen to offset this, to some degree, through line rental price increases. Observed market outcomes are attributable, therefore, to pro-competitive bundled pricing strategies adopted by all CPs, whereby broadband prices have been marketed at a very low price.
41. A low and decreasing incremental broadband price has been effective in attracting SFV customers into the segment. For voice-only customers the decision to take up broadband involves a price quality trade off which, as explained by Ofcom “*requires customers to derive a utility from the higher quality or additional features sufficient to compensate them for the higher price*”.<sup>27</sup> A decreasing incremental price means that these customers have been more easily persuaded to take dual play even when their expected valuations for broadband are very low (even at zero).<sup>28</sup>
42. The importance of low incremental broadband prices should not be underestimated for the voice-only group who are late adopters and who may not initially perceive the wider benefits of being online, but once convinced to try, by very low (or zero) additional price offers, are likely to benefit enormously. Put simply, there are significant digital inclusion benefits from encouraging SFV customers to take up broadband (as outlined in section 3 below).<sup>29</sup>

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<sup>22</sup> The Oxera Report, footnote 4

<sup>23</sup> Ofcom states, “[c]omparing the price of SFV services against promotional prices for ADSL bundles, the average incremental cost of upgrading from SFV to a promotional ADSL dual-play package has decreased, on average, by 53% (£5.30)”. Paragraph 3.34 of Ofcom’s Provisional Conclusions Consultation.

<sup>24</sup> Paragraph 3.37 of Ofcom’s Provisional Conclusions Consultation.

<sup>25</sup> Sky has offered free broadband for 12 months to customers taking up a pay TV package with Sky Sports. <http://broadbandinternetuk.com/blog/2233/sky-comnewseason-free-broadband-with-sky-sports>

<sup>26</sup> The Oxera report, section 1.1

<sup>27</sup> Paragraph 3.36.1 of Ofcom’s Provisional Conclusions Consultation.

<sup>28</sup> Ofcom relies on research findings and the slowing in the decline of the SFV customer base to argue that price is not a driving factor in switching and that customers do not respond in large numbers to specific dual play offers (paragraph 3.37). Actual market outcomes suggest that the opposite is true: the relative price of a service with and without broadband has driven the take up of broadband by voice-only customers, and BT (and other dual providers) have priced accordingly.

<sup>29</sup> [8<]

***The SFV market segment is declining rapidly***

43. SFV customers have switched to bundles in large numbers and have therefore shared in these benefits. As Ofcom acknowledges: “*The number of SFV access lines, i.e. bought outside a bundle, is in steady long-term decline. This is primarily driven by customers who upgrade to bundles communication services (e.g. dual-play).*”<sup>30</sup> [Emphasis added]
44. [redacted]<sup>31 32</sup>
45. [redacted]
- a. [redacted]
- b. [redacted]

**Chart 4 – [redacted]<sup>33</sup>**

[redacted]

46. Ofcom undertakes no analysis of the likelihood and rate of future migration by remaining SFV customers. Our analysis suggests that switching to bundles will continue, particularly in light of our highly competitive offers and those of our competitors, our targeted products for vulnerable customers (e.g. BT Basic) and digital inclusion initiatives. The SFV customer base will also decline substantially on the basis of remaining life expectancy.<sup>34</sup>
47. As shown in Table 1 below, [redacted]<sup>35</sup>. In other words, the customers about which Ofcom has expressed its main concerns will increasingly represent a very small proportion of the whole market, whilst virtually all of BT’s consumer base will derive benefit and value from fixed lines via broadband.
48. Ofcom has provided no compelling evidence that the remaining SFV customers are materially different in their propensity to switch. Ofcom highlights survey research indicating that 68% of voice-only respondents said that they did not take a bundle with broadband because they did not use broadband.<sup>36</sup> Although Ofcom attributes this finding to the 2015 Jigsaw residential survey (wave 1), the response, in this survey, to the question “Which of these statements best describes the reason you do not take up a bundle of services from your landline supplier that includes broadband?” revealed that only 34% do not

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<sup>30</sup> Paragraph 4.5 of Ofcom’s Provisional Conclusions Consultation

<sup>31</sup> Ofcom state that “the rate of decline has slowed less for BT (from 25% in the year up to Q1 2014 to 17% in the year up to Q3 2016) than for other CPs...BT’s rate of decline is, on average, 11 percentage points faster than other CPs”, paragraph A8.17 of Ofcom’s Provisional Conclusions Consultation.

<sup>32</sup> Figure A5.11 of Ofcom’s Provisional Conclusions Consultation

<sup>33</sup> [redacted].

<sup>34</sup> Oxera also reach the conclusion that the rate of decline will not decrease substantially. The Oxera report, section 1.3.

<sup>35</sup> [redacted]

<sup>36</sup> Paragraph 3.36.2 of Ofcom’s Provisional Conclusions Consultation.

use broadband, which is much lower than the figure cited by Ofcom and similar to the proportion mentioning price as an issue (26%) suggesting a high degree of price sensitivity.<sup>37</sup>

49. Equally, in 2011, [38] of customers did not intend to get broadband or were not sure.<sup>38</sup> Now, BT Consumer has only circa [38] of customers who do not have broadband.<sup>39</sup> This shows that voice-only customers have changed their minds about their intentions to take-up broadband. There is no “end point” where this effect stops, even if there is some slowing in the rate of migration before broadband becomes almost universal.

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<sup>37</sup> 2015 Jigsaw residential survey (wave 1). Question FX04C, Table 111.

<sup>38</sup> Ofcom Communications Market Review, 2015, Figure 5.25.

<sup>39</sup> The percentage will be lower still for other suppliers who do not offer a “voice-only” line.

**Table 1 – [REDACTED]**<sup>40</sup>

[REDACTED]

50. The evidence above that the SFV customer base is small and declining raises questions about the duration of the alleged issues raised by Ofcom as well as the proportionality of any proposed intervention.

***Consumers currently remaining in the SFV segment (and the small numbers going forward) are catered for***

51. In addition to BT, there are a number of providers of lines and calls services in the UK (excluding Hull), including, Sky, Fuel, SSE, Italk, Utility Warehouse, Zen, The Phone Co-Op, Sparta Telecom, Pop Telecom and True Telecom.<sup>41</sup> BT has sought to ensure that SFV customers get good value for money. We've developed specific products and offers which have provided important support to customers<sup>42</sup>, in particular, Home Phone Saver<sup>43</sup>, significant discounts on call plans and BT Basic. Other providers, namely Virgin Media and the Post Office, have also developed specific products for this segment (as described in Section 6 of this Response).
52. In focussing almost exclusively on price competition<sup>44</sup>, Ofcom has ignored the fact that competition takes place on a range of parameters including value for money, choice and innovation. For example, BT has invested [REDACTED] in adding value to our core product and surrounding experience for our customers [REDACTED]. BT has brought calls back to the UK and Ireland currently 86% of our calls are answered in the UK and Ireland, and we're on track to meet our target of 90% of our calls answered onshore by the end of the spring 2017; we now fix faults 24 hours faster than before (3 July 2016) by upgrading our customers to Openreach's Care Level 2; we have also created a free Nuisance Call diversion application with "Junk Voicemail", called BT Call Protect<sup>45</sup>. In addition, all of our line customers get free weekend calls to UK Landlines and 0845/0870 numbers.
53. Our voice-only customers do exercise choice between the products and features that they take from us. A high proportion (87%), for example, have made a change to their promotion in the last 2 years,

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<sup>40</sup> Excludes split supply customers, and as at November 2016.

<sup>41</sup> As at November 2016

<sup>42</sup> Section 3 of this Response sets out more detail the measures that BT has taken to provide for these customers.

<sup>43</sup> As Ofcom notes in the Provisional Conclusions Consultation, HPS is substantially cheaper than standard prices and this product has been actively marketed by BT. Regarding Ofcom's comment that HPS is not prominent on BT's Consumer website, it must be recognised that this service is not designed for customers who have broadband access at home.

<sup>44</sup> And, in BT's view failing to even properly consider price competition – given Ofcom's failure to give proper weight and assessment to the broader context in which this occurs and, indeed, failure to properly consider that call prices are competitive [REDACTED].

<sup>45</sup> More information can be found here:

[http://www.productsandservices.bt.com/products/phone/call-protect/?s\\_cid=con\\_ppc\\_maxus\\_vidZ60\\_T1&vendorid=Z60&qclid=CLrD-dK51tMCFYgp0wodbjAMvw&qclsrc=aw.ds&dclid=CIGFpNO51tMCFSON7QodurOF-w](http://www.productsandservices.bt.com/products/phone/call-protect/?s_cid=con_ppc_maxus_vidZ60_T1&vendorid=Z60&qclid=CLrD-dK51tMCFYgp0wodbjAMvw&qclsrc=aw.ds&dclid=CIGFpNO51tMCFSON7QodurOF-w)

including changes to calling plans and calling features.<sup>46</sup> They also churn to other providers in particular the Post Office which has targeted our voice-only base.

54. Survey evidence indicates high levels of satisfaction amongst SFV customers indicating that our initiatives are delivering what SFV customers want.<sup>47</sup>

55. More generally, digital inclusion<sup>48</sup> is an important societal objective, which should not be forgotten in the context of this customer group. As set out in the Government’s digital inclusion strategy in 2014:

*“However, to make sure the web is truly for everyone, we need to provide more than just access. We need to equip the whole country with the skills, motivation and trust to go online, be digitally capable and to make the most of the internet. There is a lot of great work going on across the public, private and voluntary sectors to help people and organisations go online, but digital exclusion remains a big issue. Maintaining momentum is not enough. We need to bring together and scale up our efforts, more than ever before. No single organisation can tackle this alone and only strong partnership across all sectors will succeed.”<sup>49</sup>*

56. BT firmly agrees with the importance of digital inclusion, and with the sentiment above that no organisation can tackle this issue alone. We do, however, seek to play our part. BT has put in place a number of schemes and measures for our customers to promote the benefits of being online and to assist customers once they have made that transition (see section 3 below). BT continues to believe that voice-only customers can and will continue to take up broadband in order to fully enjoy the benefits of digital inclusion [3<].

#### ***The voice market will continue to transform in the future***

57. New ASA rules now require CPs to advertise the price for line rental and incremental broadband as a single overall price<sup>50</sup>. Ofcom itself acknowledges that the move away from separating dual play prices into separate line rental and broadband charges will lead to *“less pressure on CPs to increase line rental prices*

<sup>46</sup> In this regard we note that Ofcom’s survey data does not fully take this fact into account: A6.2 of Ofcom’s Provisional Conclusions Consultation: *“We note that some customers may engage without switching provider, such as by changing their call plan, and this may not be captured in our survey data.”*

<sup>47</sup> Paragraph 4.9 of Ofcom’s Provisional Conclusions Consultation *“Survey evidence also suggests that SFV access customers show a high level of satisfaction with their landline provider. Figure A8.62 in Annex 8 describes the reported levels of satisfaction with the overall landline service provided. It suggests that voice-only customers are generally more satisfied, the majority of voice-only and split-supplier customers reported being very satisfied (74% and 58% respectively, compared to 54% for dual-play).”*

<sup>48</sup> *“Digital inclusion is often defined in terms of:*

- *Digital skills – being able to use computers and the internet. This is important, but a lack of digital skills is not necessarily the only, or the biggest, barrier people face.*
- *Connectivity – and access to the internet. People need the right infrastructure but that is only the start.*
- *Accessibility – services should be designed to meet all users’ needs, including those dependent on assistive technology to access digital services. Accessibility is a barrier for many people, but digital inclusion is broader.”*

<sup>49</sup> <https://www.gov.uk/government/publications/government-digital-inclusion-strategy/government-digital-inclusion-strategy>

<sup>50</sup> <https://www.asa.org.uk/news/changes-to-broadband-price-claims-in-ads-comes-into-force-today.html>

*for SFV services to match increases in line rental prices for dual play tariffs.*<sup>51</sup> Ofcom has failed, however, to fully take into account the implications of this new requirement for how CPs price overall to win customers and the pricing of SFV services in particular.

58. Following the ASA rule changes, line rental pricing cannot be de-coupled from the incremental broadband price; if line rental prices are reduced, this does not jeopardise competitiveness by requiring an offsetting increase in the incremental broadband prices (which was formerly the focus of competitive activity). Firms may, therefore, consider line rental reductions as a further means of competing for voice-only customers alongside product innovation and discounts (although dual play providers may still balance this with promoting further uptake of bundles by keeping implicit broadband prices low). See section 4 of this response and Oxera report at Annex 2 which considers that these obligations alone may address the concerns that Ofcom has raised.
59. The market will continue to transform in the future as services move from the PSTN to All IP (IP voice) and the current copper network moves increasingly to fibre based services. Ofcom considers that any such transformation will be outside of the review period (until 2020/21). However, BT is [X] aiming for all customers to be All IP by 2025. Moving from the PSTN to All IP is an important stepping stone towards a digital future and provides an opportunity for the UK to drive towards universal online participation. [X].

## **B. Ofcom’s proposed regulation does not meet the relevant legal tests and is in breach of Ofcom’s legal duties**

### ***Legal framework – Ofcom’s powers to set SMP conditions***

60. Ofcom may set SMP conditions pursuant to section 45(2)(iv) of the Communications Act 2003 (the “Act”), which implements the EU Common Regulatory Framework (“CRF”). Sections 78 to 86 of the Act set out the procedure that Ofcom must follow and Section 91 of the Act provides Ofcom with the power to set retail level SMP conditions<sup>52</sup>.
61. In setting an SMP condition, Ofcom must meet the legal test set out in section 47(2) as well as its general duties<sup>53</sup>. Section 47(2) provides that Ofcom may only set or modify an SMP condition if it is:
- (a) *objectively justifiable in relation to the networks, services, facilities, apparatus or directories to which it relates;*
  - (b) *not such as to discriminate unduly against particular persons or against a particular description of persons;*
  - (c) *proportionate to what the condition or modification is intended to achieve; and*
  - (d) *in relation to what it is intended to achieve, transparent.* [Emphasis added]
62. Section 3(1) of the Act provides that:

*“It shall be the principal duty of OFCOM, in carrying out their functions—*

<sup>51</sup> Paragraph 4.65 of Ofcom’s Provisional Conclusions Consultation.

<sup>52</sup> In particular, section 91 provides that Ofcom may only impose retail level remedies where it is not able to by the setting of access conditions or conditions authorised or required by ss87 –90 of the Act to perform its section 4 duties to fulfil its Community obligations.

<sup>53</sup> Contained within sections 3 to 9 of the Act.



- (a) *to further the interests of citizens in relation to communications matters; and*
- (b) *to further the interests of consumers in relevant markets, where appropriate by promoting competition.”*

63. Section 3(3) of the Act provides that:

- “(3) In performing their duties under subsection (1), OFCOM must have regard, in all cases, to—*
- (a) the principles under which regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed; and*
  - (b) any other principles appearing to OFCOM to represent the best regulatory practice.”*

64. Section 6(1) of the Act provides that:

- “(1) OFCOM must keep the carrying out of their functions under review with a view to securing that regulation by OFCOM does not involve—*
- (a) the imposition of burdens which are unnecessary; or*
  - (b) the maintenance of burdens which have become unnecessary.”* [Emphasis added]

65. Ofcom’s regulatory principles<sup>54</sup> provide, inter alia, that:

*“Ofcom will strive to ensure its interventions will be evidence-based, proportionate, consistent, accountable and transparent in both deliberation and outcome.”*

And that:

*“Ofcom will consult widely with all relevant stakeholders and assess the impact of regulatory action before imposing regulation upon a market”*

***The imposition of retail level SMP regulation is a retrograde step, for which there is no sound economic or legal basis in this case***

66. The imposition of retail level regulation should be a measure of last resort:

*“The aim is progressively to reduce ex-ante sector specific rules as competition in the markets develops and, ultimately, for electronic communications to be governed by competition law only. [...] it is essential that ex ante regulatory obligations only be imposed where there is no effective and sustainable competition”* [Recital 5, Better Regulation Directive<sup>55</sup>]

67. Ofcom has not adequately evidenced that BT has SMP in a relevant market. Ofcom’s market definition and analysis of market power is flawed and cannot be relied upon. Ofcom has utilised market definition as an end not the means, has ignored relevant considerations and, its conclusions are insufficiently evidence based (for example Ofcom has failed to consider the importance of historic levels of switching by SFV customers to bundled products, the importance of the competitive and efficient rationale for CPs pricing structures<sup>56</sup>, and, has conducted no proper analysis of the likely rate or future migration of SFV

<sup>54</sup> <https://www.ofcom.org.uk/about-ofcom/what-is-ofcom>.

<sup>55</sup> Directive 2009/140/EC.

<sup>56</sup> See paragraphs 37 – 42 of this Response and The Oxera Report section 1

customers). A finding of SMP would be disproportionate and unjustified. Sections 4 and 5 of this response set out in detail why this is the case.

68. BT has previously expressed its genuine concern that Ofcom had pre-determined the outcome of this consultation process. Amongst other things, Ofcom’s public positioning together with the paucity of analysis of relevant market dynamics in its provisional conclusions consultation have led BT to this conclusion.<sup>57</sup>
69. Contrary to sections 3(1), 3(3), 6(1) and 47(2) Ofcom’s proposed intervention is not targeted at where action is needed and is disproportionate:
- a. The market for voice services is a well-functioning and highly competitive one. Intervention is not required at all and no SMP finding should be made<sup>58</sup>.
  - b. Ofcom seeks to rely on s.3(4)(i)<sup>59</sup> which states that it may have regard to *“the needs of persons with disabilities, of the elderly and of those on low incomes”*. Ofcom notes in this case the higher age demographic of many voice-only consumers. However:
    - i. Consideration of this factor must be appropriately balanced with furthering the interests of citizens (pursuant to s.3(1)(a)) in other ways for example by promoting digital inclusion.<sup>60</sup>
    - ii. Section 3(4)(i) provides no justification for intervention in relation to split purchase customers who are almost identical to dual play customers from a demographic perspective<sup>61</sup>.
  - c. Moreover, the voice-only base is *“de minimis”* in terms of volume and declining. [X]<sup>62</sup>. Regulation is disproportionate and unwarranted in these circumstances and would involve the imposition of an unnecessary burden contrary to s. 6(1). In this regard, we note that Ofcom has previously taken a decision to deregulate markets with declining volumes due to significant migration of customers to competitive markets (for example the retail market for very low bandwidth leased lines<sup>63</sup>). It would

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<sup>57</sup> For example: On the date of publication of Ofcom’s provisional conclusions consultation, Ofcom publicised the findings of this consultation (BT having SMP and a price cut of at least £5) as a foregone conclusion. In an interview with Sharon White on the BBC Radio 4 today programme on 28 February 2017, Sharon White stated as follows [emphasis added]:

*“So if you’re a BT customer and you just take a landline from BT, we intend to force BT to cut your bill by at least £5 a month...”*

*“The history that we’re dealing with today is that BT is dominant in this market for only-landline customers, people who have been with BT for a very, very long period of time. It is a very discreet, difficult problem for many of the most vulnerable, and we believe that BT needs to act and that is why we’re cutting prices today.”*

*“Well, what is interesting, today, these are proposals on which we’re consulting, and we have said that we will cut monthly bills by at least £5, but it may be more, and we’re keen to get the views of the public and of industry over the next few months and then we will make our final decision on the actual price cut later this year.”*

<sup>58</sup> Insofar as Ofcom persists in continuing to consider that the relevant marks are narrower, this analysis also fails (for the reasons set out in section 4 of this Response and The Oxera Report at Annex 2.

<sup>59</sup> Paragraph 9.35 of Ofcom’s Provisional Conclusions Consultation.

<sup>60</sup> See also for example, s3(4)(e) which provides that Ofcom may also have regard to *“the desirability of encouraging the availability and use of high speed data transfer services throughout the United Kingdom”* [Emphasis added]

<sup>61</sup> See section 4 of this Response.

<sup>62</sup> [X]

<sup>63</sup> See [https://www.ofcom.org.uk/\\_data/assets/pdf\\_file/0018/63225/final-statement.pdf](https://www.ofcom.org.uk/_data/assets/pdf_file/0018/63225/final-statement.pdf)

therefore be inconsistent and contrary to the bias against intervention for Ofcom to re-introduce retail level regulation in this case where declining volumes and migration patterns are similar and where BT has taken steps to protect voice-only customers who have not migrated.

70. Ofcom's approach, and resultant provisional conclusions, are in breach of Ofcom's s.47(2) duty not to unduly discriminate. Despite identifying a market-wide issue (namely whether certain customer segments are benefitting from competition to the same extent as others, or differences in the level of customer engagement by certain customer segments)<sup>64</sup>, the approach Ofcom has taken to address its alleged concerns is an SMP one which it directs solely at BT. Ofcom then reaches the circular conclusion that because BT is the only CP that it considers has SMP it is not unduly discriminatory to seek to impose the conditions proposed upon it<sup>65</sup>. However:
- a. Ofcom does not consider whether another approach may have been more appropriate to address its concerns (for example a market investigation reference pursuant to the Enterprise Act 2002). In contrast, consumer engagement issues in other sectors have been addressed using a market-wide approach rather than seeking to impose regulation on one market player (for example the recent CMA energy market investigation<sup>66</sup> referred by Ofgem in 2014).
  - b. Even utilising regulation based on a finding of SMP (which has not been properly substantiated), Ofcom's approach reduces its flexibility in choice of remedy<sup>67</sup>. In particular, to the extent that there is consumer harm arising from market-wide features, Ofcom's remedies will not clearly and directly address the needs of the SFV customers of other providers. This is particularly the case for split purchasers where Ofcom's proposals do not address the cost of standalone broadband supplied by other providers even though this is part of the source of Ofcom's concerns. Put simply, even if Ofcom had substantiated its concern (which it has not), it is applying the wrong remedies to the wrong firm.
  - c. Similarly, Ofcom does not propose to regulate KCom, instead preferring to assume that KCom will follow independently any regulation imposed on BT:

*"We note that KCOM has consistently set matching or lower prices than BT for fixed voice line rental and calls packages. We might therefore expect the impact of any regulatory intervention in the rest of the UK to flow through to retail conditions in Hull to the benefit of its consumers. If, subsequent to this review, we had evidence of significant detriment to consumers in the Hull area, we would consider what further action is required, including the possibility of a separate review for the Hull area."<sup>68</sup>*

Ofcom provides no evidence to support these assumptions. Ofcom's pricing analysis included at Annex 8 of the Provisional Conclusions Consultation Document does not even include KCom and there is no evidenced rationale provided as to why KCom may follow any such intervention.

<sup>64</sup> See, for example, paragraph 1.11 of Ofcom's Provisional Conclusions Consultation.

<sup>65</sup> See paragraphs 9.38 and 9.39 of Ofcom's Provisional Conclusions Consultation.

<sup>66</sup> <https://assets.publishing.service.gov.uk/media/5773de34e5274a0da3000113/final-report-energy-market-investigation.pdf>

<sup>67</sup> See section 6 of this Response.

<sup>68</sup> Paragraph 2.17 of Ofcom's Provisional Conclusions Consultation.

***Ofcom has not supported its divergence from the European Commission which considers that the power of imposition of ex ante regulatory controls based on SMP in retail markets should be repealed; the three criteria test is not met.***

71. In carrying out a market review, Ofcom is required to take due account of the European Commission’s Recommendation on relevant product and service markets (“the 2014 EC Recommendation”) and its SMP Guidelines. Ofcom must demonstrate that the three cumulative conditions of the “three criteria test” are met.
72. Ofcom’s provisional conclusions are completely out of step with the way that regulation is evolving and Ofcom has not sought to address or justify this disparity in its consultation. Recital 158 of the European Commission’s proposed Directive to establish the Electronic Communications Code states:
- “Ex ante regulation imposed at the wholesale level, which is in principle less intrusive than retail regulation, is considered sufficient to tackle potential competition problems on the related downstream retail market or markets. The advances in the functioning of competition since the regulatory framework for electronic communications has been in place are demonstrated by the progressive deregulation of retail markets across the Union. Further, the rules relating to the imposition of ex ante remedies on undertakings with significant market power should be simplified and be made more predictable, where possible. Therefore, the power of imposition of ex ante regulatory controls based on significant market power in retail markets should be repealed”* [Emphasis added]
73. BT agrees with the European Commission’s proposal that the power to impose ex ante SMP regulation in retail markets should be repealed. Whilst the proposals are not yet binding, they do emphasise at the least that ex ante regulation, particularly at the retail level, is and should be a measure of last resort. Any decision to impose ex ante regulation at the retail level requires very careful consideration and detailed explanation as to why SMP regulation is appropriate. This omission by Ofcom is particularly striking in circumstances where, as mentioned above, other tools are available which may have better addressed Ofcom’s perceived concerns in downstream markets, given the market-wide nature of Ofcom’s theory of harm.
74. None of the cumulative three criteria are made out for the reasons set out below. Ofcom has not sufficiently demonstrated that there is a relevant market susceptible to ex ante regulation.
75. *Criteria 1: Presence of high and non-transitory barriers to entry*
- For the reasons set out in section 5 of this Response, Ofcom’s assessment of barriers to entry and expansion is incorrect, and cannot be relied upon (in particular in relation to split purchase customers where Ofcom’s analysis is next to absent).
76. *Criteria 2: A market structure which does not tend towards effective competition within the relevant time horizon, having regard to the state of infrastructure-based and other competition behind the barriers to entry*
- As set out above, the voice market is currently dynamic and effectively competitive and will remain so in the future absent any retail level regulation of BT (given, particularly, the move to future voice, recent ASA changes and growth in mobile as well as non-traditional means of communication). Ofcom’s market definition is incorrect (see section 4) and there is no legitimate reason to impose retail level regulation on BT.

77. *Criteria 3: Competition law alone is insufficient to adequately address the identified market failures.*

Ofcom alleges two market failures, as opposed to specific anti-competitive practices: a lack of consumer engagement and consumer harm resulting from pricing above the competitive level.

In respect of the former, Ofcom has substantially misunderstood the extent of consumer engagement that currently takes place even amongst voice-only consumers and, as set out in sections 4 and 5, SMP regulation of one provider would not be an effective means of addressing any alleged market failure.

In respect of the latter, Ofcom has not sufficiently made out that prices are too high and in particular has failed to take into account the broader dynamics of pricing driven by a pro-competitive response to bundled purchasing which occurs in the market generally (as set out above).

***Proposed remedies are disproportionate and non-transparent***

78. As set out in more detail in section 6 of this response, whilst no remedies are necessary, in addition to an SMP finding being disproportionate, the remedies proposed are themselves disproportionate, non-transparent (contrary to s.47) and, in relation to Ofcom's behavioural remedy, lack legal certainty (given in particular the unbounded nature of that proposal).

79. Ofcom argues that its proposals will “*promote competition in relation to the provision of electronic communications services by ensuring that users derive maximum benefit in terms of choice, price and quality*”<sup>69</sup>. However, BT considers that Ofcom's proposed remedies have a high risk of bringing about unintended consequences (such as more consumers ‘down spinning’ to voice-only services or sticking with BT rather than consolidating their unbundled purchases with a rival) which will have the opposite effect to that which Ofcom hopes to achieve, and which would not, therefore, be in the interests of consumers.

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<sup>69</sup> Paragraph 9.36 of the Provisional Conclusions Consultation Document.

### 3. Protecting older or more vulnerable customers

80. BT's purpose is to use the power of communications to make a better world; this goes to the heart of who we are as a company. In this, one of our core focus areas is bringing the benefits of a connected society to everyone<sup>70</sup>. We are targeting disadvantage caused by social exclusion, lack of education, unemployment and challenges related to age and disability. Since 2014/15 BT has helped 2.6 million people to overcome disadvantage through the benefits that our products and services can bring. Our ambition is to increase this to 10 million people by 2020.
81. As such, BT takes its responsibilities to older and more vulnerable customers very seriously, in respect of price, value for money, quality of service and digital inclusion. BT has been active in this area for many years, and our investment is set to continue.
82. BT offers discounts and tailored products such as Home Phone Saver to our voice-only customers which has assisted in protecting them from increasing headline line rental prices (which apply to all consumers taking a line – whether or not on a standalone basis<sup>71</sup>). BT has not increased the price of line rental since July 2016 and has committed to freeze the price of line rental throughout 2017.
83. For the UK's most vulnerable people, BT offers BT Basic<sup>72</sup>. This is a low-cost phone and broadband service which helps people who are on qualifying state benefits to keep in touch whilst on a budget. BT Basic costs £5.10 per month and includes a £10 cap on the cost of making calls. BT Basic + broadband costs just £9.95 per month. It offers eligible customers 12GB of broadband data usage per month – enough to browse the internet for up to 30 mins a day; stream enough video to watch one SD film a month; upload 100 photos to social media per month; listen to 100 music tracks a month and play online games for an hour a week.
84. BT has developed innovative approaches to protecting these consumers and provided value added services. Cognisant of this customer base's particular characteristics, BT pro-actively helps our voice-only customers to benefit from these offers and product innovations, and has found ways of encouraging engagement that are effective (for example direct marketing with easy-to-use reply coupons<sup>73</sup>). Examples of the products and services that BT offers in this area include:
- a. a free service which diverts nuisance calls<sup>74</sup>

<sup>70</sup> <http://www.btplc.com/Thegroup/Ourcompany/Ourvalues/index.htm>

<sup>71</sup> See section 2 of this Response

<sup>72</sup> BT Basic: [http://btplc.com/Inclusion/ProductsAndServices/BTBasic/index.htm?s\\_cid=con\\_FURL\\_btbasic](http://btplc.com/Inclusion/ProductsAndServices/BTBasic/index.htm?s_cid=con_FURL_btbasic)

<sup>73</sup> See also sections 4 and 5 of this Response. BT also promotes relevant services and products at exhibitions and via Government support services such as via care workers and in Job Centres. Our monthly newsletter, "Connections", is circulated to approximately 3500 health and social care professionals. It is a good source of information about our products and services for professionals who reach out to vulnerable people on a regular basis.

<sup>74</sup> BT Call Protect: <https://www.productsandservices.bt.com/products/phone/call-protect>. Over 2 million people have subscribed to this service since it was launched earlier this year.

- b. a free priority fault repair scheme<sup>75</sup>. This gives priority repair over standard faults, 365 days a year, to eligible customers who rely on their home phone as they are unable to leave the house without assistance due to chronic long-term illness or disability.
  - c. a dedicated UK-based vulnerability helpdesk to assist customers who might require additional support. A ‘flag’ can be added to a customer’s account which will route their calls through to the vulnerability helpdesk. Advisors are specially trained on products and processes which can support people with specific impairments. The helpdesk offers a “one stop shop” service for faults and billing enquiries.
  - d. our “protected services scheme” which enables a nominated person to be added to the account and contacted in the event that a bill goes unpaid (for example if the account holder is unable to pay due to hospitalisation) – which can provide comfort to our customers.
  - e. the BT Including You<sup>76</sup> website which is designed to provide support to people who might have specific access needs. It includes information about BT Products and Services which are tailored towards people who have a disability or impairment. It also includes a section on “getting the best phone package”, which provides information on finding the best phone deal and highlights some things to look out for to avoid bill shock. It also includes a section on “getting online”<sup>77</sup> which provides advice on how to help a friend or family member get online, links to free courses on internet basics, teaching resources for helpers, helpful videos, tips for ‘online beginners’ and more.
  - f. BT has over 150 “Try before you Buy” centres<sup>78</sup> around the country which provide specialist advice to this segment, including on BT Basic. These facilities enable people to see and handle our phones and equipment to try to help them find the one that’s right for them, without being pressurised by sales people.
85. BT agrees with the importance of digital inclusion for all and for many years, we have focused on a digital inclusion agenda. During this time, we have tried to make broadband accessible to voice-only customers with compelling pricing and regular marketing in a way which makes things as easy as possible for this group of consumers to respond. BT also offers special deals, highlights the features and benefits of taking a bundled service, and, works with partners to bring the benefits of broadband to these consumers.
86. [§<].
87. In addition we also offer BT Basic plus Broadband, a low-cost package for people on income support for just £9.95 a month.

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<sup>75</sup>BT Priority Fault Repair Scheme:

[http://btplc.com/inclusion/HelpAndSupport/DocumentsandDownloads/BTServices/FreePriorityFaultRepairscheme/Free\\_Priority\\_Fault\\_Repair.pdf](http://btplc.com/inclusion/HelpAndSupport/DocumentsandDownloads/BTServices/FreePriorityFaultRepairscheme/Free_Priority_Fault_Repair.pdf)

<sup>76</sup> BT Including You: <http://btplc.com/Inclusion/>

<sup>77</sup> <http://btplc.com/inclusion/GettingOnline/index.htm>

<sup>78</sup> Try Before You Buy Centres: <http://btplc.com/inclusion/trybeforeyoubuy/default.aspx>





## 4. Market definition

### A. Introduction

88. Ofcom reaches a provisional conclusion that there are two relevant markets: a market for the provision of SFV access in the UK (excluding Hull) which includes sales to voice-only customers and split purchasers, and is limited to residential services<sup>79</sup>; and a market for the provision of SFV calls (i.e. fixed voice calls sold to SFV access customers) with the same geographic scope.<sup>80</sup>
89. BT does not agree that there are separate markets for SFV services; rather there is a wider retail market for fixed line services in which BT does not hold SMP. Within this wider market there are pro-competitive explanations for the pricing structure which Ofcom is concerned about. Ofcom's approach to market definition is flawed because it fails to recognise these relevant competitive dynamics and market wide pricing practices (adopted by all suppliers).
90. The competition concern identified by Ofcom – namely, lack of engagement preventing SFV customers from benefitting from retail competition to the same extent as dual play customers – is not a sufficient condition for defining a separate SFV market.
91. Ofcom has not shown that the necessary conditions are met to define markets for specific customer groups; indeed the significant migration of SFV customers to bundles indicates that the boundaries of the markets which Ofcom has identified are not stable.
92. Finally, even if it were correct for Ofcom to find separate SFV retail markets, so-called 'split purchase' customers clearly do not form part of that market and should not be subject to the same proposed remedies.
93. BT has instructed Oxera to review Ofcom's market definition and market power assessment in its Provisional Conclusions Consultation Document ("**the Oxera Report**"). A copy of the Oxera Report is included at Annex 2 to this response.

### B. There is a wider market for voice services in which the pricing practices Ofcom is concerned about are a rational and pro-competitive response by all firms to effective competition for bundles

94. Ofcom highlights (correctly) that the market definition exercise is "*not an end in itself, but a means to assessing whether there is effective competition and thus whether there is a need for ex ante regulation.*"<sup>81</sup>
95. The approach adopted by Ofcom identifies a focal product and then considers whether there is a case for broadening the market by applying the "Hypothetical Monopolist test" (also called the SSNIP test).<sup>82</sup> Ofcom also considers whether other products should be included in the market if they face the same

<sup>79</sup> Paragraph 3.3.1 of Ofcom's Provisional Conclusions Consultation

<sup>80</sup> Paragraph 3.3.2 of Ofcom's Provisional Conclusions Consultation

<sup>81</sup> Paragraph 3.7 of Ofcom's Provisional Conclusions Consultation

<sup>82</sup> This test considers whether a hypothetical monopolist could impose a small but significant transitory increase in price (a SSNIP) without the price increase being made unprofitable by customer switching to alternative services ("demand side substitution") or due to suppliers diversifying into supply of the relevant product ("supply side substitution").

competitive conditions as the focal products and/or a common pricing constraint.<sup>83</sup> Applying this approach, Ofcom finds that:

- a. **SFV access and SFV calls are separate markets** – because Ofcom identifies a difference in competitive conditions between them;
- b. **dual play services are not in the same market as SFV access and SFV calls for either voice-only customers or split purchasers** – because these customers are unlikely to switch in sufficient numbers to dual play in response to a SSNIP<sup>84</sup> to provide a competitive constraint on SFV prices;
- c. **the relevant SFV markets include both voice-only and split purchase customers** – because these customers purchase identical products under identical terms.

96. There are a number of shortcomings to Ofcom’s approach which mean that its market definition exercise does not provide a *“means to assessing whether there is effective competition and thus whether there is a need for ex ante regulation.”*<sup>85</sup> In particular, Ofcom’s approach does not allow a proper assessment of market-wide dynamics which explains the concerns that Ofcom has identified, nor how these dynamics may change fundamentally following the ASA’s intervention<sup>86</sup>.

97. As explained in Section 2 above and in the Oxera Report<sup>87</sup>:

- a. The incremental broadband price has historically been the focus of competitive activity reflecting the significant uptake of bundles and the advantages of bundled pricing in expanding consumption, promoting competition between firms and delivering benefits to consumers.
- b. Firms have therefore prioritised keeping the incremental broadband prices low in order to be able to compete effectively for customers of bundles (which, at 90%<sup>88</sup>, is by far the largest customer segment) rather than using line rental reductions as a means of competing for voice-only customers (which are a much smaller and dwindling group).
- c. Competition for voice-only customers has focused, instead, on product innovation (e.g. the creation of fixed price products such as Home Phone Saver) and discounts from headline call plan prices.
- d. Moreover, the low incremental broadband prices have encouraged take up of bundles by SFV customers consistent with the very significant migration of these customers in recent years and which is likely to continue.
- e. Overall, competition between dual play providers has resulted in margins which are consistent with a contestable market and it is not appropriate, in this context, to focus on profitability in a narrow segment.
- f. As explained in Section 2, this competitive dynamic has been acknowledged by Ofcom to deliver strong competition and good consumer outcomes including for the SFV customers that have (in vast

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<sup>83</sup> Paragraph 3.8.1 and 3.8.2 of Ofcom’s Provisional Conclusions Consultation

<sup>84</sup> Small but significant non-transitory increase in price.

<sup>85</sup> Paragraph 3.7 of Ofcom’s Provisional Conclusions Consultation

<sup>86</sup> See section 2A of this Response

<sup>87</sup> The Oxera Report, section 1.

<sup>88</sup> 9 out of 10 customers buy fixed voice as part of a bundle – The Oxera Report, footnote 4.

numbers) chosen to switch and those who have not switched have seen new products, greater value and supplier choice including from entrants such as the Post Office.

98. Put simply, there is a pro-competitive explanation for the pricing structure which has been observed historically, namely that price competition (within a wider market) has been targeted at broadband and that incremental broadband prices have been driven down by competitive pressure with offsetting line rental increases to maintain overall margins (which are also constrained by competitive pressure).
99. This pricing (and marketing) strategy is a market-wide feature that is not driven by the actions or behaviours of a specific firm, but rather the prevailing competitive dynamics in the market for bundles containing fixed voice. In fact, the outcome Ofcom is concerned about arises as a consequence of fierce competition for bundles, and an element of these bundles (i.e. broadband) becoming the focus of competitive activity. There can be no suggestion that a single firm is exploiting its market power; rather, all firms have rebalanced their prices in this way as a rational response to effective retail competition for bundles.
100. Ofcom’s approach to market definition fails to capture these relevant market dynamics and therefore fails to provide an appropriate framework for assessing the issues that Ofcom has identified; in particular the finding of significant market power is unreliable in the context of what are clearly market-wide effects.
101. In particular, the SSNIP test is inappropriate in the context of broader competitive dynamics because if SFV services were a distinct market, a hypothetical monopolist of this market would be able to sustain high prices and, at the same time would be expected to, retain the SFV customer base because, by definition, there is no effective alternative for SFV customers to switch to.
102. This is clearly not borne out by the evidence. SFV lines (across all suppliers) have consistently decreased from 6.1m (Q1 2013) to 2.9m (Q3 2016) – a 52% fall.<sup>89</sup> Ofcom accepts that the primary driver of this decline has been switching to bundled communications services (e.g. dual play).<sup>90</sup> Far from discouraging diversion (as one would expect of a firm with market power), suppliers have adopted pricing structures which minimise the incremental price when broadband is added to SFV in order to compete effectively for bundles and this has encouraged further take up of broadband by customers (consistent with digital inclusion objectives).
103. As Oxera state “... *Ofcom’s approach to market definition does not provide an appropriate framework for assessing the concerns that it has raised. We consider that a broader framework taking account of these market-wide pricing practices would be a more appropriate, both to understand the nature of any concern, taking account of all relevant competitive dynamics, and also to ensure that any intervention is appropriate and can actually fully address the any concern in a proportionate way.*”<sup>91</sup>
104. Ofcom has also given insufficient consideration to the likelihood that the ASA’s intervention will fundamentally change these dynamics. The ASA rules effectively prevent the incremental broadband price from being the focus of competitive offers as firms are unable to advertise broadband prices

<sup>89</sup> A8.15 of Ofcom’s Provisional Conclusions Consultation.

<sup>90</sup> “*The number of SFV access lines, i.e. bought outside a bundle, is in steady long-term decline. This is primarily driven by customers who upgrade to bundles communication services (e.g. dual-play)*”, paragraph 4.5 of Ofcom’s Provisional Conclusions Consultation.

<sup>91</sup> The Oxera report, Executive Summary.

separately from line rental prices. Instead, an all-inclusive dual play price must be presented and this has become the focus of price competition.

105. Any reduction in the line rental price is now unaffected by the risk that this would require an off-setting increase in the incremental broadband price which might jeopardise competitiveness. Firms may, therefore, consider line rental reduction as a further means of competing for voice-only customers alongside product innovation and discounts (although dual play providers may still balance this with promoting further uptake of bundles by keeping implicit broadband prices low)<sup>92</sup>.

### C. Ofcom’s error in defining SFV markets by reference to levels of customer engagement

106. If competition is working well for voice-only customers who take up broadband, and for split purchasers who optimise their existing voice and broadband purchases (which Ofcom accepts), then Ofcom’s concern is not about the availability of substitute products and the degree of switching. Rather, the heart of Ofcom’s concern appears to be predicated upon the existence of demand side barriers<sup>93</sup> which allegedly prevent a residual group of SFV customers from benefitting from retail competition to the same extent as dual play customers. In other words, Ofcom is concerned about how the benefits of competition are distributed across customer groups, not about the existence of competition. It states for example that “*survey evidence suggests that SFV customers have relatively low levels of engagement in the market*”<sup>94</sup> and “*the evidence we have suggests that SFV access customers typically show low levels of engagement and low willingness to switch suppliers.*”<sup>95</sup>
107. Although SFV customers have been sufficiently engaged to switch to dual play bundles in large numbers and there has been switching to other SFV suppliers (which Ofcom accepts<sup>96</sup>), Ofcom defines narrow SFV markets on the basis of the remaining SFV customers who (in Ofcom’s view) are less likely to switch – i.e. it has defined the market by reference to what it perceives to be low levels of customer engagement, whilst at the same time ignoring the engagement that has taken place.
108. Setting aside the question of whether Ofcom has sufficiently demonstrated a lack of engagement by SFV customers (which is discussed in Section 2 and 4), this is not a sound basis for defining separate retail markets. The error in defining markets in this way becomes clear when remedies are considered. If behavioural remedies were successful in addressing demand side barriers then (following Ofcom’s logic) the market boundaries would change<sup>97</sup> because the SFV customer would be more engaged and benefit from retail competition to the same extent as dual play customers. It also follows that Ofcom would

<sup>92</sup> The Oxera Report, section 1

<sup>93</sup> Ofcom identifies difficulties in reaching customers and convincing them to switch away from BT as the main barriers to entry and expansion – i.e. problems with customer engagement.

<sup>94</sup> Paragraph 4.8 of Ofcom’s Provisional Conclusions Consultation

<sup>95</sup> Paragraph 4.39 of Ofcom’s Provisional Conclusions Consultation.

<sup>96</sup> Paragraph 4.39.1 of Ofcom’s Provisional Conclusions Consultation “*Before the introduction of competition, BT had a near monopoly on fixed voice access. Whilst some of its customer have switched away, those that have not may have never switched suppliers, and consequently may be particularly disengaged, whereas those that have switched to other CPs will have engaged with the switching process at least once (i.e. from BT).*” (emphasis added)

<sup>97</sup> Either a narrow SFV market is now judged to be a broad voice market, or the SFV market is found to be smaller.

continue to identify a separate SFV market up until the last customer in the group is deemed to be engaged which is plainly absurd.

109. Equally, Ofcom’s theory of harm – namely that there is a softening of incentives to compete because voice-only and split purchase customers are harder to reach and persuade to switch – is a market-wide issue stemming from customer behaviour, not an issue arising from single firm market power and is not therefore capable of being effectively addressed by SMP regulation.<sup>98</sup>
110. Demand side issues relating to engagement have been reviewed by other regulators without defining separate markets for precisely this reason. For example, as part of its investigation of the energy market, the CMA identified that the intensity of competition varied between customers on different payment methods, due in part to actual and perceived higher costs to engage with, and acquire, prepayment customers compared with other customers. The CMA did not, however, identify distinct product markets for customers using different payment methods but instead identified different market segments of the broader domestic energy retail market.<sup>99</sup>
111. The Oxera report cites other case studies which demonstrate that “*markets do not need to be concretely defined for the regulator to comprehensively analyse the competitive constraints on different market players and within the particular market segments.*”<sup>100</sup>
112. A more appropriate approach would therefore be for Ofcom to consider the choices, prices and services available to the SFV segment and their levels of engagement within a wider market for voice services which includes dual play services. BT has no more market power in relation to a disengaged segment than any other market player, and spuriously defining markets to backwardly engineer such a result is not appropriate, nor is it necessary in order to address the alleged relevant issues. As set out in more detail below, at a minimum, Ofcom should recognise that there are important distinctions between voice-only and split purchasers and the implications of this for any proposed SMP conditions.

**D. Ofcom has not shown that the necessary conditions are met to define markets for specific customer groups**

113. The Oxera Report examines the conditions under which it may be appropriate to define a separate market in relation to a distinct customer group – namely where a hypothetical monopolist could use price

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<sup>98</sup> Ofcom acknowledges that this is a market-wide issue. It states “*SFV customers in general are relatively disengaged and unwilling to switch compared to other types of fixed voice customers.*” (Emphasis added, paragraph 4.45 of Ofcom’s Provisional Conclusions Consultation). However, Ofcom also indicates that “*BT customers appear to be particularly loyal and less engaged than non-BT SFV customers.*” Ofcom cites lower switching levels for BT than for non-BT customers to support this view (e.g. Figure A8.56), but this is unreliable in circumstances where BT has more SFV customers than its rivals. Oxera illustrates this by assuming that BT has 100 customers, TalkTalk has 10 customers and customers are equally engaged with a 10% rate of switching (i.e. 10 BT customers switch to TalkTalk and 1 TalkTalk customer switches to BT). On one view, 53% (10/19) of TalkTalk customers would report switching and 11% (1/91) of BT’s customers would report switching which might be interpreted as a lack of engagement by BT customers. In fact, customers show the same levels of engagement but the picture is distorted by asymmetric market shares. See the Oxera Report, section 1.4.

<sup>99</sup> Para 3.40, <https://assets.publishing.service.gov.uk/media/5773de34e5274a0da3000113/final-report-energy-market-investigation.pdf>

<sup>100</sup> The Oxera Report, section 2.1.3

discrimination to segment markets. The conditions require that customers have different demand characteristics, they must be identifiable and there must be no opportunity for direct arbitrage between the customers aimed at undermining the price discrimination.

114. Oxera finds that the third condition does not hold: in fact customers are encouraged to migrate from the SFV customer group to the dual play customer group and therefore any price discrimination is a migration strategy not a market segmentation strategy.<sup>101</sup> The bundling pricing strategy described above, when considered against these tests, is evidence of a broad market, rather than separate narrow markets.

**E. At a minimum, split purchase customers should be included in a voice market which includes dual play services**

115. Ofcom finds that split purchase customers could save between £8.00 and £14.50 by switching to an equivalent dual play service from their provider. These price differences would not be sustainable, in Ofcom’s view, if dual play exerted a competitive constraint.<sup>102</sup> Ofcom also highlights that a sizeable base of split purchasers have not switched (1.2m), and annual switching rates are equally low for voice-only and split purchaser customers (3%). Ofcom concludes that the remaining base are unlikely to switch in response to a SSNIP in sufficient numbers to constrain SFV prices to competitive levels.<sup>103</sup>
116. A range of evidence supports the inclusion of split purchase customers in a voice market which includes dual play services:
- a. there has been a significant amount of switching by split purchasers to dual play packages responding to the lower prices that can be achieved by consolidating;
  - b. Ofcom has not supported its assertion that split purchase customers are not optimising (nor is this a sufficient basis for defining a separate market);
  - c. split purchasers are much closer to dual play customers in their ability to access and realise the benefits of competition; and
  - d. suppliers (including the larger CPs) have strong incentives to attract these customers to take up their dual play offers.
117. In short, split purchasers show higher levels of engagement, have historically switched in large numbers to bundles and are highly attractive to the larger CPs who can use a range of channels to reach these customers (as they do for customers across the dual play base). Split purchase customers should be viewed as dual play customers (albeit purchasing dual play products on an unbundled basis).

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<sup>101</sup> The Oxera Report, at section 2.1.4 explains the distinction as follows: “*The use of price discrimination to migrate customers is a qualitatively different strategy to that of market segmentation. Under a market segmentation strategy the hypothetical monopolist would actively try to prevent arbitrage between the consumer groups. Under a migration strategy, the arbitrage opportunity is highlighted to consumers to encourage switching (indeed, the creation of the arbitrage opportunity is the very purpose of the price discrimination).*”

<sup>102</sup> Paragraph 3.41.1 of Ofcom’s Provisional Conclusions Consultation, “*If dual-play was a close enough substitute to competitively constrain the combined prices for functionally equivalent voice and broadband services purchased on a standalone basis by split purchasers, we would not expect these price differences to be sustainable.*”

<sup>103</sup> Paragraph 3.41.3 of Ofcom’s Provisional Conclusions Consultation

***There has been a significant amount of switching by split purchasers to dual play packages***

118. Ofcom accepts that the number of split purchase customers has been falling over time due to switching to dual play services. It states that such switching “*is likely to explain, to some extent, the material decline over time in the number of SFV customers*”,<sup>104</sup> and “*it is possible that a substantial number of split purchaser customers have switched to dual-play services.*”<sup>105</sup>
119. In 2016, Ofcom also reported a 40% decrease in the share of these customers in the residential total: “*Split purchasers can only be supplied by CPs using WLR (with SMPF) on the BT network. The Ofcom Technology Tracker survey estimates residential split purchasers account for up to 11% of all residential landline users in 2016. In 2012, 18% of residential landline users reported being in this category.*”<sup>106</sup>
120. This is consistent with a more general trend towards bundling as described in section 2. This switching is entirely consistent with dual play being a competing product for many split purchaser customers.

***Ofcom has not supported its assertion that split purchase customers are not optimising (nor is this a sufficient basis for defining a separate market)***

121. The fact that not all customers have optimised is cited by Ofcom in support of a separate market for SFV services to split purchasers.<sup>107</sup> More specifically, Ofcom adds average standalone fixed broadband prices (of around £20) with a line rental price of £18.99 and compares this to average dual play prices if split purchasers bundled these services. On this basis, Ofcom identifies that dual play customers are paying on average just over £14.50 more per month (compared to promotional dual play prices) or £8.00 more per month (compared to standard dual play prices).
122. Ofcom’s analysis merely finds that savings are available in principle through consolidation. Ofcom has not, however, undertaken an empirical analysis to identify whether these savings are available in practice by comparing actual prices paid by split purchasers (which will depend on the specific providers from which they purchase broadband and voice) with bundles to which they might switch.
123. In the absence of this analysis, there are a number of reasons why Ofcom may have overstated the savings that would be available to split purchasers in practice (if any):
- a. First, Ofcom’s own analysis indicates that, for many suppliers, the difference between unbundled and bundled prices is small or non-existent. For BT’s fibre customers, the price difference is between

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<sup>104</sup> Paragraph 3.41.2 of Ofcom’s Provisional Conclusions Consultation

<sup>105</sup> Footnote 45 of Ofcom’s Provisional Conclusions Consultation (emphasis added).

<sup>106</sup> Para 4.98 from “*Narrowband Market Review: Consultation on the proposed markets, market power determinations and remedies for wholesale call termination, wholesale call origination and wholesale narrowband access markets*”, Ofcom, 1 December 2016

<sup>107</sup> Paragraph 3.41.1 of Ofcom’s Provisional Conclusions Consultation “*If dual-play was a close enough substitute to competitively constrain the combined prices for functionally equivalent voice and broadband services purchased on a standalone basis by split purchasers, we would not expect these price differences to be sustainable.*”

£0.08 and £1.26 per month. For Sky customers, potential savings are given by Ofcom as £0.00 to £3.00. These savings are small, if they exist at all, after allowing for normal switching costs.<sup>108</sup>

- b. Second, Ofcom’s methodology leads to the impression of higher savings than consumers would actually be able to achieve because (i) it omits split purchaser customers who purchase line rental from CPs other than BT (for example those paying the Post Office offer of £14.99); (ii) it omits smaller providers of standalone broadband such as Plusnet and SSE; (iii) it omits legacy deals (e.g. from Tesco, Tiscali and O2) for standalone broadband which customers may still benefit from.
124. It may be the case, therefore, that for split purchaser customers using these suppliers the savings available are small or non-existent and that some consumers are, therefore, already optimising by not switching.<sup>109</sup>
  125. As shown in Figure 2.9 of the Oxera report, there are a number of reasons why consumers choose not to buy broadband from the same CP who provides their landline. One third of customers refer to the fact that they get a better deal and 29% report value for money as the reason for their choice to split-suppliers. A significant proportion of customers mention quality aspects of service. This is evidence to support the view that many split purchase customers are already optimising, and are on a deal that they regard as appropriate for them.
  126. There are numerous and rational reasons why split purchasers may choose not to bundle. There may be specific non-price benefits to consumers of purchasing in this way and, therefore, it cannot be assumed that they are not well served because they do not appear to be optimising from a price perspective (which has not been demonstrated by Ofcom in any event). These customers may be exercising a different choice in how they purchase to meet their own specific needs. For example, if a consumer wants BT Call Protect, faster repair on their line and unlimited weekend calls (including 0845 and 0870) for free with their Line they might choose BT for the line, but if they just wanted the cheapest available broadband they might choose a supplier whose out of contract price on their lowest broadband pack is less than £13.
  127. Other reasons why a split purchaser may not buy in a bundle include:
    - a. The availability of broadband deals for pay TV customers with a second provider (e.g. Sky has marketed broadband conditional on the purchase of a Sky TV package);
    - b. Being in contract for their BT line when they chose to take broadband (from a cheap supplier), resulting in a decision to split purchase, rather than to bundle;
    - c. Enabling multiple routes for the resolution of service issues (for example, if a customer had a problem with their line which affects both voice and broadband, being a split purchaser would enable 2 routes to resolve the issue);
    - d. Taking a phone line for a business<sup>110</sup> but the broadband is for personal use and the customer needs separate bills for VAT reasons (and vice versa).

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<sup>108</sup> The Oxera Report highlights that, in any normal market, there can be frictions that are not caused by customers behaving sub-optimally. Such frictions could include switching costs (such as the time cost of finding and securing a new service), which are present in all markets, and could explain why consumers do not move provider when savings are small. The Oxera Report, section 2.3.

<sup>109</sup> The Oxera Report reaches a similar conclusion in section 2.3

<sup>110</sup> See Annex 1, section A of this Response



128. Ofcom has failed to consider, adequately or at all, the importance of these consumer benefits to split purchasing and, in particular, its analysis of whether these consumers are in fact optimising their purchases.

***Split purchasers are much closer to dual play consumers in their characteristics, their ability to access and realise the benefits of competition than they are to voice-only consumers***

129. Split purchasers share similar demographics and access options to dual play customers. Ofcom accepts that: “[t]here is evidence that split-supplier customers are on average younger and of higher socioeconomic grade than voice-only customers..., and, by definition, have internet access (unlike the majority of voice-only customers). For these reasons, they are arguably more likely to be aware of alternative offers and/or engaged in the market.”<sup>111</sup> More specifically as regards to:
- a. **functional equivalence**, split purchase customers buy a product which is functionally equivalent to dual play services.<sup>112</sup>
  - b. **demand for broadband**, whereas Ofcom asserts that insufficient numbers of voice-only customers are likely to make a price-quality trade-off between voice-only and dual play, (because they do not want broadband) this does not apply to those who already take dual play (albeit unbundled);
  - c. **demographics**, split purchase customers are comparable in age to dual play customers with 35% being under 35, compared to 32% for dual play customers; and only 4% are over 75 (the same percentage for dual play customers).<sup>113</sup> Ofcom finds that split purchase customers are “*older than average*”<sup>114</sup> but there can be no presumption that this creates any barriers to switching or optimisation (and Ofcom makes no such argument). The Oxera Report highlights that split purchaser customers also have very similar socio-economic distribution as dual play customers, with a similar level of income and a similar proportion in work.<sup>115</sup>
  - d. **internet access**, split purchasers, by definition, have internet access and can access information on competing offers online (for example through price comparison websites) and therefore internet marketing is an effective way of reaching these customers;<sup>116</sup>
  - e. **engagement**, Ofcom claims that “[r]eported annual switching rates are equally low for both voice-only and split-supplier customers (3%) compared to dual play (12%) (see Annex 8, Figure A8.55).”<sup>117</sup> However, this is an incomplete and misleading description of the data which also shows

<sup>111</sup> Paragraph 3.40 of Ofcom’s Provisional Conclusions Consultation.

<sup>112</sup> Paragraph 3.39 of Ofcom’s Provisional Conclusions Consultation “*Although split purchasers buy the same SFV access product as voice-only customers, the combination of products that they purchase (SFV and broadband services) could be considered as functionally equivalent to dual-play services.*”

<sup>113</sup> Figure A8.49 of Ofcom’s Provisional Conclusions Consultation

<sup>114</sup> Paragraph 4.7.1 of Ofcom’s Provisional Conclusions Consultation

<sup>115</sup> The Oxera Report, section 2.2.2

<sup>116</sup> Paragraphs 3.40 and 4.7.3 and 4.37.2 of Ofcom’s Provisional Conclusions Consultation

<sup>117</sup> Ofcom claims that Jigsaw survey evidence shows that only 3% of split-supplier customers reported switching in the last 12 months. BT has not been able to confirm this figure. Table 66 of Wave 1 of the Jigsaw research “All who have broadband separate from their landline” shows that 50 out of 536 (i.e. 9%) customers switched their broadband in the last 12 months.

that 16% of split purchasers have switched or are considering such action. Elsewhere in the Provisional Conclusions Consultation document, Ofcom recognises that “*split-supplier customers may be more engaged than voice-only customers (15% compared to 6%), with broadly similar levels of engagement to dual-play customers (20%).*”<sup>118</sup> but does not adequately address this fact in its market definition analysis.

A more complete review of the data indicates that split purchaser customers are much closer to dual play customers than to voice-only customers:

**Table 2: Engagement levels in relation to fixed line services**

	Dual play	Voice-only	Difference to dual play	Split supply	Difference to dual play
<b>Engaged</b> <sup>119</sup>	20%	6%	-14%	15%	-5%
<b>Engaged and interested</b> <sup>120</sup>	54%	45%	-9%	50%	-4%
<b>Switched or at least considering switching in the last 12 months</b> <sup>121</sup>	22%	5%	-17%	16%	-6%
<b>Ever switched</b> <sup>122</sup>	55%	22%	-32%	44%	-11%
<b>Average</b>			-18%		-6.5%

The Oxera Report also finds that split purchase customers do exhibit a material amount of switching, (i.e. almost 20% have switched in the last 3 years compared to 26% for dual play customers) and that self-reported levels of engagement are similar across dual play and split purchaser customers, as is the perceived ease of switching.<sup>123</sup>

- f. **tenure**, 44% of split purchase customers have been with BT for less than 5 years, compared to 14% of voice-only customers;<sup>124</sup>
- g. **mobile usage**, 95% of the split purchase customers have access to mobile phones which compares to 96% for dual play customers, meaning that there is no material difference between split purchasers and dual play customers in this regard. Split purchase customers, therefore, have the same opportunity to substitute mobile calls for fixed calls as dual play customers. The Oxera Report also highlights that very similar proportions of dual play customers and split purchaser customers

<sup>118</sup> Paragraph 3.40 of Ofcom’s Provisional Conclusions Consultation

<sup>119</sup> Figure A8.51 of Ofcom’s Provisional Conclusions Consultation

<sup>120</sup> Figure A8.51 of Ofcom’s Provisional Conclusions Consultation

<sup>121</sup> Figure A8.55 of Ofcom’s Provisional Conclusions Consultation

<sup>122</sup> Figure A8.57 of Ofcom’s Provisional Conclusions Consultation

<sup>123</sup> The Oxera Report, section 2.2.2

<sup>124</sup> Figure A8.53 of Ofcom’s Provisional Conclusions Consultation

would respond to a SSNIP on their landline bill by switching some or all of their calls to mobile services.<sup>125</sup>

130. Split purchase customers are the same as, or very similar to dual play customers across all relevant dimensions. Ofcom accepts this, (in particular that split purchasers tend to be more connected and more engaged than voice-only customers) but observes “*that the remaining split purchasers have not responded to date to widely-advertised dual-play offers.*”<sup>126</sup> As noted above, there are many possible, and entirely legitimate, reasons why this may be the case. It is clear, therefore, that Ofcom’s concern is with the responsiveness and levels of engagement shown by split purchasers. There is no material difference between split purchase customers and dual play customers in this regard. Nor does this provide a valid basis for defining a distinct product market (as explained above).

***Suppliers (including the larger CPs) have strong incentives to attract split purchase customers to take up their dual play offers.***

131. Ofcom finds that the larger providers of bundled services are much less significant in SFV access.<sup>127</sup> In relation to split purchase customers, this is only because Ofcom inappropriately focuses on their voice purchases as opposed to their broadband purchases. BT understands that split purchase customers are supplied by the larger CPs when their broadband purchases are taken into account. Indeed the Oxera Report estimates that, other CPs could account for more than 80% of the supply of standalone broadband to split purchaser customers.<sup>128</sup>
132. Ofcom also acknowledges that, “*The majority of these [split purchase] customers could be supplied with MPF if they switched to a dual-play offer from a single CP. The falling share of split purchasers among landline users suggests some retail customers are willing to switch to a dual-play offer.*”<sup>129</sup> MPF providers (who account for 36%<sup>130</sup> of all Openreach lines) can, therefore, address split purchase customers, and have just as much incentive to acquire them as they do for dual play customers.
133. There can be no suggestion that incentives to compete for split purchasers are dampened due to their characteristics, as is asserted in relation to voice-only customers, given that those characteristics are much closer to those of dual play customers (if not identical). In particular, the expected value of the split purchasers is similar to dual play customers,<sup>131</sup> nor will the length of the supply relationship be shortened by the age profile of SFV customers.

<sup>125</sup> The Oxera Report, section 2.2.2

<sup>126</sup> Paragraph 7.24 of Ofcom’s Provisional Conclusions Consultation

<sup>127</sup> Paragraph 4.14 of Ofcom’s Provisional Conclusions Consultation

<sup>128</sup> The Oxera Report, section 2.5.1

<sup>129</sup> Paragraph .99 Narrowband Market Review Consultation on the proposed markets, market power determinations and remedies for wholesale call termination, wholesale call origination and wholesale narrowband access markets, 1 December 2016.

<sup>130</sup> Openreach Key Performance Indicators Q3 2016/17.

<sup>131</sup> Ofcom states “*There may be relatively limited scope for upselling additional services to SFV customers. This may particularly be the case for voice-only customers who may not have a need for broadband, although less relevant in the case of split purchase customers who could potentially be persuaded to switch to dual play.*” (emphasis added, paragraph 4.43.1 of Ofcom’s Provisional Conclusions Consultation.

134. In summary, not only do split purchase customers themselves have more incentive to switch according to Ofcom data, but suppliers also have more incentive to supply them with services. There is simply no sound basis for including split purchase customers in a distinct market with voice-only customers.

## 5. Market power

### Introduction

135. Ofcom assesses market power in SFV access and SFV calls using the following criteria<sup>132</sup>: market shares; barriers to entry and expansion; pricing and profitability; and countervailing buyer power.<sup>133</sup>
136. As set out in more detail below, BT does not agree with Ofcom’s market power assessment for the following reasons:
- a. BT does not accept that it is able, and will be able, to set the terms and conditions of sales for SFV services without facing competitive constraints from other providers.
  - b. Ofcom’s market share calculations do not provide a meaningful indication of market power.
  - c. Ofcom has overstated barriers to acquisition.
  - d. Ofcom ignores important distinctions between voice-only customers and split purchasers; there can be no suggestion that BT has market power in relation to split purchasers.
  - e. Ofcom’s pricing analysis ignores the broader context of switching to bundles which has been driven by lower incremental broadband prices.

### **B. BT is not able to set the terms and conditions of sales for SFV services without facing competitive constraints from other providers**

137. BT must offer attractive dual play services to retain SFV customers who are switching to dual play. [X] to aggressive broadband deals and increased price competition, for example deals with sub-line rental pricing (Sky) – see below – or Vodafone campaigns centring on no line rental.

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<sup>132</sup> Paragraph 4.16 of Ofcom’s Provisional Conclusions Consultation

<sup>133</sup> BT agrees with Ofcom that countervailing buyer power is not a factor in this analysis, and this is not therefore discussed further.

## £15 a month Sky Broadband Unlimited including line rental

This Cyber Monday get our best broadband deal. Reliable and totally unlimited Sky Broadband for just £15 a month when you join without Sky TV. Plus, get a £75 reward to spend wherever you like - online exclusive.

[> More about this offer](#)

[> View more offers](#)



138. In response to this competitive pressure, BT has made broadband accessible and available to the voice-only base with compelling pricing and regular marketing. We send marketing every quarter, outbound call customers with permissions, and provide existing customers exclusive offers to take broadband<sup>134</sup>.
139. For customers not inclined to switch to dual play services (an ever declining group), BT has created tailored products to defend against losses to competing providers, in particular the Post Office. In fact, a key part of our strategy is looking after customers to whom broadband may not appeal. For example, in 2014, in response to competitive pressure, BT developed Home Phone Saver. It was designed, based on insight, to help customers fix their bill including their call spend. We created a single price product, which provided peace of mind, with a 3 year price freeze that protected against price changes. Ofcom dismisses this significant innovation on the basis of modest take up and an assertion that the product is not “prominently advertised”.<sup>135</sup> This is inaccurate:
- a. The product is currently taken by [redacted] customers and has proved extremely popular with [redacted]. [redacted];
  - b. As well as regular direct marketing campaigns to voice-only customers,<sup>136</sup> BT’s main sales website also promotes Home Phone Saver (the prominence given to the product on the website reflects the fact that this is not the main marketing channel to voice-only customers although many do have access to the internet) as discussed below. Our efforts to promote Home Phone Saver have produced very impressive outcomes [redacted].

### C. Ofcom’s market share calculations do not provide a meaningful indication of market power

<sup>134</sup> See also section 3 of this Response.

<sup>135</sup> Paragraph 4.66 of Ofcom’s Provisional Conclusions Consultation “A relatively small proportion of BT’s SFV customers take the Home Phone Saver tariff. This implies that relatively few of BT’s SFV customers are sufficiently engaged to have sought out a lower price offer which is available (although not prominently advertised).”

<sup>136</sup> [redacted].

140. Ofcom estimates that BT has a share in excess of 60% for voice-only customers.<sup>137</sup> In respect of split-supplier customers, Ofcom finds that BT has a share approaching 100%, whilst for split-service customers, BT also has a share approaching 100%.<sup>138</sup> Ofcom estimates that, across the SFV access market as it has defined it, BT “*has a very high market share of 79%*”.<sup>139</sup>
141. BT does not agree that 79% is a valid market share estimate. In part the error arises from Ofcom’s narrow focus on SFV services which means that Ofcom incorrectly treats customers who have switched to dual play as having left the market. As a consequence, the very significant loss of voice-only and split purchaser customers to dual play services is not captured in Ofcom’s market share estimates for BT, nor the share gained by competitors who focus on multi-play and who have acquired a large number of SFV customer in recent years. Although BT retains a proportion of SFV switching to dual play, its share would be much lower when this switching is taken into account.
142. Further, shares of approaching 100% for split purchase customers suggests that BT has a monopoly when in fact this share is inflated because it excludes:
- a. the wider base of dual play customers who purchase exactly the same services as split purchasers albeit on a bundled rather than unbundled basis;
  - b. the broadband purchases by these customers which are just as relevant to any competition assessment. This again highlights the flaw in defining these customers only by reference to their voice purchase rather than by reference to their dual play (albeit unbundled) purchase.
143. The Oxera Report, section 2.5.1, calculates that BT’s share of the broadband component of split customers is modest at around 17%, [§<]. On this basis, BT does not have SMP in standalone broadband.
144. Although Ofcom’s analysis is flawed for these reasons, it does show BT’s share declining consistent with competitive pressure within the SFV segment and this trend is expected to continue. Ofcom finds that “*BT’s market share has fallen by six percentage points and those of Post Office and SSE have increased by [redacted] percentage points respectively, (to [redacted]% and [redacted]% respectively)*” but attributes this to “*BT customers leaving the market (through taking dual play or decline of overall customer base) at a faster rate than customers of other CPs, rather than being due to switching away from BT to other firms.*”<sup>140</sup>
145. Notwithstanding that BT does not see customers who have taken dual play as having left the market, BT is also concerned that Ofcom has under-estimated switching from BT to other firms for voice-only services.
146. [§<]<sup>141 142</sup>

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<sup>137</sup> Paragraph 4.21 of Ofcom’s Provisional Conclusions Consultation

<sup>138</sup> Paragraph 4.22 of Ofcom’s Provisional Conclusions Consultation

<sup>139</sup> Paragraph 4.18 of Ofcom’s Provisional Conclusions Consultation

<sup>140</sup> Paragraph 4.18 of Ofcom’s Provisional Conclusions Consultation.

<sup>141</sup> A8.17 of Ofcom’s Provisional Conclusions Consultation.

<sup>142</sup> [§<].

**Chart 4 – [REDACTED]<sup>143</sup>**

[REDACTED]

147. Our split purchase customers are:
- a. consolidating broadband and voice with other providers
  - b. consolidating broadband and voice with BT.
148. Our voice-only customers are:
- a. choosing another provider for voice services;
  - b. upgrading to a dual play bundle with BT; and
  - c. leaving BT to take voice and broadband elsewhere as their first entry into broadband
149. The Post Office is a key competitor, in the voice segment; Ofcom accepts that their share has increased as ours has declined.

**D. Ofcom has overstated barriers to acquisition**

150. Ofcom asserts that there are “*barriers to the acquisition of new customers in the SFV access market which may limit the ability of providers to compete effectively and expand in the market.*”<sup>144</sup> This is on the basis that:
- a. SFV access customers typically show low levels of engagement and low willingness to switch suppliers.<sup>145</sup> Ofcom states that BT’s SFV customers have lower switching rates and levels of engagement compared to non-BT customers, based on Jigsaw research.<sup>146</sup>
  - b. It is difficult for rival suppliers to find a cost-effective way of identifying customers within the SFV access market which is necessary to run an efficient marketing campaign.<sup>147</sup>
  - c. Online marketing is unlikely to be suitable for targeting these customers as a substantial proportion of SFV customers have limited internet access.<sup>148</sup>
  - d. BT has the ability to engage in “targeted retention” activities that limits other CPs’ ability to attract new customers<sup>149</sup>.

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<sup>143</sup> [REDACTED]

<sup>144</sup> Paragraph 4.36 of Ofcom’s Provisional Conclusions Consultation

<sup>145</sup> Paragraph 4.39 of Ofcom’s Provisional Conclusions Consultation

<sup>146</sup> Paragraph 4.39.2 of Ofcom’s Provisional Conclusions Consultation

<sup>147</sup> Paragraph 4.37.1 of Ofcom’s Provisional Conclusions Consultation

<sup>148</sup> Paragraph 4.37.2 of Ofcom’s Provisional Conclusions Consultation

<sup>149</sup> Paragraph 4.40 of Ofcom’s Provisional Conclusions Consultation



e. BT may enjoy a higher degree of brand loyalty compared to other CPs.<sup>150</sup>

151. As a result Ofcom says, “[t]he main barrier to entry and expansion is the ability of other CPs to reach customers and convince them to switch away from BT.”<sup>151</sup>

***SFV customers are more engaged than Ofcom has found; voice-only customers can be engaged; split purchasers are similar to dual play customers***

152. In addition to switching activity (described above), our SFV customers are actively engaging in a number of ways. [REDACTED].

**Table 3:** [REDACTED]

[REDACTED]

153. We consider, therefore, that [REDACTED].

154. There are examples of success in reaching and influencing voice-only customers:

- a. the Post Office has gained around [REDACTED] from a standing start in 2005 indicating that SFV customers have been successfully attracted away from BT. The launch was reported in 2005 as follows “*The Post Office has set its sights on grabbing a “significant slice” of the home phone market as it returns to the sector after an absence of 24 years. Launching its new HomePhone residential service, the group said call costs would be almost 20% cheaper than BT’s. The Post Office said it aimed to sign up one million customers - 5% of BT’s current residential business - by 2008.*”<sup>152</sup> This Post Office is an active competitive constraint on BT in the voice-only segment with a strategy that involves having the cheapest line rental price (since 2011);<sup>153</sup> three acquisition channels (online, call centre and in-branch); various marketing campaigns which highlight the ease of switching (including a recent radio campaign); and introductory offer of lower prices (12 months at £14.99 per month, £6 per month cheaper than BT Line Rental Plus and £4 less than BT’s standard line rental price).

<sup>150</sup> Paragraph 4.41 of Ofcom’s Provisional Conclusions Consultation

<sup>151</sup> Paragraph 4.45 of Ofcom’s Provisional Conclusions Consultation

<sup>152</sup> BBC 10/1/2005. <http://news.bbc.co.uk/1/hi/business/4159823.stm>

<sup>153</sup> Figure A8.24 of Ofcom’s Provisional Conclusions Consultation.

**Just need a phone line?**

Want to keep it simple? Free weekend calls to UK landlines including 0845 and 0870 numbers for just £15 a month

- ✓ £6 a month cheaper than BT Line Rental Plus
- ✓ FREE weekend calls to UK landlines (01, 02 and 03) and 0845/0870 numbers
- ✓ Keep your existing number and services
- ✓ UK based customer service
- ✓ FREE to pay your bill by cash or direct debit
- ✓ Low call rates. [Find out more.](#)

- b. SSE is currently offering a line only package at £13.50 per month (of which they indicate that £12 is for line rental) which is inclusive of local and national calls during the evenings and at weekends. Alternatively, customers can choose a Talk Anytime package which is inclusive of calls to local and national numbers at any time, and includes calls to 20 nominated international destinations.<sup>154</sup> SSE has been able to build on its presence as a household supplier in energy and extend this into telecoms, including to voice-only customers.
- c. BT has found good levels of responsiveness for campaigns aimed at voice-only customers (for examples in relation to BT's Home Phone Saver product). [X].
155. These examples show that such customers can be reached and persuaded to switch and the segment is clearly not as ossified as Ofcom is suggesting.
156. Split purchasers are virtually identical to dual play customers as an acquisition proposition as explained further below.

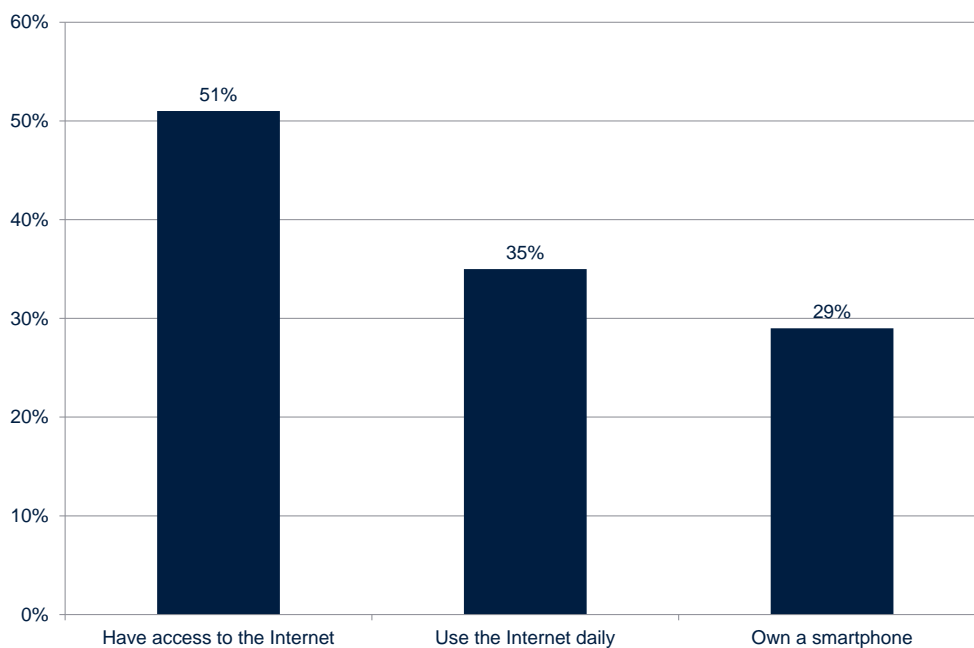
***Many voice-only customer have access to the internet***

157. Ofcom highlights “[o]nline access to information on competing offers” as a key feature of SFV customers and states “[a]mong SFV customers, a substantial proportion of voice-only customers (as opposed to split purchase customers) do not have direct broadband access, although some have internet access via mobile phones and some may have access via family, libraries or internet cafés.”<sup>155</sup> No evidence is provided by Ofcom to support the assertion that “a substantial proportion” of voice-only customers do not have internet access

<sup>154</sup> <https://sse.co.uk/phone-and-broadband/talk#Phone-packages> accessed on 13 April 2017.

<sup>155</sup> Paragraph 4.7.3 of Ofcom's Provisional Conclusions Consultation

158. In fact, just over half of voice-only customers have access to the internet and over a third use it daily. Also, 29% of voice-only customers own a smartphone.



The Oxera Report, Figure 2.8

159. Oxera conclude that “*many voice-only customers would be able to access market information, such as price comparison websites which are an important source of information. The barriers to consumer engagement in the voice-only segment are less than Ofcom assume.*”<sup>156</sup>

***Describing BT’s competitive activity as a barrier to acquisition is inappropriate; nor can a strong brand be a source of concern***

160. Ofcom unfairly badges BT’s competitive activity (targeted retention activity) as a barrier to other CPs attracting customers. The fact that competitive activity by BT makes it harder for CPs to attract customers is not a competition concern – it is competition. There is also a logical inconsistency between Ofcom’s assertion that take up of Home Phone Saver has been low and, at the same time, that BT is creating barriers to acquisition through its retention activity. It would appear that BT is doing something wrong both if it competes and if it does not compete.
161. As regards brand, BT is deemed to have market power in part because it has brand loyalty and is a “trusted brand”. It is not the case that this loyalty is undeserved. As Ofcom accepts, SFV customers indicate very high levels of satisfaction, of whom 79% are with BT.<sup>157</sup> Ofcom should not penalise suppliers for

<sup>156</sup> The Oxera Report, section 2.4.3

<sup>157</sup> Paragraph 4.9 of Ofcom’s Provisional Conclusions Consultation “*the majority of voice-only and split-supplier customers reported being very satisfied (74% and 58% respectively, compared to 54% for dual-play).*”

successfully building brand value or for being trusted where this is attributable to high levels of customer satisfaction with the service provided.

162. Further, the key competitors for voice-only customers have strong retail brands themselves (e.g. Post Office). YouGov Brand Index ranks the Post Office as the second highest utilities and service brand between January and December 2016.<sup>158</sup>

**E. Mobile has not been adequately considered as a constraint on landline services including for voice-only customers**

163. The Jigsaw wave 1 survey finds that 69% of those with a landline but no broadband own a mobile phone. Moreover, the same survey indicates that, if the overall landline price increased by 10%, a significant proportion of voice-only customers (11%) would be likely to switch some calls to mobile; 8% would be likely to switch some calls to email/text messages/instant messages; and 10% would be likely to give up their landline altogether.<sup>159</sup> Ofcom has not adequately considered the degree of constraint exerted by mobile including in relation to landline service taken by voice-only customers.

**F. There is no market power in relation to split purchasers**

164. Split purchasers are virtually identical to dual play customers as an acquisition proposition. They show:
- a. high levels of engagement – Ofcom accepts that “*split-supplier customers may be more engaged than voice-only customers (15% compared to 6%), with broadly similar levels of engagement to dual-play customers (20%)*”<sup>160</sup>;
  - b. have historically switched in large numbers to bundles – Ofcom accepts that “*it is possible that a substantial number of split purchase customers have switched to dual-play services*”<sup>161</sup>. 44% of split purchasers have switched, similar to 55% for dual play customers<sup>162</sup>;
  - c. are highly attractive to the larger CPs (including MPF providers).<sup>163</sup> The value of these customers to CPs is similar to dual play customer which drives high willingness to compete and high willingness to incur acquisition costs;<sup>164</sup> and

<sup>158</sup> <http://www.brandindex.com/ranking/uk/2016-annual/category/utilities-services>

<sup>159</sup> Jigsaw survey wave 1, table 639 (p.1011), table 661 (p.1048), table 672 (p.1065).

<sup>160</sup> Paragraph 3.40 of Ofcom’s Provisional Conclusions Consultation (emphasis added)

<sup>161</sup> Footnote 45 of Ofcom’s Provisional Conclusions Consultation (emphasis added)

<sup>162</sup> Figure A8.57 of Ofcom’s Provisional Conclusions Consultation.

<sup>163</sup> Narrowband Market Review, Consultation on the proposed markets, market power determinations and remedies for wholesale call termination, wholesale call origination and wholesale narrowband access markets, Ofcom 1 December 2016 paragraph 4.93. Ofcom indicates that voice-only customers might be uneconomic for MPF-providers because such customers only offer one revenue source having rented an exchange line (voice and not broadband). MPF providers do, however, compete for split purchase customers who offer two revenue sources in common with dual play customers.

<sup>164</sup> Ofcom’s analysis of CPs’ profitability in Annex 5 of Ofcom’s Provisional Conclusions Consultation only reflects the economics of attracting a voice-only customer, but the economic case is much better for dual play customers as is clear from the history of losses to CPs which has occurred over recent years.

d. can be reached using a range of channels, in particular internet marketing.

165. Ofcom appears to place some weight on “CPs’ views on customer acquisition” but these CPs have clearly only been asked (or have given answers solely for) voice-only customers, rather than split purchasers. For example, Ofcom quotes a CP as having “no appetite to re-enter the market”; mentions the older age profile of customers; describes channels for voice-only customers (and that these are restricted); and describes a voice-only proposition offered by a competitor. None of these barriers apply to split purchasers.<sup>165</sup>
166. In short, competition from large CPs who focus on multi-play services is being disregarded by Ofcom although these suppliers have acquired a large number of split purchase customers in recent years. The Jigsaw study on which Ofcom relies extensively in coming to their provisional conclusions does not suggest there are material impediments in this regard. As set out above split purchasers exhibit a material amount of switching and high self-reported levels of engagement (similar to dual play customers on both metrics). Split purchasers currently comprise just under [redacted] of BT’s “SFV” customer base, and are forecast to form around a third of such lines over the forward-looking period under review.

**G. Ofcom’s pricing analysis ignores the broader context of switching to bundles which has been driven by lower incremental broadband prices**

167. As indicated in section 2 and 3 above, line rental price increases must be understood in the broader context of the pro-competitive strategy (adopted by all of the main CPs) to offer attractively priced bundles where competitive activity has focused (historically) on the incremental broadband price. The ASA rules provide a greater opportunity going forward for competition in the voice-only segment to focus on the line rental price (in addition to other means of competing).
168. Dealing with each of Ofcom’s arguments on pricing:<sup>166</sup>
- a. *prices are significantly above costs and have been diverging further over recent years.* This divergence, however, has narrowed in recent years as our cost to serve the base have increased reflecting the additional value that we have offered (e.g. fixing faults 24 hours faster by upgrading to Openreach’s Care Level 2 and bringing back calls to the UK with 90% of calls answered onshore). More generally, this position has not come about due to the exercise of market power but rather due to a pro-competitive pricing strategy responding to bundled purchasing which has been adopted by all of the main CPs.
  - b. *BT’s prices also appear to be above those of other operators without this materially affecting its position in the market.* [redacted];
  - c. *there is evidence that BT acts as a price leader, with other CPs following its increases in line rental in terms of both timing and magnitude;* There is no reliable evidence of BT playing a price leadership role. Oxera has reviewed the limited evidence presented by Ofcom and concludes that (i) Ofcom’s sample is too small to reach meaningful conclusions (ii) in recent years BT has implemented price

<sup>165</sup> Paragraph 4.74 to 4.79 of Ofcom’s Provisional Conclusions Consultation

<sup>166</sup> Paragraph 4.67 of Ofcom’s Provisional Conclusions Consultation

changes first but in prior years other CPs have changed their prices first, and price changes do not follow an annual adjustment pattern in any event.<sup>167</sup>

- d. *price discrimination to offer greater discounts to more engaged customers (for example, through its Home Phone Saver tariff) allows BT to increase prices for (largely unengaged) SFV customers whilst limiting the risk to the revenues it earns from more active customer groups.* Given the active marketing by BT of the Home Phone Saver product, there can be no suggestion of a price discrimination strategy. Rather BT created this product in the face of competition from the Post Office.
- e. as regards calls, Ofcom itself states that, *“on balance, we have not sought to draw any conclusions as to market power on the basis of the pricing evidence alone.”* Ofcom does not find any evidence that BT’s prices are higher than competitors’, or that there is any question of “price leadership”.
169. More generally, Ofcom estimate that BT’s rental charge has increased in real terms by 46% since December 2009, and for Virgin Media by 49%.<sup>168</sup> However, line rental is purchased in order to access usage services, in particular to make and receive voice calls and access broadband enabled services. When this is recognised, the data shows that in real terms, customers are not paying more for their fixed services than when the retail market was deregulated in 2009, or in 2007/8 (the earliest year for which Ofcom shows data).
170. For the circa 90% of customers who have broadband, Ofcom data shows that average monthly charges for dual play bundles (including promotions) have been largely flat in nominal terms.<sup>169</sup> Whilst prices have been flat, the broadband speeds which CPs have been supplying broadband have increased hugely, as has the level of usage so value adjusted prices have gone down.<sup>170</sup>
171. As Ofcom also shows in Figure A5.4, revenue per month earned by BT from line rental and voice calls was £25.34 in 2007/8 and £23.67 in 2015/16 – this is a decrease of nearly 7% in real terms. This has largely come about due to changes in the market where customers are making fewer narrowband voice calls and instead making other forms of voice services, as well as making more calls over mobile phones. The reduction in the volume-based charges means that CPs have to recover their fixed costs from usage invariant charges.
172. In addition, as Ofcom reports, BT has been making improvements in its retail offer, see section 2 of this response for detail.

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<sup>167</sup> The Oxera report, section 2.4.5

<sup>168</sup> Paragraph 4.53 of Ofcom’s Provisional Conclusions Consultation

<sup>169</sup> Ofcom Communications Market Report 2016, Figure 4.4.

<sup>170</sup> For example, usage increased nearly 400% from 17GB per month in March 2011 to 82GB per month in June 2015. Ofcom Communications Market Review 2016, Figure 4.39.

## 6. Proposed Remedies

### A. Introduction

173. BT's position is that Ofcom has failed to define the relevant market or markets and in turn appropriately assess BT's market power; however, even if Ofcom had adequately defined the market and appropriately assessed BT's market power, there would be no justification for the intrusive nature of the remedies proposed.
174. The key issue is not whether BT has SMP but whether: (a) customers with particular characteristics (those who are relatively less engaged) are benefitting as much from the highly competitive retail voice market as customers with different characteristics (those who are relatively more engaged); and (b) whether the relative level of engagement is at a level which justifies a given intervention.
175. Split purchasers can be ruled out from any such discussion because Ofcom has not demonstrated that they are acting irrationally or are otherwise less engaged than other dual play customers<sup>171</sup>. In any event, for this group of customers, the most effective behavioural interventions cannot be delivered by BT acting in isolation.
176. For voice-only customers, Ofcom has underestimated the degree of engagement that these customers currently exhibit, and are likely to continue to exhibit in the future, absent any regulatory intervention, if current trends continue (for which there is no compelling evidence they will not). A correct assessment of engagement and other future trends demonstrates the disproportionate nature of Ofcom's remedies.
177. Ofcom's proposed price control remedies risk unwanted and unintended consequences for competition and consumer welfare, through:
- a. dis-incentivising voice-only customers from migrating to dual play bundles, thereby precluding these consumers from the benefits that would otherwise flow contrary to digital inclusion objectives;
  - b. unwinding the significant progress already made in relation to digital inclusion by incentivising customers to spin down from dual play to voice-only products; and
  - c. reducing the incentives of BT's rivals to compete by removing or significantly reducing available margins, (even when coupled with behavioural remedies), thereby limiting choice and stalling innovation.

The remedies are therefore contrary to Ofcom's s3 duties to further the interests of citizens in relation to communication matters, and to further the interests of consumers<sup>172</sup>, where appropriate by promoting competition.

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<sup>171</sup> See sections 2 and 3 of this Response

<sup>172</sup> See section 2B of this Response. BT also notes in this regard that pursuant to section 3(5) of the Act, Ofcom must have regard in performing its section 3 principal duties to the interests of consumers in respect of choice, quality of service and value for money as well as to price – which is only one relevant parameter.

178. If, however, Ofcom continues to pursue the imposition of an SMP remedy or remedies (incorrectly in BT's view), these adverse consequences must be fully assessed and minimised such that the remedies implemented are limited to:
- a. behavioural communication remedies that are the minimum necessary to encourage engagement. Such remedies should not seek to directly change outcomes, as this would not promote greater engagement and may have perverse outcomes; or alternatively
  - b. keep any starting price adjustment and subsequent control to a minimum to provide maximum room for continued and effective competition; and
  - c. extend only to voice-only customers.
179. Any remedies of this nature, in particular price control, should be assessed in the context of the propositions already in the market, for example the proposition introduced by Virgin Media targeted at SFV customers, and the active marketing by the Post Office of a low price landline only offer which specifically targets BT's customers<sup>173</sup>. In particular, they should preserve the potential for competition and protect the interests of citizens and consumers. In any event, the Virgin Media and Post Office initiatives demonstrate that the market is not in need of significant or obtrusive intervention to address engagement issues.

**A. Ofcom has not adequately supported the need for SMP regulation either legally or substantively**

180. To achieve a consumer protection end (the protection of vulnerable and elderly customers), Ofcom has mischaracterised an alleged problem relating to the levels of engagement of a sub-set of consumers, as a problem relating to single firm market power. If there are consumer engagement issues, they are (by definition) not the result of operator behaviour (as Ofcom itself recognises – see 3.128.2), but the symptom of a market wide demand side feature.
181. This market feature (to the extent it exists) affects and has implications for all operators in the industry. Addressing any such concern would require an industry-wide approach, not a remedy solely targeted at a single operator.

**B. There is no basis for imposing remedies in relation to split purchasers**

182. There is no basis for the imposition of SMP remedies in relation to split purchasers because Ofcom has not demonstrated that BT enjoys SMP in relation to these customers. Ofcom (wrongly) finds that split purchase customers are not optimising their purchases and have not responded to widely advertised dual play offers. However, this is pure speculation and Ofcom provides no compelling analysis or evidence to support this position (see Section 4 above).

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<sup>173</sup> See section 5 of this Response.



183. To the extent that Ofcom provides any justification this is limited to suggesting that switching rates for these customers is lower than Ofcom would expect given the savings that Ofcom claims are available to these customers. However, Ofcom has not substantiated that these savings are available in practice to split purchasers, nor that they are sufficiently large to drive incentives to switching. In any event, switching rates, are not in and of themselves evidence of a failure to engage and optimise.<sup>174</sup> Indeed, consumers may be engaged and choose not to switch particularly if the gains from doing so are modest. Ofcom fails to explore the reasons why these customers have chosen to split their line and broadband purchases, in particular the range of factors which may explain such a decision.
184. Even if Ofcom could successfully show that split purchase customers are disengaged and therefore not optimising their telecoms purchases, this is not in and of itself a sufficient basis for defining a separate market (as discussed in Section 4). Even if Ofcom were to persist with a market definition based on relative engagement levels (which is analytically incorrect in this context), it cannot limit the scope of this market to only the voice purchase when disengagement (and the alleged problems this creates) applies just as much to the split broadband purchase.
185. The flaws in Ofcom’s approach to this group becomes evident when remedies are considered:
- a. price control: Ofcom’s focus on the SFV-access and calls purchases by split purchasers in isolation of their broadband purchases, is asymmetric and inappropriate if, due to their disengagement, the split service provider is able to increase its price for the standalone broadband service; and
  - b. behavioural remedies: cannot be justified for split purchase customers in circumstances where BT has no visibility of these customers’ broadband purchases and would be unable, in isolation, to properly devise a sensible information remedy which would encourage these customers to select a better value product that suits their needs.<sup>175, 176</sup>

**C. For voice-only customers, Ofcom’s proposed remedies are disproportionate**

186. Ofcom has considerably underestimated the degree of engagement that SFV customers currently, and on a forward looking basis, will exhibit both in connection with our offers and services, as well as those of our rivals:
- a. a vast number have switched to dual play bundles in recent years;
  - b. our voice-only customers have also churned to competitors, [redacted];
  - c. [redacted];
  - d. [redacted]; and
  - e. engagement is likely to continuing for the period covered by the proposed remedies.

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<sup>174</sup> BT observes that the switching levels for this segment are considerably above those for pay TV retail markets, where Ofcom has declined to regulate.

<sup>175</sup> The situation is further aggravated by the asymmetry and therefore unfairness that a split-supplier of Broadband, knows that there is voice line provider, as otherwise the Broadband service could not be provided.

<sup>176</sup> Further, BT unlike other providers, through its Universal Service Obligations, has no option but to supply a line rental product creating asymmetry between service providers.

187. A range of factors suggest that this level of engagement will be maintained or increase going forward, including BT's desire to migrate these customers to dual play services, both for commercial reasons and future network migration (i.e. closure of BT's PSTN and move to IP services over broadband), and the need to react to competition from mobile and from SFV providers, including the Post Office, through the continued promotion of services like Home Phone Saver.
188. If engagement is assessed correctly, on both a current and prospective basis, with other future trends properly taken into account, Ofcom's proposed remedies are clearly disproportionate and unnecessary.

**D. Ofcom's proposed conditions could have serious and unintended consequences**

189. There are a number of unintended consequences of Ofcom's proposed conditions.
190. A reduction in the price of SFV services will:
- a. at best, freeze the existing SFV customer base by making migration to bundles very much less attractive; and
  - b. worse, increase the size of the SFV customer base by incentivising dual play customers to spin down to SFV services.
191. In both cases, these effects arise because the incremental price of broadband becomes higher relative to the price of SFV services, especially SFV-access services.
192. This will work against the grain of trends to date which has delivered a significant and ongoing migration of SFV customers into a market segment which Ofcom regards as competitive. It also has adverse consequences from a digital inclusion perspective which Ofcom has not assessed, and which has significant consumer detriment implications.
193. In the case of split purchasers, there is the further risk that a price reduction will act to deter consolidation of purchasers with a single provider by these customers through the elimination of any price differential between bundled and unbundled offers (to the extent that such a differential exists). In short, providers of bundles may find it more difficult to persuade split purchasers to consolidate in circumstances where the gains from doing so are significantly reduced or eliminated. Put simply, the price reduction will reduce incentives of voice-only customer to switch into bundles and of split purchasers to consolidate with rivals; both effects are contrary to Ofcom's objective of protecting customers and stimulating greater competition.
194. Ofcom suggests that benefits may be available even after a price reduction from more vigorous competition including further price reductions as well as benefits from product differentiation by reference to service features.<sup>177</sup> These price and non-price benefits are not explained further by Ofcom, nor does Ofcom assess the likelihood of such innovation post price cuts.

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<sup>177</sup> Paragraph 6.7 of Ofcom's Provisional Conclusions Consultation

195. In practice, customer engagement may fall following the imposition of a price cap which may create a moral hazard through a safe haven effect because SFV customers may feel protected and that they do not therefore need to engage and, for example, shop around for a better dual play deal or better line and calls package. This may compound other barriers to stimulating competition following a price reduction, in particular, lower profitability associated with winning customers.
196. More generally, these benefits are hard to envisage after significant price cuts and in the context of a declining market, the age profile of customers and the limited share of household budgets accounted for by SFV services (as accepted by Ofcom).<sup>178</sup>
197. These adverse effects and perverse outcomes are contrary to Ofcom’s s3 duty to further the interests of consumers, where appropriate by promoting competition<sup>179</sup>.

**E. If Ofcom continues to seek to impose regulation these adverse consequences should be minimised and any conditions should be proportionate**

***Prospect of success of behavioural remedies if implemented without a price reduction***

198. Behavioural remedies have a greater prospect of success if implemented without a price reduction, as accepted by Ofcom which states that this would “*ensure that BT’s competitors have the greatest possible incentive to compete for SFV customers, both in terms of prevailing prices and hence returns associated with winning customers.*”<sup>180</sup>
199. Ofcom should not, however, take forward more intrusive remedies seeking to directly change outcomes as these do not promote greater engagement and may have perverse outcomes. In this respect, while not accepting that other communication remedies are objective, proportionate or transparent, BT agrees with Ofcom that remedies that would require automatic switching within BT tariffs or the creation of a customer database and disclosure of this information to CPs and other third-parties, should not be taken forward.
200. As Ofcom acknowledges<sup>181</sup>, nor should Ofcom pursue remedies which force BT to market to its customers the offers available in the market from its rivals, such a remedy may give rise to unforeseen consequences, create disputes between BT and other providers and customers (e.g. through BT being accused of misrepresenting another CP’s proposals or being unaware of all offers in the market) and therefore create significant practical compliance challenges.
201. Any behavioural options which are trialled must not give rise to disproportionate costs nor risk damaging BT’s customer relationships. Further, Ofcom’s analysis of the costs of its proposed remedies is limited; Ofcom makes no attempt to assess the cost to BT, (other than in respect of postal charge costs), of trialling

<sup>178</sup> Paragraph 9.15 of Ofcom’s Provisional Conclusions Consultation.

<sup>179</sup> See section 2 B of this Response.

<sup>180</sup> Paragraph 9.13 of Ofcom’s Provisional Conclusions Consultation

<sup>181</sup> At paragraphs 7.26 to 7.28, Ofcom identifies a range of difficulties with requiring BT to advertise all market offers.

a variety of measures in terms of format, content, etc. and is therefore unable to conclude whether any measure is objectively justifiable or proportionate. This is especially so given the very open and wide nature of the proposed legal instrument that lacks specificity as to the format and content of the communications that Ofcom may in the future wish to trial, the number and frequency of trials and how these might be run (e.g. number of participants) as well as the implementation and monitoring phase following the trials which is not bounded in any way.<sup>182</sup>

***Any price control must avoid deterring CPs from engaging in the market by unduly reducing margins***

202. If Ofcom decides to proceed with a price control, it should be cautious in setting the level of any such price control to avoid deterring CPs from engaging in the market by unduly reducing margins. If Ofcom wishes to protect customers from price increases in the short term then a safeguard cap would deliver a level of protection while providing the maximum incentive to compete for SFV customers.
203. Any price control should also be time limited; it should be removed once there is sufficient evidence that behavioural remedies are enhancing competition and delivering benefits for consumers in terms of price, choice and available services.

**F. Regulation is unnecessary in light of market-led initiatives**

204. Given the recent changes to the rules around the way that dual play broadband packages are advertised, [redacted]. Indeed, BT has already frozen the price it charges for its standard line rental product (see section 3 above). In addition, BT has been increasing the value of its line rental product to its customers by increasing the quality of its care (repair) levels and through the introduction of a free consumer protection product, BT Call Protect, which enables BT's customers to reduce nuisance calls<sup>183</sup>. A deeper price cut would stifle current competition and may chill innovation, as exemplified by BT Call Protect.
205. It is both appropriate and necessary to leave room for competition to ensure the continued delivery of choice for voice-only consumers and the potential for benefits in terms of price, quality of service and innovation.
206. [redacted]. BT has developed offers for its voice-only customers which have [redacted], for example BT's Home Phone Saver proposition, demonstrating that BT has successfully found ways of providing information on alternative products (within the BT portfolio) and facilitating responses (using coupons) to help ensure that voice-only customer continue to gain better value for money.
207. We consider, that the measures which are more likely to increase engagement are those measures that prompt customers to take action, by explaining the potential benefits in general terms.
208. Given BT's considerable experience, expertise and the relationship that we have with our customers it is important that, if a communications remedy is imposed, we lead the development of such

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<sup>182</sup> See Annex 1 of this Response.

<sup>183</sup> See section 3 of this Response.

communications, taking input from Ofcom. It is not necessary for Ofcom to require BT to work with Ofcom to trial and implement such measure.<sup>184</sup> Nor is this appropriate [§<]. Nor is any such obligation proportionate given that Ofcom has not demonstrated to the requisite legal standards that BT has SMP in relation to a distinct market for voice-only services.

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<sup>184</sup> Ofcom has proposed that behavioural trials should be led by Ofcom (i.e. Ofcom determines what is trialled, the process and what is implemented following trialling); BT would be required to (i) provide information to assist Ofcom determine trial design and (ii) undertake trials and would incur the associated costs.

## Annex A: Legal instrument

1. BT provides the comments below on Ofcom’s draft legal instrument. These are without prejudice to BT’s position set out in the main body of this response that no SMP regulation of BT is justified in this case and that the proposed SMP conditions are not compliant with the requirements of the Communications Act 2003 and CRF<sup>185</sup>.

### A. Definitions and overall scope of the draft legal instrument

2. BT notes that the “Dominant Provider” is defined as BT and, in turn, BT is defined as BT Plc (including all subsidiaries and holding companies). In this regard, we note that Ofcom has expressed to BT that the proposed SMP Conditions should apply only to SFV customers of BT Consumer’s voice products sold under the BT brand (and that, in particular, customers of BT Business & Public Sector, Plusnet and EE are intended to be excluded from scope). BT is concerned that, as currently drafted, the conditions could inadvertently include other lines of business than BT Consumer and / or other group companies. As a result, and for the reasons set out below, BT considers that some amendments to the definitions are required to make this clear.

#### ***BT Business and Public Sector (“BPS”) and other BT lines of business***

3. Ofcom provisionally concludes that business SFV is excluded from the relevant markets it has defined<sup>186</sup>. Ofcom therefore proposes no action in respect of business customers. BT agrees with this and notes the following additional reasons why business customers should be excluded from the scope of any SMP regulation of BT (whilst none is justified in any event):
  - Business customers seek to manage their commercial activities and control their costs in the most effective way (perhaps even having more incentive to do so than residential consumers).
  - There are a wide range of competitive offerings which enable a business SFV customer to obtain a good deal, including on a voice-only or split purchase basis.
  - Many of BT’s business SFV customers will use their lines for specific purposes e.g. alarms, fax machines, lift phone etc. To meet these and other basic telephony needs, BPS offer a basic “Value” phone package at £16.90pm which is advertised alongside its standard phone packages at £22.50<sup>187</sup>. This value package includes 100 free landline call minutes per month. In comparison, TalkTalk offers a single line for business at £16.95 per month with PAYG calls.
4. Ofcom’s current definitions mean that business customers may be inadvertently caught by the proposed SMP conditions if implemented as drafted. In particular:
  - BPS sells business lines to sole traders, partnerships and limited liability partnerships – as well as to registered companies. Defining a BT Business Service as: “*all BT products and/or services that are only available to entities with a company registration number*” is therefore inaccurate and would mean that these other types of business customers could be caught by the proposed SMP Regulations.

<sup>185</sup> See in particular section 2 B of this response.

<sup>186</sup> See paragraphs 3.54–3.56 and 3.106 of Ofcom’s Provisional Conclusions Consultation.

<sup>187</sup> <https://business.bt.com/products/voice/phone-lines/>

- BT suggests therefore that the definition of BT Business Service is amended to read:

*“BT Business Service means all BT products and / or services that are only available to business entities, in particular but without limitation those products and services provided by BT’s Business & Public Sector Division, Global Services Division, EE or Plusnet”*

5. For clarity, a specific exclusion should be provided for BPS (and indeed for Plusnet, EE and all BT lines of business other than BT Consumer) under each of conditions 1 and 2 as opposed to relying on the current definition of “Services” to exclude non-residential products / services or services provided by other parts of BT. There are many ways that this could be achieved but we propose that: 1) the definition of “Customer” is amended to include the word “residential” before “Service”; 2) “legal entity” is removed from the definition of Customer; 3) the definition of Service is amended to make clear that these are services provided by BT’s Consumer line of business; 4) this could also be achieved by amending the Annex to Schedule to say, those products provided by BT, through its Consumer business unit to residential customers alongside the inclusion of a footnote (or equivalent text in the recitals), that states, *“It is not Ofcom’s intention, for example, that BT’s Plusnet and EE brands, should be caught by the Conditions, including following any internal re-organisations.”*

#### **B. Condition 1 is disproportionate and non-transparent in respect of scope and lacks legal certainty**

6. In relation to Ofcom’s proposed behavioural remedy (“the Communication Requirement” – Condition 1), Ofcom states that this is *“transparent in that it is clear what it is seeking to achieve – the promotion of competition through greater consumer engagement – and in setting out what BT is or may be required to do in future”*<sup>188</sup>. However, the communication requirement is so open ended that it effectively constitutes a ‘blank cheque’ for Ofcom to require BT to do whatever Ofcom asks of it in relation to communications with its SFV customers (and at any cost) without sufficient clarity as to what will be required and within what timescales. This is clear from a plain reading of Condition 1<sup>189</sup> which states as follows:

*“1.1 The Dominant Provider must comply with any Communication Requirement which Ofcom may from time to time direct.*

*1.2A The Dominant Provider must cooperate with Ofcom in the development and evaluation of Communication Requirements and must provide Ofcom with such information as Ofcom may require for the purposes of evaluating the effectiveness of any Communication Requirement.*

*1.2B In complying with its obligations under Condition 1.2A, the Dominant Provider must comply with any directions made by Ofcom.*

*1.3 For the purposes of Conditions 1.1 and 1.2A, Communication Requirement means any direction issued by Ofcom which requires the Dominant Provider to produce, provide or distribute information, or make specific communications to, its Customers, in a specified manner and form. [...]*

[1.3A then goes on to describe some non-exhaustive examples]

<sup>188</sup> Paragraph 9.38 of Ofcom’s Provisional Conclusions Consultation.

<sup>189</sup> See Annex 9 of Ofcom’s Provisional Conclusions Consultation (emphasis added).

7. This proposed remedy is a clear breach of Ofcom’s section 6 duty<sup>190</sup> not to impose unnecessary regulatory burdens. Contrary to Ofcom’s assertion that this condition is *“the least onerous means of achieving the objective we have identified in that it allows for the trialling of the least onerous engagement remedies<sup>191</sup>”*, it is not even possible to properly evaluate whether there would be less onerous (and therefore proportionate) means of addressing Ofcom’s concerns because Ofcom’s proposed remedy is so uncertain and non-specific in terms of what it actually requires.

- As to scope:

- i. Ofcom considers that the first step in the process of trialling engagement remedies would be: *“Diagnosing the issue to be addressed, potentially including research to identify the specific factor(s) restricting engagement. For example, which are the most critical barriers to engagement. This would also include considering whether the issue is common across all standalone voice customers, or just a subset (such as voice-only or split-purchase customers).<sup>192</sup>”* “Diagnosing the issue” should, respectfully, be a matter for Ofcom’s initial review – not for the setting of remedies.
- ii. Ofcom then considers<sup>193</sup> that remedies to be trialled should be identified, research and tests should be carried out to refine these options, a trial would then be run and the results assessed. The measures would then be monitored with further testing if Ofcom considers needed. Ofcom does not specify (either in the body of its consultation document nor in the draft legal instrument) the number or frequency of trials (Ofcom simply notes that this should reflect the detriment identified).
- iii. As set out in the main body of this response, BT must not be subject to open ended obligations to re-trial and implement different remedies. For the avoidance of doubt, BT is not disputing the importance of trials *per se* but rather that this is not appropriate to impose as an SMP condition because of this lack of transparency (contrary to s47(2)) and certainty.

- As to cost:

- i. Ofcom would require BT to bear the cost of running any trials<sup>194</sup>
- ii. Ofcom itself notes that it has: *“not at this stage attempted to estimate in detail the costs involved in implementing any of these remedies<sup>195</sup>”*.

- As to timings:

- i. Ofcom envisages that the process of development, trialling and implementation *“could take up to two years before any engagement remedies are fully implemented”<sup>196</sup>*.

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<sup>190</sup> See section 2B of this Response.

<sup>191</sup> Paragraph 9.38 of Ofcom’s Provisional Conclusions Consultation.

<sup>192</sup> Paragraph 7.96.1 Ofcom’s Provisional Conclusions Consultation.

<sup>193</sup> Paragraph 7.96 of Ofcom’s Provisional Conclusions Consultation.

<sup>194</sup> Paragraph 7.99 of Ofcom’s Provisional Conclusions Consultation.

<sup>195</sup> Paragraph 7.15 of Ofcom’s Provisional Conclusions Consultation.

<sup>196</sup> Paragraph 7.103 of Ofcom’s Provisional Conclusions Consultation



- ii. BT notes that the market review period envisaged is three years and, that by this time, [§<]<sup>197</sup>
8. As a result of these issues, in BT's view, Condition 1 is fundamentally flawed. It is disproportionate, non-transparent and in breach of Ofcom's duties. It would need to be completely re-drafted in order to resemble an appropriate SMP condition which would meet the requirements of s.47(2).
  9. In addition, as noted above, it should be made clear on its face that this obligation only relates to BT's Consumer line of business.

### Condition 2 - Price control

10. In setting the level of the price control, Ofcom must consider the impact of its proposals on its primary duties to further the interests of citizens in relation to communications matters; and to further interests of consumers in relevant markets, where appropriate by promoting competition<sup>198</sup>. However, Ofcom's price control proposals, in particular the range of the starting price reduction in the first year of the review, bring with them a number of risks<sup>199</sup>, these risks include:
  - a chilling of the forecast take-up of dual play broadband bundles by those who are currently digitally disengaged, or who are only partially digitally engaged, and therefore removing or limiting the real benefits that citizens and consumers will potentially gain from becoming digitally engaged; and
  - potentially reduce the positive impact of any behavioural 'communication' remedy, reducing the benefits of those remedies.
11. It is essential, therefore, that Ofcom more fully assess these risks, in order to construct a price control remedy that discharges Ofcom's duties, meets the needs of citizens and consumers, and maintains and promotes competition.
12. In terms of more specific changes that are required to the legal instrument:
  - VAT – the price control should be net of VAT and this should be reflected in the wording of the draft legal instrument.
  - As set out above, the price control should explicitly describe that it is targeted at BT's Consumer business unit. This could be achieved by amending the Annex to Schedule, to say, those products provided by BT, through its Consumer business unit to residential customers. And have a footnote, that states, "*It is not Ofcom's intention, for example, that BT's Plusnet and EE brands, should be caught by the Conditions.*"
  - It is not clear to BT where the revenues to be used in any SMP Condition (and in the first formula in 2.6A) are defined in Condition 2. BT assumes these revenues are for services consumed by the Customer (as defined in Part 1 Interpretation of the SCHEDULE) but we are unsure where, in the definitions, this is explicitly set out.

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<sup>197</sup> See section 2 of this Response

<sup>198</sup> See section 2B of this Response.

<sup>199</sup> See also section 6 of this Response.

- There is a square bracket missing from the formula copied below (at 2.2) and this would need to be corrected:

$$CC_t = CC_{t-1} * (1 + CPI_t + [0-2.5\%])$$

- In addition, as noted above, it should be made clear that this obligation only relates to BT's Consumer line of business.

In respect of Ofcom's proposed obligation on BT to provide and publish information BT notes that Ofcom has published a separate consultation in relation to regulatory reporting and publishing requirements. BT will respond fully to both the need for Conditions 2.7 and 2.7A and structure and extent of the obligations in its response to that separate consultation. However, BT would observe that Ofcom has demonstrated no objective or proportionate need for the publication of any BT information.

## Annex B: Responses to Ofcom's questions

*Question 3.1: Do you agree with our provisional conclusion that there is a separate market for Standalone Fixed Voice residential access which includes both voice-only and split purchase consumers? Please provide reasons and evidence in support of your views.*

BT does not agree with Ofcom's provisional conclusion that there is a separate market for Standalone Fixed Voice residential access which includes both voice-only and split purchase consumers.

Our reasons and evidence are set out in Section 4 where we show why there is a wider retail market for fixed line services (in which BT does not have SMP). This is on the basis that:

- The pricing practices Ofcom is concerned about are a rational and pro-competitive response by all firms to effective competition for bundles (section 4B, paragraphs 94–105).
- Ofcom has made an error in using levels of customer engagement to define markets (section 4C, paragraphs 106–112).
- Price discrimination has not been by suppliers used to separate customer segments (section 4D, paragraphs 113–114).
- At a minimum, split purchase customers should be included in a voice market which includes dual play services (section 4E, paragraphs 115–134).

*Question 3.2: Do you agree with our provisional conclusion that there is a separate market for Standalone Fixed Voice residential calls? Please provide reasons and evidence in support of your views.*

BT does not agree with Ofcom's provisional conclusion that there is a separate market for Standalone Fixed Voice residential calls given that there is not a specific market for corresponding access services for the reasons set out in Section 4.

*Question 4.1: Do you agree with our provisional conclusion that, during the period covered by this market review, BT will have Significant Market Power in the Standalone Fixed Voice access market? Please provide reasons and evidence in support of your views.*

BT does not agree with Ofcom's market power assessment for the following reasons:

- BT is not able to set the terms and conditions of sales for SFV services without facing competitive constraints from other providers (section 4B, paragraphs 137 – 139).
- Ofcom's market share calculations do not provide a meaningful indication of market power (section 5C, paragraphs 140–149).
- Ofcom has overstated barriers to acquisition (section 5D, paragraphs 150–162).
- Mobile has not been adequately considered as a constraint on landline services including for voice-only customers (section 5E, paragraph 163).

- Ofcom ignores important distinctions between voice-only customers and split purchasers, and there can be no suggestion that BT has market power in relation to split purchasers (section 5F, paragraphs 164–166).
- Ofcom’s pricing analysis ignores the broader context of switching to bundles which has been driven by lower incremental broadband prices (section 5G, paragraphs 167–172).

*Question 5.1: Do you agree with our provisional conclusion that, during the period covered by this market review, BT will have Significant Market Power in the Standalone Fixed Voice calls market? Please provide reasons and evidence in support of your views.*

BT does not agree with Ofcom’s provisional conclusion that BT will have Significant Market Power in the Standalone Fixed Voice calls market given that it will not have SMP in the Standalone Fixed Voice access market for the reasons given in Section 5.

*Question 7.1: Do you agree with the need to trial and test engagement remedies before implementation? Please explain your reasons for this.*

In Section 6 and the Legal instrument, Annex A, BT has provided a full response to the proposed SMP Conditions. As set out in Section 6F, paragraphs 198 to 201, even if Ofcom had adequately defined the market and appropriately assessed BT’s market power, there would be no justification for the intrusive nature of the remedies proposed.

As Ofcom recognises, behavioural remedies have the best prospect of success if implemented without a price reduction (paragraph 213).

As set out in, the measures which have the best prospect of success are limited to those measures that prompt customers to take action, by explaining the potential benefits in general terms, while assuaging concerns about potential loss, for example that switching processes are complex or likely to fail (paragraph 213). BT should lead this process with input from Ofcom (for reasons given paragraph 208).

For comments on trialling of behavioural remedies, see section 6F, paragraphs 198– 201 and the Legal instrument annex.

*Question 7.2: Do you agree that remedies focussed on improving consumer communications to increase engagement listed below offer a reasonable prospect of success in encouraging competition?*

- *information on savings;*
- *information on the switching process;*
- *introduction of a decision point; and*
- *remedies to facilitate response to this information.*

*Please explain your reasons.*

Potentially for voice only customers; BT discusses communication remedies in Section 6.

*Question 7.3: Do you agree with our conclusions that the other remedial options we have considered, namely the establishment of a customer database for marketing purposes and automatic switching within BT's tariffs, raise significant implementation risks and therefore do not warrant further consideration? If you do not agree or consider there are other options we should have considered, please provide your reasons.*

BT agrees that measures directed at establishing a customer database for marketing purposes and automatic switching within BT's tariffs, raise significant implementation risks, amongst other risks, and do not warrant further consideration.

*Question 8.1: Do you agree with our approach to determining the options for the level of price controls for Standalone Fixed Voice services? If not, please give your reasons.*

BT does not agree; Ofcom's approach to determining the options for the level of price control results in a starting price adjustment range that may have significant and unforeseen consequences.

*Question 8.2: Do you agree with our proposed basket structure if implementing a price control for Standalone Fixed Voice services? In particular, do you agree with the need for a separate sub-cap on the Line Rental within the basket? If not, please give your reasons.*

While providing flexibility to BT, which is important, the construction of the sub-cap does not recognise, for example, that BT is unable to differentiate its call and ancillary features charges between SFV customers and those customers who take a dual play bundle.

*Question 8.3: Do you agree that it would be appropriate to allow the prices in a price control basket to rise by up to consumer price index (CPI)? If not, please give your reasons.*

It is important that any control reflect inflation; however, Ofcom should give consideration to including inflation measures that include housing costs, for example CPIH.

*Question 8.4: Do you agree that we should exclude Home Phone Saver and Line Rental Plus from the price control? If not, please give your reasons.*

BT agrees that these services should be excluded given that the services are already discounted and SFV customers have made an active decision to optimise through the purchase of one or other of the two services.

*Question 8.5: Do you agree that it is appropriate for the Line Rental sub-cap to have greater price flexibility than the overall price cap to allow BT to rebalance pricing between the line rental and call prices? If not, please give your reasons.*

BT agrees that flexibility is important.

*Question 8.6: Do you agree with the services we are proposing to include in a price control remedy basket for Standalone Fixed Voice services? If not, please set out your alternative proposals and please give your reasons.*

BT understands that Ofcom has included those services, which are not discounted, and which may be purchased by SFV customers, so to that extent does not disagree. However, the design of the basket does not reflect the practical difficulties that BT faces in being unable to differentiate its charges for lines, calls and calling features as between SFV and dual play customers.

*Question 9.1: Do you agree with our proposed set of remedies for the Standalone Fixed Voice services markets, that is a price control, with a one-off adjustment set with reference to the costs of BT competitors in this market, and an obligation on BT to with work with us to explore and ultimately implement information options to promote competition? If not please set out your reasons.*

BT disagrees that Ofcom's proposed remedies are appropriate for the reasons set out in this response.

*Question 9.2: Do you agree that BT should have at least one month after the date of the statement to implement the new price structure? If not, please set out your reasons.*

BT does not have the ability to differentiate its charges for lines, calls and calling features as between SFV and dual play customers. [§<].

*Question 9.3: Do you have any additional comments on our analysis or conclusions in this consultation?*

BT's position is set out in this response, save in respect of the proposed remedies for financial reporting and publication and in respect of which BT will deal with as part of its response to Ofcom's separate consultation.

## Annex C: Oxera Report

See attached report.

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**ANNEX 14**

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# Assessing the market for standalone fixed telephone services

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Is Ofcom's approach robust from an  
economics perspective?

Prepared for  
BT

06 June 2017

Non confidential

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[www.oxera.com](http://www.oxera.com)

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## Executive summary

BT has asked Oxera to analyse whether Ofcom's approach in the standalone landline market review is robust from an economics perspective.

Ofcom's primary concern relates to the perception that customers who do not purchase fixed voice services in bundles have not benefited from competition in retail telecoms markets to the same extent as customers who do purchase bundles. In particular, Ofcom has expressed concerns with the levels of engagement displayed by customers of a voice-only service and those who purchase voice and broadband outside of a bundle—denoted as standalone fixed voice (SFV) customers.<sup>1</sup>

Ofcom has provisionally determined that the cause of these concerns is BT's position of significant market power (SMP) in a narrowly defined retail market for the provision SFV services (in regard to both access and calls). It has therefore proposed a package of remedies that includes a cut in BT's standard line rental of at least £5 per month. The line rental price would then be subject to a cap that can only rise in line with inflation. BT would also be required to work together with Ofcom to trial ways of communicating with SFV customers in order to increase their levels of engagement in the market.

However, our assessment of the evidence and arguments presented by Ofcom finds that, in so far as there is an issue of certain customer segments not benefiting from competition to the same extent as others, or differences in the level of engagement by certain consumer segments, these are market-wide features that are not caused by the actions or behaviours of a particular operator (BT in this case). We therefore conclude that it is not proportionate or reasonable to impose retail-based SMP obligations on a single provider (in this case BT) to address the alleged concerns.

Furthermore, our analysis also finds a number of shortcomings with Ofcom's approach and conclusions.

First, Ofcom fails to recognise that the pricing structure that it is concerned with (low pricing for bundles via low incremental broadband price, and relatively higher line rental prices) is a direct consequence and a rational response to intense competition in retail markets. It is also a market-wide pricing strategy. As such, the concern raised by Ofcom is not caused by the actions of a dominant operator exploiting its customers, but rather a rational response by all firms to effective retail competition for bundles.

As a result, Ofcom's approach to market definition does not provide an appropriate framework for assessing the concerns it has raised. We consider that a broader framework taking account of these market-wide pricing practices would be more appropriate, both to understand the nature of any concern, taking account of all relevant competitive dynamics, and to ensure that any intervention is appropriate and can address the identified concern in a proportionate way.

Second, Ofcom also fails to take account of how the intervention by the Advertising Standards Authority (ASA) preventing communications providers (CPs) from splitting out the line rental and broadband prices in dual play bundles will go a long way towards addressing Ofcom's alleged concerns. This is

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<sup>1</sup> See Ofcom (2017), 'BT's landline-only customers set for cheaper bills', press release, 28 February, which states as one of the headline bullet points that 'Landline-only customers are often elderly or vulnerable, unlikely to switch'.

because the incremental broadband price will no longer be the focus of competitive offers. As a consequence, CPs may lower the standalone line rental price as a further means to compete for these customers because the implicit rise in the incremental broadband price will no longer be directly visible to dual play customers, reducing the risk of uncompetitiveness in the dual play market from such a strategy.

Nevertheless, providers may still wish to balance this opportunity for greater headline price competition targeted at those who are unlikely to take up broadband, with a desire to keep implicit broadband prices low in order to drive further migration to bundles for those who might still migrate.

Third, the market identified by Ofcom is declining rapidly and may soon cease to exist altogether as a result of natural churn and continued migration to bundles. This calls into question the proportionality of reintroducing retail SMP remedies at this point.

Fourth, in relation to Ofcom's approach to market definition and market power, our analysis finds that the regulator has failed to take account of the principles of price discrimination in the context of market definition. This has implications for Ofcom's conclusion that SFV access and calls constitute separate relevant economic markets. Robustly viewed, the significant migration of SFV customers towards bundles reveals that the boundaries of the market that Ofcom has identified are not stable. This is an important condition (both theoretically and in practice) for separating relevant markets into narrow segments.

Fifth, the separation by Ofcom of split purchase and dual play customers is incorrect. Split purchase customers should be part of the same market as dual play customers: we reach this conclusion on the basis of: i) both sets of customers consuming a functionally equivalent service; ii) both sets of consumers having very similar (demographic, mobile usage, and market engagement) characteristics. Furthermore, a large number of split purchase customers are engaged in the market and are already optimising their service consumption decision. Ofcom's concerns in relation to this customer segment are, therefore, unfounded.

Having incorrectly defined narrow SFV markets, Ofcom then finds that BT has SMP. Even within these incorrectly defined markets, we find that Ofcom has not fully accounted for the competitive constraints that BT faces in respect of the voice-only customer segment. This results in an overstatement of the degree of market power that BT would have in relation to voice-only customers. In particular, BT faces constraints both from mobile substitution and from rivals with strong brands and competitive advantages, such as the Post Office, which is competing actively for voice-only customers.

As a direct result of these shortcomings, Ofcom's proposals to remedy the alleged concerns are inappropriate, for a number of reasons:

- SMP has not been properly substantiated for the reasons give above, and therefore there is no clear basis for SMP regulation;
- Ofcom's approach reduces its flexibility in choice of remedy—market-wide remedies are artificially ruled out. This is inappropriate because the concerns identified by Ofcom (although not properly substantiated) are market-wide in nature;
- the remedies that Ofcom does propose are disproportionate and would have unintended consequences. In particular, we note that:

- 
- i) Ofcom's remedies are targeted solely at standalone fixed voice customers and only at BT, when in practice, a significant proportion of the customers Ofcom is concerned about are split purchasers, who pay *the same* line rental as dual play customers. Given that the line rental is the same in the two cases (which Ofcom itself assumes in its analysis of the savings from a split purchase customer moving to dual play), the saving from moving to dual play from split purchase is attributable to a saving on the broadband component. If the saving is attributable to the broadband component, it is not immediately clear why a remedy should be applied to the line rental (voice) component. However, this is precisely what Ofcom is proposing for these split purchase customers. Furthermore, it is proposing to apply such a remedy to BT only, which has only a small (less than 20%) share of the broadband component of split purchase customers. Therefore, not only is Ofcom applying remedies to the wrong product, but to the wrong firm—BT does not have SMP in standalone broadband;
- ii) Ofcom does not appear to have considered how a deep price cut on standalone line rental might affect the migration towards dual play bundles and digital inclusion. These unintended consequences, which could include slowing migration to dual play and possibly even reversing migration (as some dual play customers decide to switch back to split purchase or even voice only) could ultimately be detrimental.

## 1 The market context

In this section we set out the relevant market context which should inform an assessment of standalone fixed voice services.

The main arguments we develop in this section are as follows.

- **Price competition occurs at the level of the wider market, and has been targeted at broadband, which provides a pro-competitive explanation for the pricing structure that Ofcom is concerned about:** we set out why competition has historically focused primarily (but not exclusively) on incremental broadband prices within a dual play bundle. This explains what we see in the market, with very low incremental broadband prices offset by line rental prices. Overall, however, competition between dual play bundle providers results in margins that are consistent with a contestable and highly competitive market.
- **Obligations recently imposed by the Advertising Standard Authority may alone address the concern Ofcom raises:** the new advertising rules (which came into force in October 2016) no longer allow operators to advertise the price of broadband separately from the inclusive (and requisite) line rental, instead the total dual play bundle price must be presented. This means that lowering line rental prices may become a further means to compete for voice-only customers alongside product innovation and discounts (although dual play providers may still balance this with promoting further uptake of bundles by keeping implicit broadband prices low). As a result, the market-wide pricing structure Ofcom has identified as being problematic for voice-only customers may be (at least partly) addressed by the new ASA rules.
- **The markets identified by Ofcom are declining rapidly:** the concern identified by Ofcom is in relation to a rapidly declining segment. As such, any concern will be transitory, which brings into question the proportionality of Ofcom's proposed remedies.
- **The concern Ofcom alleges is a market-wide feature, not BT-specific:** both the nature of competition in the market (historically based around low incremental broadband prices), and the level of engagement exhibited by certain consumer segments, are market-wide features, and are not caused by the actions or behaviours of a specific firm in the market. It is therefore not proportionate or reasonable to impose retail-based obligations on a single provider (in this case BT) to address the alleged concerns.

### 1.1 Price competition occurs at the level of the wider market, and has been targeted at broadband, which provides a pro-competitive explanation for the pricing structure we have observed

In this section we set out how competition in the wider market has focused on bundles, and why that has led to the outcome now observed, including the concern that Ofcom has raised.

## Bundling

Ofcom itself recognises that since the removal of regulation in retail voice telephony markets in 2009, many consumers have moved towards buying services in bundles and ‘this is where we have seen the focus of competition.’<sup>2</sup>

Indeed, as Ofcom notes, in 2016,<sup>3</sup> 68% of households reported buying at least two of their communication services in a bundle, with dual play packages of landline and broadband and triple play packages of landline, broadband and pay-TV being the most popular; furthermore, this percentage keeps rising.

Most starkly, almost 9 out of 10 people taking voice services do so in a bundle.<sup>4</sup> Ofcom itself notes that the number of customers who take voice services in a bundle is increasing over time.

Bundling can be beneficial to firms and consumers. The benefits of bundling are well understood; bundling can expand output, increasing efficiency relative to standalone pricing.<sup>5</sup>

Furthermore, a key consideration related to pricing by high fixed-cost, multi-product firms is the optimal recovery of costs.

For such firms, an important question is how they can efficiently recover their costs of providing the range of products and services in their portfolio.

Ofcom has long recognised the importance of efficient cost recovery, and allowing firms (even under a charge control) pricing flexibility to recover costs from different products in order to maximise overall efficiency.

## Use (historically) of low incremental broadband prices

On the basis that 9 out of 10 customers buy fixed voice as part of a bundle (and this proportion is set to increase in the future), it is not surprising that operators in the market have structured their pricing policies on the basis of bundle purchasing. This is indeed recognised by Ofcom, which notes that the incremental broadband price within a bundle has generally been the focus of competitive activity for bundles and has declined significantly.<sup>6</sup>

Broadband marketing material illustrate how operators have historically opted to present low incremental broadband prices as a marketing tool to attract consumers for whom this is a key driver, as shown in the examples below.

<sup>2</sup> Ofcom (2017), ‘The review of the market for standalone landline telephone services: Provisional conclusions’, 28 February, para. 2.2. Hereafter referred to as ‘RMSLTS’.

<sup>3</sup> Ofcom (2016), ‘Communications Market Report’, section 1.3.4, <https://www.ofcom.org.uk/research-and-data/cmrr/cmrr16> accessed 8 May 2017. Hereafter referred to as ‘CMR’.

<sup>4</sup> Currently 2.9m households take voice services outside a bundle, representing 11% of all residential landline users (i.e. including those who purchase landline services in a bundle). This means that 89% of all residential landline users take voice in a bundle.

<sup>5</sup> The use of bundling as a means of efficient price discrimination is well explored in economic literature. See, for example, Motta, M. (2004), *Competition Policy: Theory and Practice*, Cambridge University Press, section 7.3.

<sup>6</sup> Ofcom (2017), ‘RMSLTS’, para. 3.34.



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Calls to 01, 02 & 03 UK landline numbers at any time on weekends.

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+ Sky Talk & Line Rental (at £16.40 a month)

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Hurry sale ends 10 July

TalkTalk's **HALF PRICE BROADBAND SALE**

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+ £15.95 monthly line rental

**SAVE £160's BT every 12 months**

**£75 VOUCHER**

**Buy now**

TalkTalk 2014 offer

Low incremental pricing of broadband (within bundles) is likely to encourage take-up of broadband, since consumers will consider the incremental broadband price when deciding whether to add it to their fixed voice service (i.e. the price–quality trade-off referred to by Ofcom at paragraph 3.35.1).<sup>7</sup>

As such, the pricing structure that Ofcom is concerned about is clearly a key pricing (and marketing) strategy for all operators in the market. Indeed, in certain cases, broadband is given away for free—for example, Sky has offered free broadband for 12 months to customers taking up a pay-TV package with Sky Sports.<sup>8</sup> Offering a service for free acts to highlight the strategic pricing practices employed in this market.

Such practices could be used by communication providers (CPs) that wish to attract customers into one service in order to on-sell them another service. In the above example, Sky can use broadband as a 'carrot' to entice customers onto its high-margin pay-TV business.

A pricing strategy based on low incremental pricing is not unique to broadband (or telecoms markets in general). It can be seen in many markets as a strategy

<sup>7</sup> For information on incremental broadband trends, see OECD (2011), 'Broadband Bundling: Trends and Policy Implications', <http://www.oecd.org/internet/broadband/47180401.pdf>, accessed 8 May 2017.

<sup>8</sup> <http://broadbandinternetuk.com/blog/2233/sky-comnewseason-free-broadband-with-sky-sports>, accessed 8 May 2017

to expand consumption, for example to encourage the take-up of add-on services.<sup>9</sup> It also allows pricing to better reflect relative valuations for different bundle elements that might be highly differentiated between different customers.

Such strategic pricing can expand consumption and promote competition between firms and deliver benefits for customers. Indeed, this is exactly what has happened in UK retail telecoms markets, where Ofcom itself notes that the UK ranks first against close EU comparators in relation to many telecoms service metrics, including: percentage of individuals accessing the Internet at least once per week; broadband connections above 30Mbps; and the weighted average bundle pricing for fixed broadband and fixed voice services.<sup>10</sup>

In this light, it becomes clear why a firm specialising in broadband bundles (such as TalkTalk) would not wish to lower its price for landline in order to directly target voice-only customers (and would instead prefer to maintain relatively high line rental charges but very low incremental broadband prices). Doing so would hamper its ability to compete for customers of broadband bundles, which are by far the largest customer segment (equating to approximately 90% of customers, and growing).<sup>11</sup>

Such a strategy would also explain why firms in the market have moved to increase line rental in order to compete in low incremental broadband prices—i.e. it is the outcome of fierce competition for the broadband incremental price.<sup>12</sup>

From this perspective, the market outcome does not result from targeted abuse by a dominant firm, but is more a question of whether a cohort of consumers (i.e. standalone fixed voice customers) are sharing in the benefits delivered by competition as much as other groups. In other words, the issue is how the benefits of competition are being distributed and not a question of abuse of market position.

Finally, in the overall market for both voice and broadband, high levels of competition (most especially for dual play bundles) have ensured significant benefits to consumers, and margins for CPs that are not excessive (with an EBIT margin of between [x] and [x] according to Ofcom's analysis).<sup>13</sup>

Given the pricing strategy described above, and the market context in this case, it would not be appropriate to focus on the profits earned in a narrow segment of the market.

<sup>9</sup> Low incremental pricing can be seen in the transport sector, where volume discounts are prevalent. The cost of a return travel ticket is often less than that of two one-way tickets, resulting in a low incremental price for the return journey. This is good for consumers, who benefit from the lower incremental price and may choose to make more journeys as a result. Another example can be seen in the food industry, such as for cinema popcorn, whereby significantly larger bags of popcorn are sold at only slightly higher prices.

<sup>10</sup> See:

[https://www.ofcom.org.uk/data/assets/pdf\\_file/0036/79956/european\\_broadband\\_scorecard\\_2015.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0036/79956/european_broadband_scorecard_2015.pdf) accessed 8 May 2017.

<sup>11</sup> Furthermore, owing to the high level of competition in the dual play market there is little scope to undercut competitors.

<sup>12</sup> As an example, we note that TalkTalk has continually dropped the incremental broadband price (in real terms). If we take the average price paid per month over the first 12 months, we get £5.25 per month in 2010, £3.25 per month in 2013 and £0 per month in 2016. (TalkTalk offered free broadband for the first 12 months.) This change over time is matched closely by the reverse change in line rental, which increased from £11.49 in 2010, to £14.95 in 2013 and £17.70 in 2016. This information was acquired via the WayBackMachine (<https://web.archive.org/>).

<sup>13</sup> Ofcom. RMSLTS consultation, paragraph A5.81.

## 1.2 Obligations recently imposed by the Advertising Standards Authority may alone address the concern Ofcom raises




Given the above context, a key market change has occurred which creates further opportunities for competition to deliver benefits to voice-only customers: the intervention by the Advertising Standards Authority (ASA) to ensure that broadband prices cannot be advertised separately from line rental charges.<sup>14</sup> Ofcom has failed to take such market dynamic effects into account in its assessment.

The obligations imposed on broadband providers by the ASA (which came into force on 31 October 2016) stipulate that the all-inclusive dual play price (i.e. including line rental) must be presented in marketing materials without line rental being presented separately. See examples below:



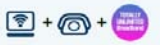


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TalkTalk website,  
April 2017

Sky website,  
April 2017

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As a result of these changes, and the new form that price competition will (and must) now take going forward (on the basis of the full dual play bundle price), the incentives to compete in the voice-only segment are materially increased, in that they are less affected by the impact on what were formerly headline incremental broadband prices.

In fact, going forward, lowering line rental prices provides a further means to compete for voice-only customers alongside product innovation and discounts (although dual play providers may still balance this with promoting further uptake of bundles by keeping implicit broadband prices low). The logic for this can be set out in four steps:

<sup>14</sup> <https://www.asa.org.uk/news/tougher-approach-to-broadband-price-claims-in-ads.html> accessed 8 May 2017.

1. the vast majority of consumers value and wish to purchase broadband. As such, it was rational for CPs to advertise the broadband component of dual play bundles at a low price. In order to maintain overall margins (which are competitively constrained), the low broadband incremental price could be offset by the line rental fee (although BT also created tailored products to protect voice-only customers from these effects, under competitive pressure from other voice-only providers);
2. one way to compete for voice-only customers would have been to reduce landline prices, and therefore increase the broadband incremental price (in order to maintain overall bundle margins). Owing to this trade-off (rebalancing), competing in the voice-only segment (of 2.9m customers, if we include split purchase customers) could inhibit a CP's contestability for the much larger (approximately 28m) dual play segment.
3. Now that dual play bundles are advertised as a single price (following the ASA requirements), price competition can no longer focus on low incremental broadband prices but rather the entire bundle price must be presented. The constituent prices for the dual play offering (broadband and voice) are, therefore, no longer relevant from a marketing perspective.
4. Given this new paradigm of price competition, headline line rental price reductions may be more likely to be used as a further means of competing in the voice-only segment. That is, CPs may now be more relaxed about an implicit increase in the incremental broadband price, to offset a decrease in the line rental price (to maintain overall margins) because it is no longer the focus of price competition, although it remains a relevant pricing parameter in driving uptake of bundles.

### 1.3 The SFV segment is declining rapidly

We set out below why, owing to the significant forecast declines in SFV customers (as a result of migration to bundles and natural churn), intervention is unlikely to be proportionate.

Ofcom notes that BT has a high share of customers (70%) in the market that Ofcom defines for SFV services.<sup>15</sup>

However, the market has been declining as consumers: switch to dual play bundles; cease to need a service altogether; or in the case of customers not requiring fixed broadband, substitute to mobile voice services from fixed (for either calls or access).<sup>16</sup>

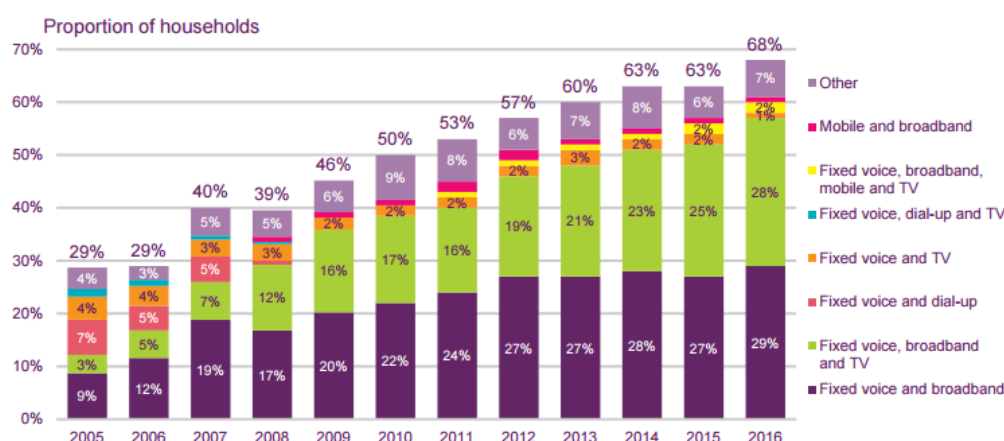
Ofcom notes that the rate of year-on-year decline has been decreasing.<sup>17</sup> However we anticipate that the base will continue to decline, particularly as the SFV base continues to migrate to bundles. This is in line with Ofcom's own analysis which demonstrates the growing trend of consumers taking bundled services and in line with historical trends. We present this in Figure 1.1 below.

<sup>15</sup> This is an average across all SFV customers. It is made up of a lower share of voice-only customers, around 60%, and a higher share for split purchase customers. However, as we set out in section 2.2, the latter should not be included in this narrow market, and therefore the figure of 70% is inflated.

<sup>16</sup> As Ofcom points out, the number of SFV lines decreased from 6.1m in Q1 2013 to 2.9m in Q3 2016—i.e. by 52%. See Ofcom (2017) 'RMSLTS', para. A8.15.

<sup>17</sup> For the market as a whole Ofcom calculates a decrease in the rate of decline from 23% in the year before Q4 2014 to 15% in the year before Q3 2016. For BT, Ofcom calculates a smaller decrease, from 25% in the year before Q1 2014 to 17% in the year before Q3 2016. Ofcom notes in particular that BT's rate of decline is on average 11 percentage points faster than that of other CPs. See Ofcom (2017), 'RMSLTS', para. A8.17.

Figure 1.1 Take-up of bundles services



Source: Ofcom (2016), 'RMSLTS', Figure 1.6.

In addition to the strong trend of customers migrating to bundles, we also note that the SFV segment is characterised by a degree of natural churn. The SFV customer base has a high proportion of elderly customers (see RMSLTS, Figure A8.47). In particular, among respondents whose age was known, more than a third were 80 years of age or older.<sup>18</sup> At the same time, younger customers are less likely to buy SFV services. Indeed, respondents less than 44 years of age accounted for a mere 8% of responses. This suggests that the SFV customer base will decline substantially on the basis of remaining life expectancy.<sup>19</sup>

In light of the above, and making a number of conservative assumptions,<sup>20</sup> we estimate that the proportion of SFV lines over the total line rental lines in the market will almost halve by the end of 2020 (to less than 6.5% of total lines).<sup>21</sup> On this basis we consider that the market is likely continue to decline rapidly as a result of both continued switching and natural churn.

We also note that Ofcom has set a precedent for deregulating declining market segments; that is, where Ofcom has identified a market power issue, and still chosen not to regulate.

In the 2016 BCMR, for example, Ofcom concluded that deregulation was appropriate on the basis of the decline in the use of legacy leased lines:<sup>22</sup>

given the context that this is a legacy market, with rapidly declining volumes, we consider that it is appropriate to rely on ex post competition law rather than imposing ex ante regulation. Consequently, we have decided that the three

<sup>18</sup> That is, 31% out of the 92% of respondents who provided information on their age. It is also worth noting that elderly respondents might be more likely than younger respondents to refuse to provide information about their age. See Ofcom (2017), 'RMSLTS', Figure A8.47.

<sup>19</sup> For example, 17% of respondents whose age is known are 85 years of age or above. In 2014, of the total number of death registrations among this age group, 29% were between 85 and 87 years of age and 47% were between 85 and 89 years of age.

<sup>20</sup> For example, assuming the rate of decline in the SFV base continues to reduce for the next two years in line with historical trends, and that total fixed voice lines will grow in line with the growth in the number of households in the UK.

<sup>21</sup> Assuming that the decline in SFV churn continues (as Ofcom states), and as such there remain some 1.8m SFV customers by the end of 2020, relative to 28.4m total retail lines.

<sup>22</sup> Ofcom notes that BT has 'a high share of the supply of retail VLB TI (very low bandwidth traditional interface) leased lines'. See Ofcom (2015), 'Business Connectivity Market Review: Very low bandwidth leased lines', para. 5.17, [https://www.ofcom.org.uk/data/assets/pdf\\_file/0033/69378/vlb\\_ti\\_retail\\_market.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0033/69378/vlb_ti_retail_market.pdf), accessed 5 May 2017. As such, this example presents a similar context to the case at hand.

criteria test is no longer satisfied and this market therefore is no longer susceptible to ex ante regulation.<sup>23</sup>

Furthermore, Ofcom also highlighted in this case that the trend of migration to other/better services (deemed to be competitive) was an important factor in its decision to deregulate:

as users can and are migrating to alternative services, and will increasingly do so over the market review period, any barriers to, and prospects for, the competitive provision of retail VLB services are now less relevant (para. 5.19)

The SFV segment is also small and declining, raising questions about the duration of any alleged issues identified by Ofcom, as well as the proportionality of any proposed intervention.

#### **1.4 The alleged competition concern identified by Ofcom is market-wide, not BT-specific**

As set out in section 1.1, the pricing strategy historically observed in the market (based on low incremental broadband prices) is market-wide.

Furthermore, Ofcom's alleged concern—that 'Standalone landline customers generally do not engage with the market'<sup>24</sup>—is not a BT-specific issue, but a market-wide one (to the extent that it exists).

Other CPs are, therefore, highly relevant to any discussion about improving customer engagement for specific customer groups particularly in relation to split purchasers where BT holds a small market share of standalone broadband (as we discuss in section 2.5.1).

As regards any demand side considerations relating to customer engagement, it is not appropriate to apply an analytical framework that singles out one operator, when in fact any issue of this nature (which Ofcom has not properly substantiated) affects all operators, and does not relate to an abuse of market power (i.e. customers can be disengaged for reasons other than CPs abusing a strong market position).

Ofcom bases its finding that BT should be the target of SMP remedies on the data on engagement levels. It claims that the data shows that BT customers are 'less engaged compared to customers of other CPs'.<sup>25</sup> Ignoring the low sample size, we note that the data Ofcom presents does not support this conclusion. This is because BT has a high share of SFV customers (historically and currently); as such, the data presented by Ofcom distorts the indication of engagement between BT and other CPs.

If we imagine the stylised example of BT having 100 customers and TalkTalk having 10, and we assume that each year 10% of consumers switch provider (i.e. all consumers are equally engaged, regardless of their service provider), we would expect 10 of BT's consumers to switch to TalkTalk this year, and 1 TalkTalk consumer to switch to BT.

In this example, using Ofcom's formulation of the data (which it presents in Figure A8.52), Ofcom would say that 53%<sup>26</sup> of TalkTalk's customers are

<sup>23</sup> Ofcom (2016), 'Business Connectivity Market Review: Very low bandwidth leased lines', Statement, 28 April, para 3.22. [https://www.ofcom.org.uk/data/assets/pdf\\_file/0018/63225/final-statement.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0018/63225/final-statement.pdf), accessed 5 May 2017.

<sup>24</sup> Ofcom (2017), 'RMSLTA', para. 1.13.

<sup>25</sup> Ofcom (2017), 'RMSLTA', para. A8.156.

<sup>26</sup> (10/19)=53%.

engaged (i.e. have switched in the last 12 months), whereas only 11%<sup>27</sup> of BT's customers are engaged. This statement distorts the reality in this example that all customers are equally engaged (irrespective of provider), and it is simply a result of asymmetry in the market shares that leads to an apparent asymmetry of engagement.

For the reasons above, many regulators have sought to tackle competition problems of this nature not by changing market structure but by stimulating greater customer engagement across the whole market.<sup>28</sup>

### 1.5 Oxera's conclusion on the market context

We conclude that the concern Ofcom raises has likely arisen as a result of the historical pro-competitive pricing policies of CPs, which have opted to employ bundled pricing strategies, whereby broadband prices are marketed at a very low price.

Many millions of customers who were once SFV customers have migrated to dual play and thereby benefited from this price competition. For SFV customers who have not yet switched (the number of whom is continually declining), the question posed by Ofcom is whether they are sufficiently engaged, and able to access and realise the benefits of competition to the same extent as dual play customers, within both the SFV segment and the wider market.

We consider that it is not appropriate to attribute any competition issues arising from a lack of customer engagement to SMP for a particular operator (in particular, BT). Such issues are market-wide; observed outcomes reflect pro-competitive strategies as the market has evolved towards almost ubiquitous take-up of bundles, and any issue of this nature is unlikely to persist in any event. This is because, not only is the market declining rapidly (meaning that it may not be proportionate to intervene at all), but new regulations imposed by the ASA mean that bundle pricing policies that historically have placed significant emphasis on incremental broadband prices are no longer permitted.

As a result, there is a greater opportunity to compete for voice-only customers using headline line rental prices alongside other means of competing for these customers.

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<sup>27</sup> (1/91)=11%.

<sup>28</sup> In section 2.1.3 below we describe recent examples in energy, retail banking and payment protection insurance.

## 2 Ofcom has reached the wrong conclusions on market definition and SMP

In this section we assess and critique the approach taken by Ofcom in respect of market definition and SMP. This is notwithstanding the overall conclusion we have reached in the previous section regarding the fact that an SMP framework is the wrong tool to address the alleged concerns Ofcom has identified.

Ofcom arrives at its final market definition via three steps:

1. dual play customers are not in the same market as voice-only customers. RMSLTS, paras 3.30–3.38;
2. dual play customers are not in the same market as split purchasers. RMSLTS, paras 3.39–3.43;
3. split purchase customers are in the same market as voice-only. RMSLTS, paras 3.44–3.53

On this basis, Ofcom concludes that the relevant market in this case is one that includes both voice-only and split purchase customers, which it terms ‘SFV’.<sup>29</sup> Ofcom then concludes that BT has SMP over this market on the basis of an analysis of market shares and BT’s profits for such customers.

In our view (and on the basis of our analysis in section 1), a perfectly reasonable and valid way for Ofcom to have defined the market would have been as a wider voice market including all of voice-only, split, and bundle customers, while recognising, if necessary, that different segments exist, based on preferences for broadband, willingness to pay, and levels of engagement in the market. This would be consistent with the approach adopted by the Competition and Markets Authority (CMA) in the context of market investigations conducted in the energy markets and by the FCA and the CMA for certain financial services products (see examples in section 2.1.3).

In such a broadly defined market, BT would not have SMP. This does not preclude the possibility that market outcomes cannot improve, but this is a different question, unrelated to an SMP finding, which would require a market-wide assessment and consideration of whether market trends will quickly render any concerns *de minimis*.

Ofcom has not taken such a view, and instead has chosen (incorrectly in our view) a more granular route to defining relevant markets. In this section we set out an economic assessment of the approach taken by Ofcom.

In section 2.1 we set out some of the general shortcomings of Ofcom’s approach, including the following.

- Ofcom’s approach to market definition does not provide an appropriate framework for assessing the issues that Ofcom has identified, and therefore weight cannot be placed on the provisional conclusions that Ofcom has reached. A broader market-wide framework would be a more appropriate approach.
- Ofcom misapplies the principles of price discrimination in conducting its analysis.

<sup>29</sup> Ofcom defines separate markets for access and calls, but this does not affect the analysis or findings of this report.



- In section 2.2 we present evidence that split purchase customers are in the same market as dual play customers and therefore Ofcom is incorrect in its SFV market definition.
- In section 2.3 we set out how Ofcom has overstated the concerns in relation to split purchase customers, given that many such customers are switching and appear to be already optimising across the services they consume.
- In section 2.4 we show that Ofcom has overlooked the competitive constraints that BT faces in respect of the voice-only customer segment resulting in an overstatement of the degree of market power that BT would have under Ofcom's (narrow) market definition.
- In section 2.5 we show the limitations of using an SMP approach in relation to the remedial action that can be used to address any concerns— this limitation is demonstrated by the fact that Ofcom's remedy proposals do not actually address its concerns, are disproportionate and will have unintended consequences:
  - Ofcom's proposed remedies for split purchasers do not address the cost of standalone broadband;
  - Ofcom has not addressed the impact of the proposed remedies on the migration to dual play bundles and digital inclusion.

## 2.1 Ofcom's approach has a number of shortcomings

According to Ofcom, the approach to market definition should keep in mind the end-goal of assessing the competitive constraints faced by firms and the necessity of regulatory interventions:

The market definition exercise is not an end in itself, but a means to assessing whether there is effective competition and thus whether there is a need for ex ante regulation.<sup>30</sup>

There are, however, different approaches to market definition. We show below that a different approach would have given Ofcom a richer understanding of the market in question and a more appropriate framework for assessing any competition issues.

In particular, understanding SFV customers as segments of a wider market, rather than hypothesising artificially narrow markets, would enable Ofcom to more accurately assess the nature of competition and relevant interactions between segments (which are not properly captured by Ofcom), as well as the effects of any ex ante regulation (including potentially adverse effects).

Below we expand on a number of key flaws in Ofcom's approach. These can be summarised as follows:

- Ofcom's approach to market definition does not provide an appropriate framework for assessing the issues that it has identified—in particular, the level of market engagement by SFV customers;
- Ofcom overlooks the significant decline in the SFV market segment, which undermines the narrow-market SMP approach;

<sup>30</sup> Ofcom (2017), 'RMSLTS', para. 3.7, p. 15.

- markets do not need to be concretely defined in order for the regulator to comprehensively analyse the competitive constraints on different market players and how this delivers benefits to different customer segments;
- price discrimination between dual play customers and SFV customers is not necessarily proof of these two customer segments being in separate markets.

### **2.1.1 Ofcom's approach to market definition does not provide an appropriate framework for assessing the issues that Ofcom has identified**

Ofcom's primary concern is the levels of engagement displayed by SFV customers:<sup>31</sup>

Survey evidence suggests that SFV customers have relatively low levels of engagement in the market (para. 4.8)

There are significant challenges in effectively communicating with consumers who are not actively engaged in the market. (para. 1.25)

[...] which limit the ability of other communications providers (CPs) to compete effectively and expand in the market (para. 7.3)

Our aim in imposing [...] measures is to allow other providers to compete more vigorously in this market and to win customers. If the engagement remedies we are proposing are effective, we would expect consumers to benefit in terms of price and choice (para. 1.26)

As we have explained in further detail in section 1 above, to the extent that this is an issue, it is a problem that affects not only BT customers but all consumers; in short, it is a market-wide issue.

Ofcom's approach erroneously labels this market-wide issue as an SMP issue, and one applicable only to BT.

### **2.1.2 Ofcom gives insufficient weight to key factors relevant to market definition**

As also explained in section 1, Ofcom has overlooked the significant decline in the SFV market segment, and implies that the remaining customers are more inert than those who have moved to dual play bundles.<sup>32</sup> However, the SFV market will decline significantly over the coming years, as explained in section 1.3.

A claim that the remaining SFV customers would not continue to switch would necessarily imply that there is a change in the nature of the customers. That is, current SFV customers are less engaged than those who have already switched to dual play bundles. However, it is not clear from Ofcom's analysis that this is the case, and there is no reason to believe that the rate of decline of the SFV base will materially slow down going forward. Indeed, only 5% of SFV customers state that they do not want or need broadband.<sup>33</sup>

<sup>31</sup> See Ofcom (2017), 'BT's landline-only customers set for cheaper bills', press release, 28 February, which states as one of the headline bullet points that 'Landline-only customers are often elderly or vulnerable, unlikely to switch'.

<sup>32</sup> Ofcom (2017), 'RMSLTS', para. 3.41.3, p. 24.

<sup>33</sup> Jigsaw (2016), 'Narrowband Review 2016', November, Figure 15, p. 22.

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### **2.1.3 A broader market framework would provide a richer understanding of the competitive dynamics and how to address any alleged concerns**

While it may be legitimate to investigate levels of customer engagement, this has nothing to do with the behaviour of an individual firm (or indeed a collection of firms).

Any such assessment would start from the view of a broad market and would consider whether less-engaged customer segments are benefiting as much from the highly competitive retail voice market as groups who are more engaged.

Boxes 2.1 and 2.2 detail two recent examples of where the CMA has analysed markets including customer engagement issues on a market-wide basis, without the need to define narrow markets including the customer groups of concern or to identify SMP (individually or collectively).

The key messages of these case studies are:

- markets do not need to be concretely defined for the regulator to comprehensively analyse the competitive constraints on different market players and within the particular market segments;
- a market-wide assessment (as opposed to the SMP framework) enables the application of more effective and flexible (market-wide) remedies, which can better address concerns around customer engagement. (For example, disengaged customers with the Post Office and other providers such as KCom would not be addressed under Ofcom's SMP analytical framework.)

**Box 2.1 CMA energy market investigation**

Consider the recent example of the 2016 CMA investigation into the energy market.<sup>34</sup> While it did consider different aspects to market definition, the CMA preferred to view the energy market as a broad market with different market segments. Some of these market segments had lower levels of customer engagement and remedies were targeted at these groups. The CMA did not use the SSNIP test to show narrow markets, and did not conclude on SMP. This is a more suitable approach when considering differing levels of customer engagement in a broad market.

The CMA's summarises its approach as:

Defining the market provides a framework for the assessment of the effects on competition of features of a market. Market definition is a useful tool, but not an end in itself, and we note that the boundaries of the market do not determine the outcome of our competitive assessment in any mechanistic way. Notably, in some cases, where we consider that competitive pressures differ between different types of customer, we identify discrete customer segments within markets.<sup>35</sup>

Therefore it concluded that, while certain groups of identifiable customers were less engaged (those on standard variable tariffs, SVT) and while there was evidence of price discrimination:

customers do not fall into discrete camps of 'engaged' and 'disengaged'. There is a variety of degrees of engagement, and some domestic customers are relatively active before defaulting to an SVT. We therefore did not think that customers subscribing to SVT and non-standard tariffs were sufficiently distinct to warrant defining separate markets for them.

Accordingly, our conclusion is that customers subscribing to an SVT and those subscribing to non-standard tariffs fall into different market segments of the domestic retail markets, in the light of the different intensity of competition to which they are subject.<sup>36</sup>

This approach gave the CMA more flexibility in understanding the market dynamics and enabled it to target remedies at all SVT customers.

Thus Ofcom's SMP approach has limited Ofcom's flexibility regarding remedy options. The remedy options left available to Ofcom are disproportionate and fail to deal with the market-wide issue.

Source: Oxera.

<sup>34</sup> Competition and Markets Authority (2016), 'Energy market investigation', Final report, 24 June. <https://assets.publishing.service.gov.uk/media/5773de34e5274a0da3000113/final-report-energy-market-investigation.pdf> accessed 8 May 2017.

<sup>35</sup> Ibid., para. 27.

<sup>36</sup> Ibid., paras 3.33–3.34.

**Box 2.2 CMA retail banking market investigation**

Another example is the 2016 retail banking market investigation by the CMA.<sup>37</sup> Here the CMA identified one broad market, without defining separate markets for different types of personal current account. The CMA's starting point was as follows:

The guidelines also state that, in some cases, the CMA may treat a group of product, geographic or other types of markets together for the purposes of assessing competitive effects. This can be the case where a feature manifests itself in a similar way across several different markets (for example, the need for an operating licence may be an aspect of many local markets) and the CMA is able to reach a view about the effects of the feature on competition across the group of markets as a whole. Thus we are not required to identify the narrowest possible market(s).<sup>38</sup>

The CMA found that different customer segments paid different prices,<sup>39</sup> and that some customer segments were making more of a contribution to common costs than other segments (although all segments were covering incremental costs).<sup>40</sup> Notably, some of the banking providers submitted to the CMA that they were able to identify customers according to whether they were active or inactive, and therefore could price-discriminate between customer segments.<sup>41</sup> The CMA agreed that price discrimination was occurring, although with some limitations.<sup>42</sup>

Despite finding varying degrees of customer engagement and the presence of price discrimination, the CMA did not identify narrow markets and was able to target remedies at customer segments that raised the most concern. The CMA was able to make the remedies market-wide (with a de minimis threshold).

Source: Oxera.

Box 2.3 discusses the payment protection market investigation by the Competition Commission, and illustrates that disengaged customers are usually a market-wide problem.

**Box 2.3 Competition Commission investigation into payment protection insurance**

A 2009 investigation into payment protection insurance (PPI) found that consumer engagement was so low for the purchase of PPI that all suppliers had market power over their own customers. This was because PPI was an add-on (a secondary market) and thus consumers tended not to shop around when deciding whether to purchase it.

Thus the problem of disengaged customers was identified as a market-wide issue: PPI providers had market power over their customers (as the customers were not shopping around). Specifically, the Competition Commission found barriers to consumer searching, including: the time-consuming nature of obtaining quotes; difficulty in making comparisons between providers; complexity of the products on offer; and misperceptions of the benefits of the products. The Commission also found barriers to switching, poor consumer awareness of PPI products and that the high marketing costs associated with attracting PPI customers acted as a barrier to entry.<sup>43</sup>

Therefore the remedies were also market-wide, rather than imposed only on the larger PPI providers. This ensured that no disengaged customers were ignored.

Source: Oxera.

<sup>37</sup> Competition and Markets Authority (2016), 'Retail banking market investigation', Final report, 9 August. <https://assets.publishing.service.gov.uk/media/57ac9667e5274a0f6c00007a/retail-banking-market-investigation-full-final-report.pdf>, accessed 8 May 2017.

<sup>38</sup> *Ibid.*, para. 4.7.

<sup>39</sup> *Ibid.*, para. 5.73.

<sup>40</sup> *Ibid.*, para. 9.135(d).

<sup>41</sup> *Ibid.*, para. 10.24.

<sup>42</sup> *Ibid.*, para. 10.51.

<sup>43</sup> *Ibid.*, para. 3.139.

### 2.1.4 Ofcom misapplies the principles of price discrimination

This section shows that price discrimination between dual play customers and SFV customers is not necessarily proof of these two customer segments being in separate markets.

Price discrimination is a practice in many markets, as is the presence of consumers with heterogeneous preferences. Price discrimination is neither a necessary nor sufficient condition for the definition of a separate market. Accordingly, the 2013 Competition Commission Market Investigation Guidelines state that:

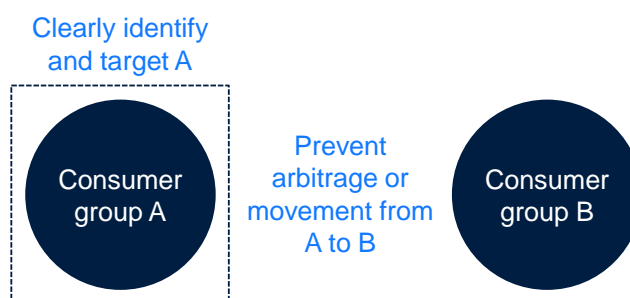
Many markets serve a diverse customer base, for example suppliers may have both business and personal customers. One set of customers may be more affected than others by any particular feature. Where such diversity exists, and where suppliers can charge different prices to different groups (ie price discriminate), the CC will recognize these differences. In terms of market definition, depending on the market and the evidence presented, the CC may choose either to treat these different groups as separate markets, or as segments within one market, noting the scope for price discrimination between different groups within the market<sup>44</sup>

Price discrimination could be used to define separate markets if a hypothetical monopolist could impose a SSNIP on a consumer group (rather than the whole market). That is, if the hypothetical monopolist could use price discrimination to segment markets. As shown by Hausman, Leonard and Velturo (1996),<sup>45</sup> price discrimination<sup>46</sup> can occur only when certain conditions are met:

- different groups of consumers have different elasticities of demand;
- the different consumer groups can be accurately identified and targeted by the hypothetical monopolist. Even small amounts of uncertainty in identifying consumer groups can preclude profitable price discrimination;
- profitable arbitrage of the product between the consumer groups is not possible.

This is illustrated in Figure 2.1. Here consumers groups A and B may be separate markets.

**Figure 2.1 Price discrimination as segmentation strategy**



Source: Oxera.

<sup>44</sup> Competition Commission (2013), 'Guidelines for market investigations: Their role, procedures, assessment and remedies', CC3 (Revised), April, [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/284390/cc3\\_revised.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/284390/cc3_revised.pdf), accessed 8 May 2017.

<sup>45</sup> Hausman, J. A., Leonard, G. K. and Velturo, C. A. (1996), 'Market definition under price discrimination', *Antitrust Law Journal*, 64.

<sup>46</sup> Specifically, third degree price discrimination.

However, in the case at hand which is the focus of Ofcom's market review, the third condition does not hold: customers are encouraged to arbitrage.

### Price discrimination as a migration strategy, not a segmentation strategy

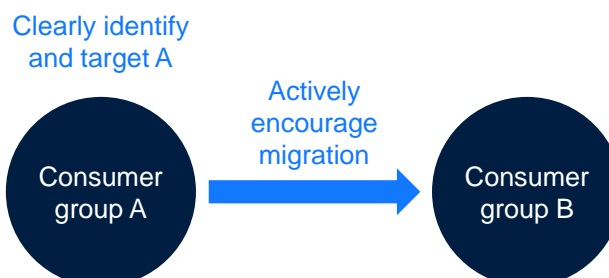
A core assumption of Hausman et al. (1996) is that the hypothetical monopolist finds it profitable to separate the consumers and keep the groups apart. In the case of the landline market, it is the express strategy of the CPs to migrate customers from one customer group to the other (SFV to dual play). Price discrimination is a migration strategy, not a market segmentation strategy.

Indeed, Ofcom acknowledges that the migration strategy is consistent with the evidence:

Offering competitive dual-play prices alongside line rental price increases may be a more effective way for SFV suppliers (or a hypothetical monopolist in SFV) to compete for voice-only customers who are considering buying fixed broadband as well, compared to keeping line rental prices lower. This would be consistent with the historical pattern of price changes.<sup>47</sup>

The use of price discrimination to migrate customers is a qualitatively different strategy to that of market segmentation. Under a market segmentation strategy the hypothetical monopolist would actively try to prevent arbitrage between the consumer groups. Under a migration strategy, the arbitrage opportunity is highlighted to consumers to encourage switching—indeed, the creation of the arbitrage opportunity is the very *purpose* of the price discrimination. This is shown in Figure 2.2.

**Figure 2.2 Price discrimination as migration strategy**



Source: Oxera.

Additionally, the inability to prevent arbitrage means that Ofcom's proposed price cut could have a detrimental effect on the migration to bundles—dual play customers would have the incentive and ability to 'unbundle' and return to split purchases if their valuation for broadband no longer exceeds the implicit incremental broadband price which is increased as a result of the price control.

In summary, Ofcom correctly identifies that price discrimination is ongoing between SFV customers and dual play customers. However, a careful analysis of this pricing strategy reveals that it is evidence of a broad market, rather than separate narrow markets.

## 2.2 Split purchase customers should be in the same market as dual play

In this section we set out why split purchase customers are in the same market as dual play customers. This is on the basis of the following:

<sup>47</sup> Ofcom (2017), 'RMSLTS', para. 3.36.5, p. 22.

- split purchaser and dual play customers consume functionally equivalent services;
- split purchaser and dual play customers have very similar characteristics in terms of demographics, engagement levels and switching activity,

We set each of these out in more detail below.

### **2.2.1 Split purchaser and dual play customers consume functionally equivalent services**

Split purchase customers are by definition purchasing landline and fixed broadband services. In other words, the products consumed are functionally equivalent to those consumed by dual play customers. This means that:

- CPs are able to offer broadband on the basis of split purchase or dual play;
- split purchase customers can switch to dual play bundles without losing either of the services they consume. Similarly, dual play customers might wish to switch back and unbundle (although the strategy of price discrimination is aimed at preventing this, see above).<sup>48</sup>

From the perspective of consumers wishing to have broadband, they do not experience any service difference from a split or dual play service. The quality of the service will be alike.

### **2.2.2 Split purchase customers and dual play customers have very similar consumer characteristics**

Ofcom's research highlights that split purchase customers and dual play customers are very similar in terms of a number of key features, such as:

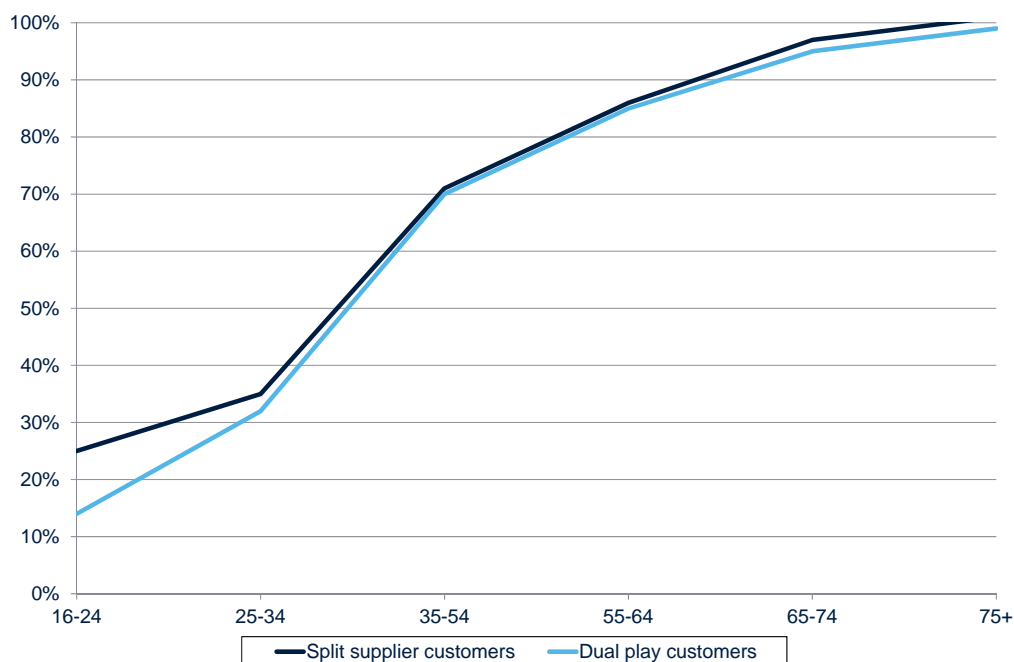
- demographics;
- engagement levels and switching activity;
- mobile usage and degree of substitutability.

#### **Demographics**

Using Ofcom's own analysis, we can see that split purchase customers have very similar demographics to those of dual play customers. First, split purchase customers have a very similar age distribution to dual play customers (see Figure 2.3). The most significant difference between the segments is that there are more split purchase customers in the youngest category (16–24-year olds).

<sup>48</sup> While a particular CP may disallow its consumers from unbundling its dual play services (i.e. becoming a split service customer), it would not be able to stop a customer using another CP's standalone products (i.e. becoming a split provider customer).

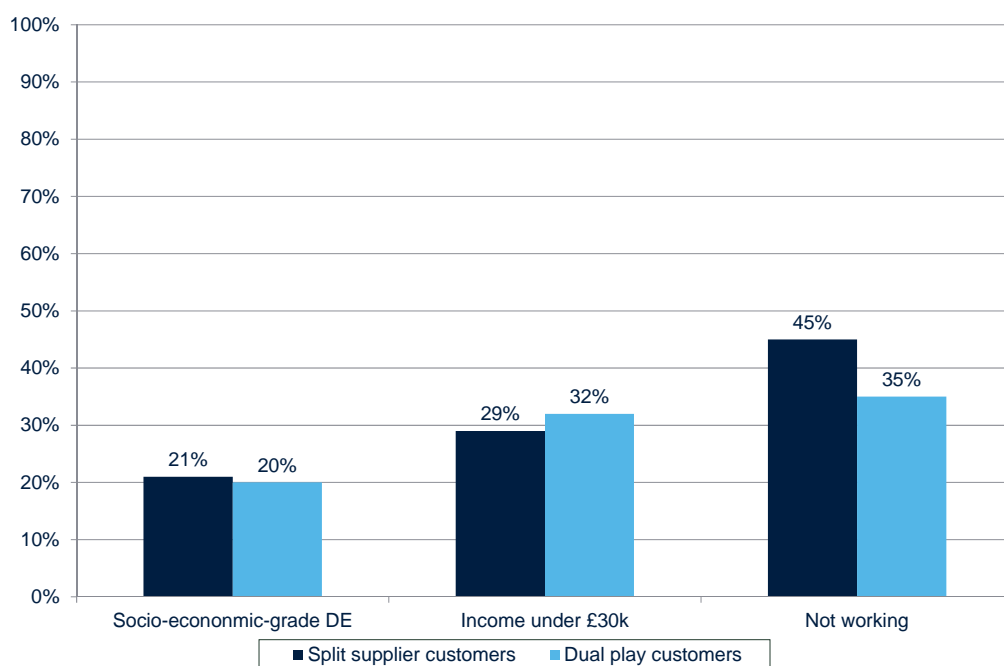


**Figure 2.3** Cumulative age distribution of landline customers

Note: The total does not sum to 100% due to rounding. Split purchase supplier data collected by Jigsaw survey rather than split purchaser, but this should be representative of the split purchaser consumer group—see Ofcom (2017), ‘RMSLTS’, Annex Footnote 191. Split supplier customers purchase their standalone voice from one provider and standalone fixed broadband from another provider.

Source: Ofcom (2017), ‘RMSLTS’, Table A8.49.

Second, split purchase customers have very similar socio-economic distribution to dual play customers, with a similar level of income and a similar proportion in work. As shown in Figure 2.4, the proportion of customers who are in the lowest socio-economic grades DE is almost identical for split purchaser and dual play customers, as is the proportion who earn less than £30,000 per year. The proportion who are working is broadly similar, although lower for split purchaser customers.

**Figure 2.4** Proportion of landline customers who are less wealthy

Note: Split supplier data collected by Jigsaw survey rather than split purchaser, but this should be representative of the split purchaser consumer group—see Ofcom (2017), ‘RMSLTS’, Annex Footnote 191.

Source: Ofcom (2017), ‘RMSLTS’, Tables A8.49 and A8.50.

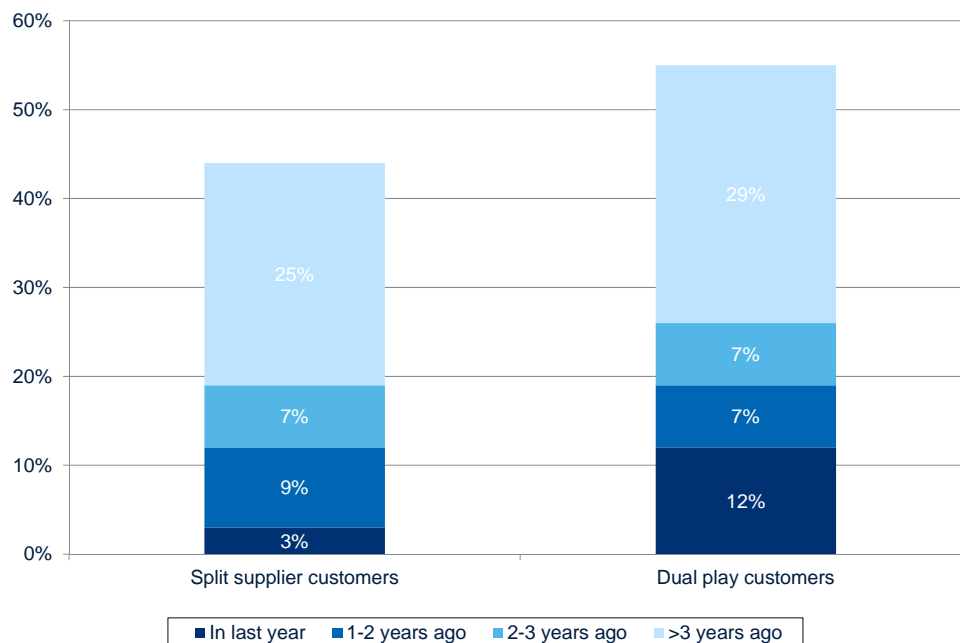
### Engagement levels and switching activity

Split purchase customers and dual play customers also show similar levels of engagement and switching activity. We present Ofcom’s analysis in Figure 2.7, noting that the levels of switching are broadly similar—26% of dual play customers have switched in the past 3 years; for split purchase customers this is 19%.

First, according to Ofcom’s research, significant numbers of split purchase customers have switched supplier, although the switching rate is stated as lower than that of dual play customers. We present this data in Figure 2.5 below. This, however, misses a key point. A significant proportion of split purchaser customers have already switched to dual play bundles over the last few years. The statistics will therefore display such (previously split purchase) consumers as now consuming dual play bundles. The switching of these formerly split purchase customers to dual play will appear in the chart as switching undertaken by current dual play customers.

The statistics shown in Figure 2.5 therefore underestimate the level of switching among split purchase customers. However even on the basis of the figures, we note that split purchase customers do exhibit a material amount of switching—almost 20% have switched in the last 3 years, compared with 26% for dual play customers.

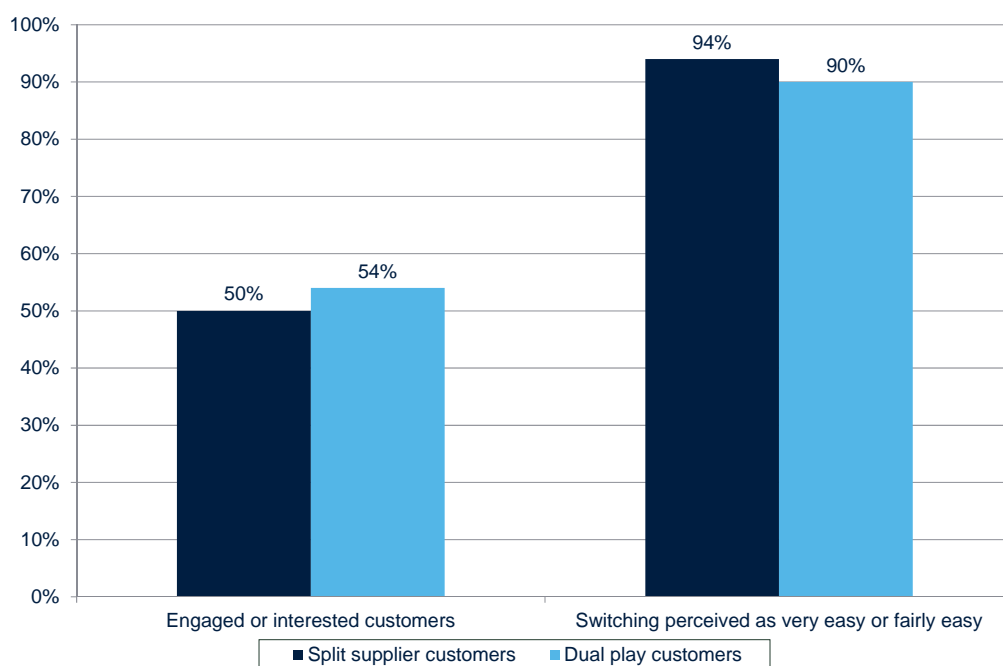
**Figure 2.5 The proportion of customers who have switched landline provider**



Note: Split supplier data collected by Jigsaw survey rather than split purchaser, but this should be representative of the split purchaser consumer group—see Ofcom (2017), ‘RMSLTS@ Annex Footnote 191.

Source: Ofcom (2017), ‘RMSLTS’, Table A8.57.

Second, self-reported levels of engagement are similar across dual play and split purchase customers, as is the perceived ease of switching. This is shown in Figure 2.6 below.

**Figure 2.6 Engagement levels and perceptions of switching**

Note: Split supplier data collected by Jigsaw survey rather than split purchaser, but this should be representative of the split purchaser consumer group—see Ofcom (2017), 'RMSLTS', Annex Footnote 191.

Source: Ofcom (2017), 'RMSLTS', Table A8.51 and Table A8.60.

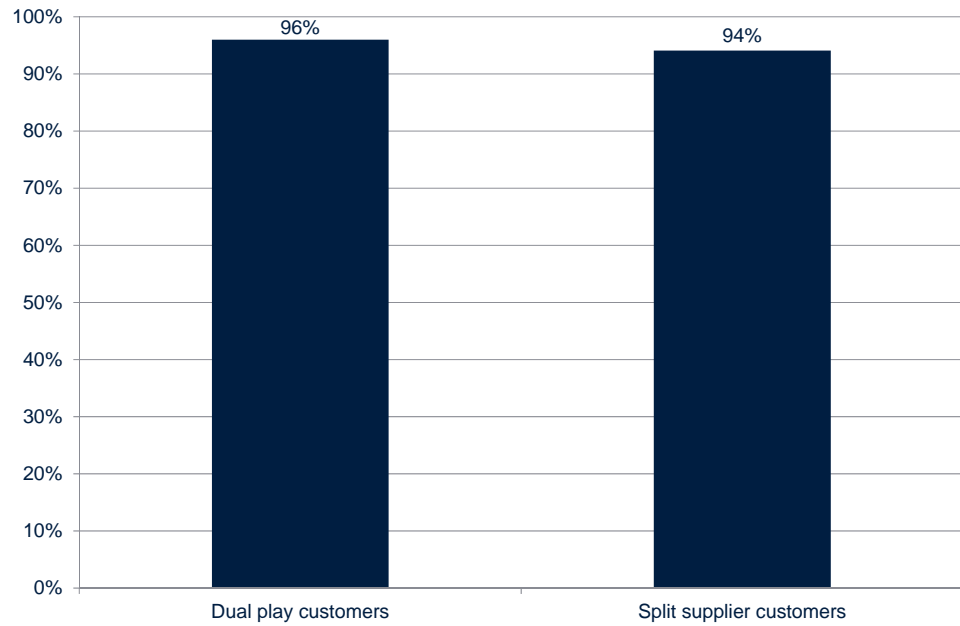
In summary switching activity or levels of engagement are broadly comparable between split purchaser and dual play customers. This further supports the view that both groups of customers should be considered as part of the same market.

### Mobile usage and degree of substitutability

Mobile services place a competitive constraint on the providers of fixed landline services. Indeed, the proportion of split purchase customers who own a mobile phone is nearing saturation.

The data (presented in Figure 2.7) shows that when compared with dual play customers, a very similar proportion of split purchase customers have a mobile phone. We also note that the majority of split purchase customers have smartphones (71%).<sup>49</sup>

<sup>49</sup> Jigsaw market research for Ofcom Narrowband Review 2016, residential survey (wave 1) table 906 (pp. 1443).

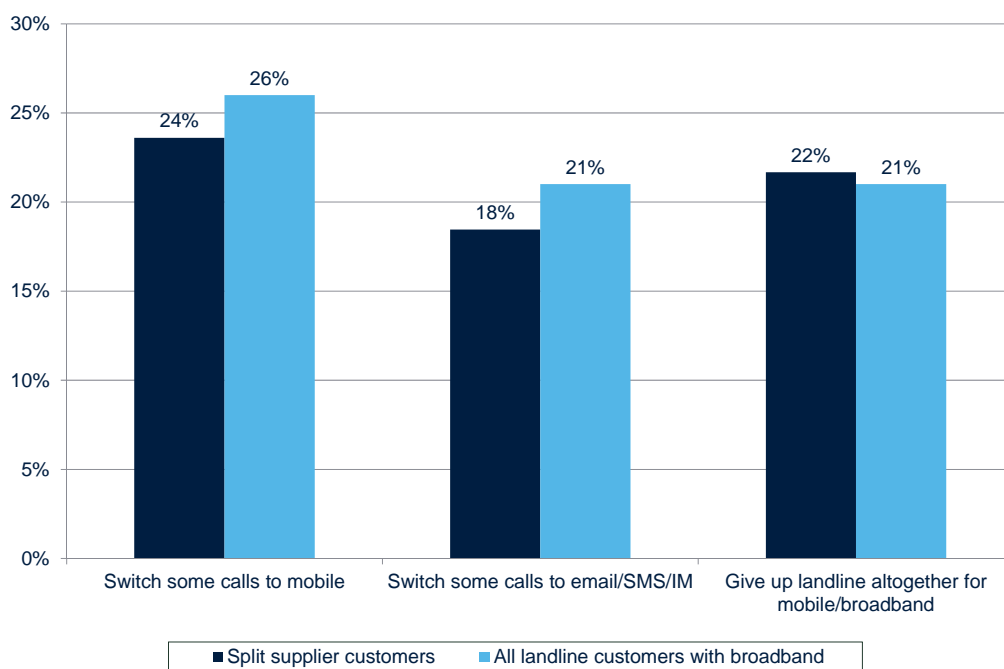
**Figure 2.7** Proportion of customers who own a mobile phone

Note: Split supplier data collected by Jigsaw survey rather than split purchaser, but this should be representative of the split purchaser consumer group—see Ofcom (2017), ‘RMSLTS’, Annex Footnote 191.

Source: Jigsaw market research for Ofcom Narrowband Review 2016, residential survey (wave 1), table 908 (p. 1485); and Ofcom (2017), ‘RMSLTS’, para. A8.149.

Additionally, very similar proportions of dual play customers and split purchase customers would respond to a SSNIP on their landline bill by switching some or all of their calls to mobile services (see Figure 2.8 below).

**Figure 2.8** If overall landline bill price increases by 10%, what proportion of customers would be likely to...



Note: Split supplier data collected by Jigsaw survey rather than split purchaser, but this should be representative of the split purchaser consumer group—see Ofcom (2017), 'RMSLTS', Annex Footnote 191. 'SMS': text messaging; 'IM' instant messaging.

Source: Jigsaw market research for Ofcom Narrowband Review 2016, residential survey (wave 1) data tables, tables 633 (p. 1011), 661 (p. 1048), and 908 (p. 1485).

In light of the above, there is convincing evidence that split purchase customers are similar to dual play in terms of demographics, propensity to switch product/provider, level of engagement, and their propensity to switch to mobile services.

### 2.3 Ofcom overstates the concerns for split purchase customers

In this section we set out how (at least a proportion of) split purchase customers are engaging with offers in the market and are making reasoned choices. Ofcom appears to reach a view that, in general, split purchase customers are not getting a good deal; however it provides little evidence that this is the case, and implies that all split purchase customers would be better off moving to dual play.

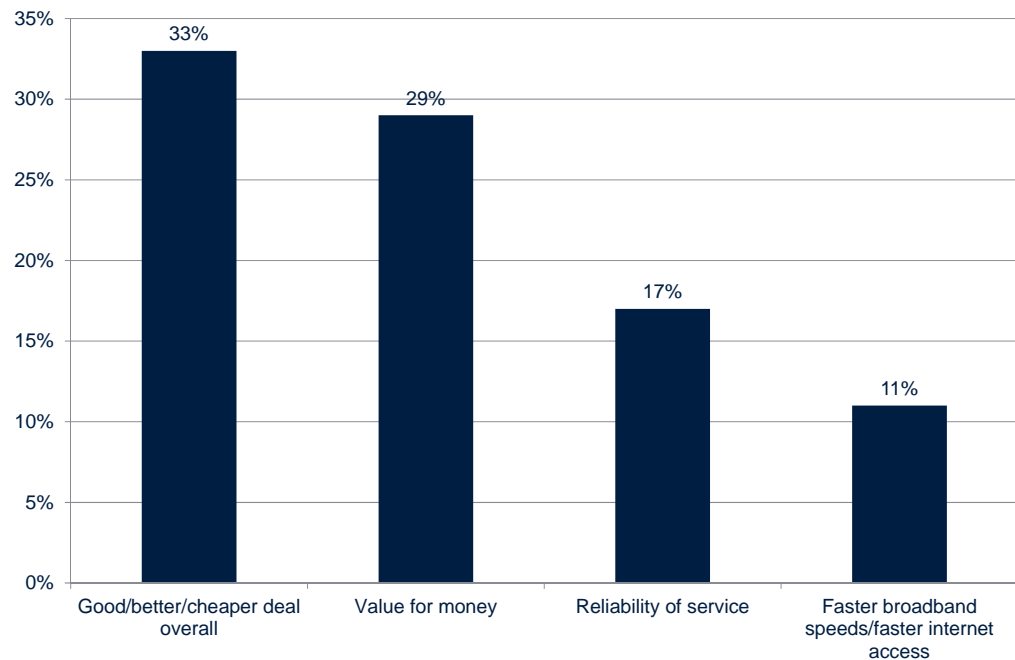
We show below that the savings available to some split purchasers may be small, leading to the conclusion that split purchasers may be optimising their purchases already (in the presence of rational switching costs). This is supported by Ofcom's survey evidence.

#### 2.3.1 Survey evidence supports the conclusion that some split purchasers are already optimising

Ofcom's survey evidence points to the fact that many split purchase customers are already optimising.

As shown in Figure 2.9, consumers set out a number of reasons why they chose not to buy broadband from the same CP as that providing their landline. This insight shows that a significant proportion of split purchase customers are making rational decisions.

**Figure 2.9 Why do split purchasers purchase broadband and landline from different companies?**



Source: Jigsaw market research for Ofcom Narrowband Review 2016, residential survey (wave 1) data table 106, p. 226.

This is good evidence to support the view that some split purchase customers are already optimising [their service]—i.e. have found the best deal for them.

As the above figure indicates, this optimisation is likely to capture both price and non-price factors (reliability and speed of service), and indicates that some split purchase customers are making informed choices.<sup>50</sup>

### 2.3.2 Rational switching costs may outweigh small savings

In this section we set out why consumers not switching may be a rational choice.<sup>51</sup> This is because, in any normal market, there can be frictions that are not caused by customers behaving sub-optimally. Such frictions could include switching costs, which are present in all markets, and could explain why consumers do not switch provider when the savings are small. Examples of such costs include:

- the time cost of finding and sorting a new contract—calling a new provider to discuss offerings, and calling the old provider to cancel the existing contract;
- fear of service decline—risk-averse customers may not wish to switch for fear of a reduction in service quality, or a perception of installation issues during the CP handover; and,
- the time cost of an engineer visit—this typically involves waiting at home for the installation to be completed by an engineer. Again, the consumer may

<sup>50</sup> Split purchase customers may be optimising their service by choosing the best service/provider in respect of each component: fixed voice and broadband. For example, if a consumer wants within their fixed call service, Nuisance Call Protect, faster repair on their line and unlimited free weekend calls (including 0845 and 0870), they might choose BT for the line rental. They may then look for the broadband offering that best meets their needs (taking into account quality and price factors), which may not be from the same provider as their landline.

<sup>51</sup> There are models of rational inattention. For example, see Sims, C.A. (2003), 'Implications of rational inattention', *Journal of Monetary Economics*, 50.

value their time highly and, in full knowledge of the small savings from switching, choose not to switch.

When combined, such costs may deter consumers from switching to a lower cost service, unless the savings they would make were very significant. Ofcom appears to overlook these switching costs in its assessment. For example, if the available savings from switching were £1 per month (which Ofcom suggests will be the case for some split purchase migrations), a rational consumer with a time horizon of one year would make the effort to switch only if they valued the lost time and expended effort at under £12. However, it is entirely plausible that a rational consumer would not switch under these circumstances—i.e. the £12 annual saving is not sufficient to offset the inconvenience of switching.

In short, some switching friction should be anticipated, and we would not expect all customers to migrate immediately to another CP offering the same service at a lower price. Furthermore, some consumers may be optimising their service already.

### 2.3.3 Ofcom may be overstating the savings from switching to dual play bundles

In the Annexes to the consultation document Ofcom shows that some split purchase consumers face small gains from switching to dual play bundles.<sup>52</sup> For example:

- a BT customer consuming 52MB/Unlimited would enjoy savings of £0.08 per month if they switched to a standard price dual play bundle;
- a BT customer consuming 76MB/Unlimited would enjoy savings of £1.26 per month if they switched to a standard price dual play bundle;
- a Sky customer consuming 17MB/Unlimited would enjoy savings of £3 per month if they switched to a standard price dual play bundle;
- a Sky customer consuming 38MB/Unlimited would enjoy zero savings if they switched to a standard price dual play bundle.

These savings are small, if they exist at all. However, Ofcom still calculates the weighted average saving as £8.01 per month. There are aspects of Ofcom's methodology that lead to the impression of higher savings than consumers would actually be able to achieve. For example:

- **omitting lower line rental prices:** some split purchase customers receive their line rental from CPs other than BT. The use of BT's line rental (£18.99) overstates the cost of line rental for many split purchasers. For example, those taking line rental from the Post Office may be paying only £15 per month for their line rental).<sup>53</sup>
- **omitted providers, such as Plusnet and SSE:** some split purchase customers will be with providers, such as Plusnet, which offer standalone broadband from £13.49 per month which is cheaper than the BT weighted average deals shown by Ofcom.<sup>54</sup> If a customer purchased Plusnet

<sup>52</sup> Ofcom (2017), 'RMSLTS', Annexes Figure A8.43.

<sup>53</sup> Ofcom (2017), 'RMSLTS', Annexes Figure A8.24; and the Post Office website <http://www.postoffice.co.uk/broadband-phone>, accessed 8 May 2017.

<sup>54</sup> <https://www.plus.net/home-broadband/broadband-only/> <https://www.plus.net/home-broadband/>, accessed 8 May 2017.



standalone broadband and the BT line rental, the savings from switching to a dual play bundle of the same speed would be small;

- **omitted deals from legacy customers:** some standalone broadband customers will come from legacy operators including Tesco, Tiscali and O2. These brands may have advertised low standalone broadband, which may mean some split purchase customers are on low-cost deals.

Together, these mean that the estimated savings available to the split purchase consumers from switching to dual play bundles are overstated. In light of these smaller savings, it may be that some consumers are already optimising by not switching.

## **2.4 Ofcom appears to underestimate the constraints BT faces in respect of voice-only customers**

Ofcom appears to overlook the fact that BT faces material competitive constraints in the voice-only customer segment. Notably:

- the Post Office is actively looking to secure voice-only customers
- mobile provides a constraint on landline services including voice-only customers
- many voice-only customers have access to broadband, and therefore are able to assess market offers

These three factors are explored below.

### **2.4.1 The Post Office is actively looking to secure voice-only customers**

The Post Office is an active competitive constraint on BT in the voice-only customer segment. The Post Office's overall SFV market share has been increasing since 2012 and is in the range of 5–15%.<sup>55</sup> The Post Office also has 5–15% market share of the voice-only customer segment.<sup>56</sup>

The Post Office has a strong strategy to attract new voice-only customers, which is detailed in the Ofcom consultation document.<sup>57</sup> This strategy has involved having the cheapest line rental price (since 2011)<sup>58</sup> and:

- three acquisition channels (online, call centre and in-branch);
- various marketing campaigns which highlight the ease of switching;
- an introductory offer of lower prices (12 months at £14.99 per month—£6 per month cheaper than BT).

<sup>55</sup> Ofcom (2017), 'RMSLTS', para. 4.18.

<sup>56</sup> *Ibid.*, para. A8.39.

<sup>57</sup> *Ibid.*, para. A8.56.

<sup>58</sup> *Ibid.*, Figure A8.24.

**Figure 2.10 Post Office advertising landline services**

### Just need a phone line?

Want to keep it simple? Free weekend calls to UK landlines including 0845 and 0870 numbers for just £15 a month

- ✓ £6 a month cheaper than BT Line Rental Plus
- ✓ FREE weekend calls to UK landlines (01, 02 and 03) and 0845/0870 numbers
- ✓ Keep your existing number and services
- ✓ UK based customer service
- ✓ FREE to pay your bill by cash or direct debit
- ✓ Low call rates. [Find out more.](#)

Source: Post Office Website, accessed 3 May 2017.

In summary, the Post Office is an active competitive constraint on BT in the voice-only market segment.

#### **2.4.2 Ofcom does not appear to fully account for the constraint mobile has on fixed voice services**

Mobile services are an active competitive constraint on providers of fixed voice services. The evidence for this includes the following.

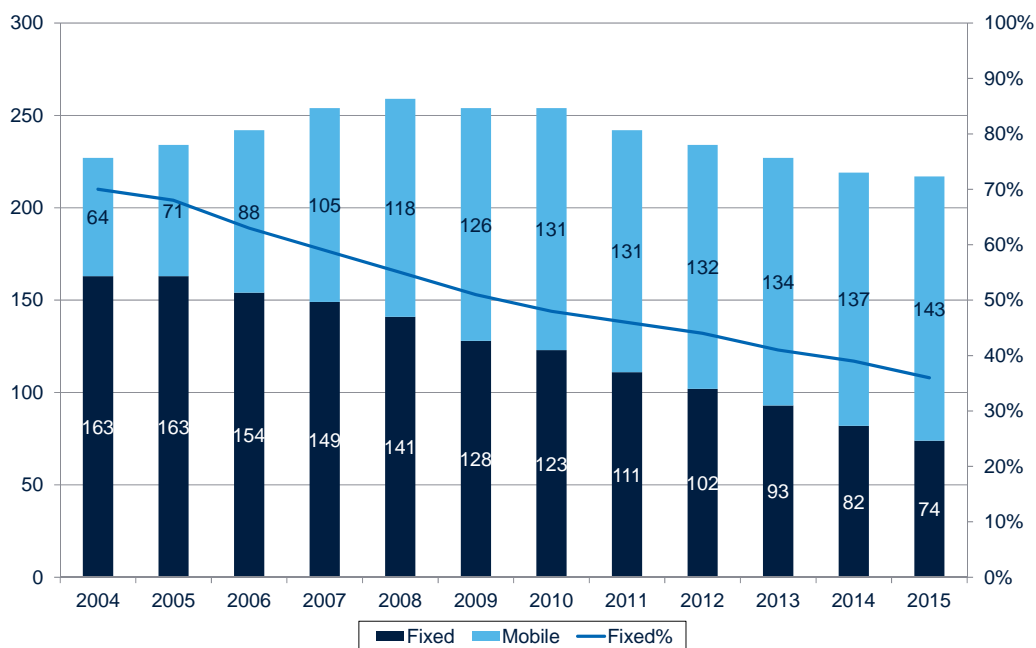
- Ofcom claims that over half (58%) of voice-only customers own a mobile phone.<sup>59</sup> Other evidence suggests that this proportion could be even higher—for example, the Jigsaw wave 1 survey finds that 69% of those with a landline but no broadband own a mobile phone.<sup>60</sup>
- If the overall landline price increased by 10%, a significant proportion of voice-only customers would switch to mobile services.<sup>61</sup> Specifically, 11% of voice-only customers would be likely to switch some calls to mobile; 8% would be likely to switch some calls to email/text messages/instant messages; and 10% would be likely to give up their landline altogether

Thus, in light of ongoing fixed to mobile substitution in the voice market, mobile is likely to provide a material competitive constraint to the pricing on landline services. See, for example, Figure 2.11.

<sup>59</sup> Ofcom (2017), 'RMSLTS', para. 3.58.

<sup>60</sup> Jigsaw survey wave 1, Table 906 (p. 1439).

<sup>61</sup> Jigsaw survey wave 1, tables 639, p.1011, 661, p.1048, and 672, p.1065. It is not clear from the survey whether these percentages can be summed together, or whether they represent the same customers.

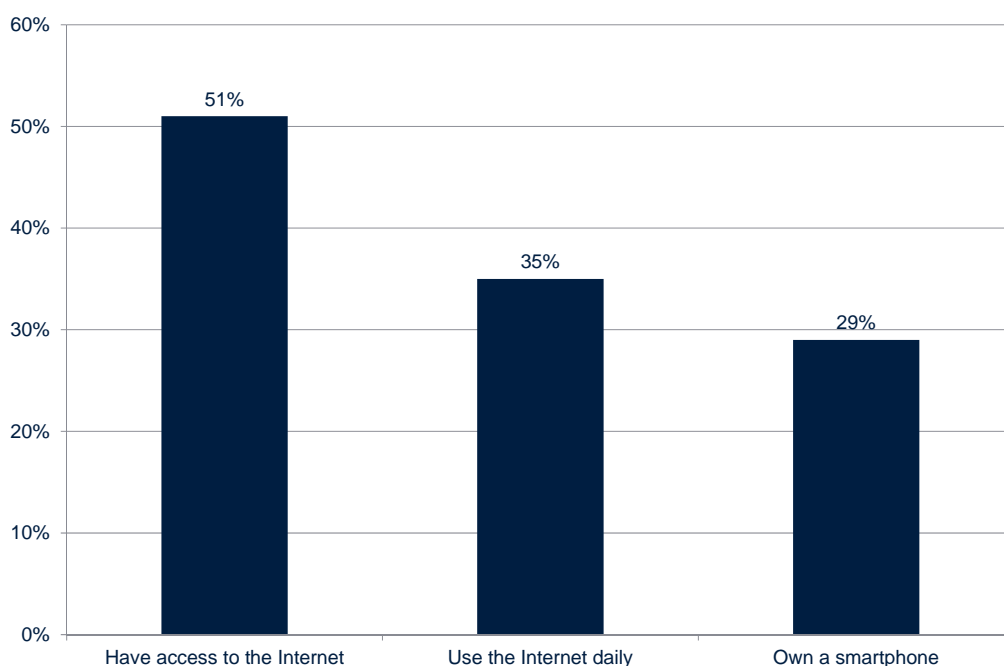
**Figure 2.11 Decline in fixed call volumes (billions of minutes)**

Source: Ofcom (2016), 'Narrowband Market Review', consultation, 1 December, Figure 1.1, p. 4.

### 2.4.3 Many voice-only customers have access to the Internet despite not having a fixed broadband service themselves

Ofcom overlooks the fact that many voice-only customers have access to broadband (for example by using their friends'/family's Internet connection, free Internet in local libraries, or mobile data/broadband) and are therefore able to search for better landline offers.

Figure 2.12 shows that just over half of voice-only customers have access to the Internet and over a third use it daily. Also, 29% of voice-only customers own a smartphone.

**Figure 2.12 Voice-only customers have access to the Internet**

Source: Jigsaw market research for Ofcom Narrowband Review 2016, residential survey (wave 1). Data table 906 (p.1441, 1443).

As seen in the figure, many voice-only customers have internet access and are active online. Indeed, the Post Office acquires 20% of its voice-only customers through online channels.<sup>62</sup> This means that many voice-only customers would be able to access market information,<sup>63</sup> such as price comparison websites which are an important source of information.<sup>64</sup> The barriers to consumer engagement in the voice-only segment are less than Ofcom assumes.

#### **2.4.4 CPs do have an interest in competing for standalone voice customers**

We note that there are still significant gains to be made from the voice-only segment, which provide an incentive for CPs to enter, or compete more strongly in, the voice-only segment. Ofcom states that:

The data suggests that some other CPs are making reasonably high profits from their fixed voice customers, though none as high as BT.<sup>65</sup>

Ofcom assumes that CPs would have to offer a 25% discount on line rental compared with BT in order to win customers, but that the CPs would still be making a 'significant and positive' marginal profit per consumer.<sup>66</sup>

Therefore Ofcom assumes that the marginal SFV customer currently generates at least £4.74 per customer (with line rental of £18.99).<sup>67</sup> If a CP competed in the voice-only market and gained a 10% market share, the CP would have approximately 170,000 customers.<sup>68</sup> With line rental of £18.99 and market share

<sup>62</sup> Ofcom (2017), 'RMSLTS', para. A8.56.

<sup>63</sup> With regard to the access/assess/act framework.

<sup>64</sup> Ofcom (2017), 'RMSLTS', para. A6.5.5.

<sup>65</sup> Ofcom (2017), 'RMSLTS', para. A5.71.

<sup>66</sup> Ofcom (2017), 'RMSLTS', Table A5.12

<sup>67</sup> Ten percent of £18.99 minus £5 is £1.40.

<sup>68</sup> Total segment size of approximately 1.7 million. Ofcom (2017), 'RMSLTS', Figure A8.8.

of 10%, this would therefore generate profits of at least £807,075 per annum. Indeed, the Post Office currently offers line rental for £15, a price that is profitable according to this analysis.<sup>69</sup>

This is demonstrated by the efforts currently being made by the Post Office, as set out in more detail in section 2.4.1.

#### **2.4.5 It is not clear that BT is a price leader for voice-only**

As a result of being found to have SMP for the provision of wholesale local access services, BT is regulated and required to provide at cost (and in a non-discriminatory way) wholesale access to landline phone and standard broadband (MPF and WLR+SMPF). Currently, the regulated wholesale charge is around £8 per calendar month for WLR.

As such, retail service providers can purchase a wholesale input and compete at the retail level for the provision of fixed voice services. Given this, there is a level playing field, which creates a platform for competition to play out downstream, and for firms to compete for customers.

As a wholesale provider, BT has no control over the retail prices set by its downstream competitors.

Despite this, Ofcom argues that prices have converged as a result of price increases and, in particular, that other CPs have followed price changes implemented by BT over the period April 2014 to January 2017 (RMSLTS, para. 4.52).

We do not consider that this provides any reliable evidence of BT playing a price leadership role for a number of reasons.

- The period is too short to make any meaningful inferences. As noted by Ofcom, CPs appear to be updating their prices on an annual basis (para A8.63). As a result, the period considered by Ofcom (2014–17) contains a sample of only three price adjustments (Figures A8.26–A8.28).
- What might appear to be price leadership is likely to reflect BT implementing its annual price changes earlier within the year for recent years—indeed, the assumption that price adjustments are annual is incorrect to begin with. In 2014, BT raised prices in December, in 2015 it raised prices in October and in 2016 it raised prices in July (Figures A8.26–A8.28).
- If prior years are taken into account, other CPs adjust their prices prior to BT. In particular, in 2013, Virgin Media adjusted its price first; in 2012, Sky adjusted its price first; and prior to that price adjustments were implemented more than once per year, such that it is no longer meaningful to speak of a CP changing price before or after another CP.

The view taken by Ofcom—that BT is a price leader—is therefore not clear from the limited evidence Ofcom presents.

#### **2.5 Ofcom’s approach leads to flawed remedies**

We now turn to consider the remedies that Ofcom proposes following its market assessment, and outline the shortcomings in Ofcom’s approach to remedies.

<sup>69</sup> A 25% discount on line rental of £18.99 leads to a line rental of £14.24, a price that Ofcom assumes to be profitable.

Notwithstanding that Ofcom has not substantiated the need for intervention, its analytical approach results in significant shortcomings in respect of remedial action, in terms of what can be imposed (given the SMP finding) and how remedies are imposed.

First, the SMP approach used by Ofcom reduces its flexibility in choice of remedy. Market-wide remedies are artificially ruled out which is inappropriate given the market-wide nature of the concerns identified by Ofcom.

Second, the remedies that Ofcom does propose are disproportionate and will have unintended consequences:

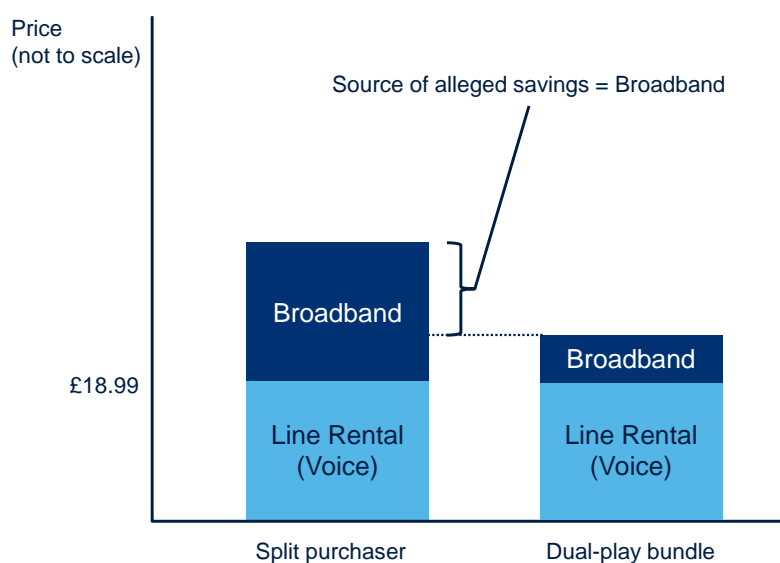
- its proposals do not address the cost of standalone broadband for split purchase customers. The remedy is targeted solely at standalone voice
- Ofcom does not appear to have thought about the impact of the proposed remedies on the migration towards dual play bundles and digital inclusion. The unintended consequences would be detrimental to consumers.

These two problems are analysed below.

### **2.5.1 The proposed remedies ignore any issues relating to standalone broadband**

Ofcom believes that split purchasers pay over the odds when compared to dual play customers (who receive a functionally equivalent service). However, this is supported only by evidence of hypothetical savings by reference to average bundle prices, as opposed to any empirical investigation of savings actually achievable by split purchasers (which will depend on their actual suppliers and purchase prices).

Given that the line rental is the same in the two cases (which Ofcom itself assumes in its analysis of the savings from a split purchase customer moving to dual play), the saving from moving to dual play from split purchase is attributable to a saving on the broadband component, as illustrated in Figure 2.13.

**Figure 2.13** Stylised example of savings from dual play bundles

Source: Oxera.

If the saving is attributable solely to the broadband component, it is not immediately clear why a remedy should be applied to the line rental (voice) component. However this is precisely what Ofcom is proposing for these split purchase customers. Furthermore, Ofcom proposes to apply such a remedy to BT only.

We note that BT has only a small share of the broadband component of split purchase customers, at around 17%. This figure is reduced further when accounting for the fact that around [§<] of BT's split purchase customers are BT employees (who receive the service at a reduced rate). Taking this into account BT's share of the broadband component of split purchase customers is likely to be around [§<].<sup>70</sup> Therefore, not only is Ofcom applying remedies to the wrong product, but also to the wrong firm—BT does not have SMP in standalone broadband.

In summary, Ofcom proposes to apply a remedy on split purchase customers in relation to the line rental price, solely in relation to BT. However, the issue identified by Ofcom relates to the price of *broadband* for split purchase customers, in which BT has a share of less than 20%.

We therefore conclude that Ofcom's proposal to apply SMP obligations on BT for the split purchase customer cohort is disproportionate and inconsistent with the nature of its concerns.

### 2.5.2 Ofcom has not considered the impact of the proposed remedies on future migration to dual play bundles and digital inclusion

Ofcom's proposed price cut on BT's standalone voice products could significantly reduce the incentive for customers to purchase broadband, and thereby damage the government's stated goal of increasing digital inclusion.<sup>71</sup>

<sup>70</sup> On the basis that there are 200,000 split purchase customers on BT, and some 1.2m split purchase customers (split service + split supply) in total, we get  $(200,000 - [§<]) / (1.2m - [§<]) = [§<]$ .

<sup>71</sup> See, for example, Cabinet Office (2014), 'Government Digital Inclusion Strategy', policy paper, updated 4 December 2014, <https://www.gov.uk/government/publications/government-digital-inclusion-strategy/government-digital-inclusion-strategy>, accessed 8 May 2017.

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The price cut could have an adverse impact on digital inclusion because it would:

- **reduce migration from voice only to dual play:** by increasing the marginal price to a voice-only customer of purchasing a dual play bundle (i.e. the incremental price between dual play bundles and voice-only becomes greater), incentives to migrate to dual play would be reduced, as would the likelihood of those who are digitally excluded (do not have mobile Internet access, etc.) gaining broadband access. There may even be existing dual play customers who migrate back to voice-only and drop broadband altogether thereby increasing the size of the customer base that Ofcom has concerns about;
- **reduce migration from split purchase to dual play and possibly inducing migration from dual play back to split purchase:** by reducing the savings that can be made from split purchasers switching to a dual play bundle. Indeed, if there were negative savings, customers would have the incentive to 'unbundle' and switch from a dual play bundle back to split purchases.

As part of Ofcom's assessment, careful consideration needs to be given to such migration and switching incentives, in order to ensure that any intervention does not have unintended consequences.

Indeed, in other markets Ofcom has taken the migration of legacy services into consideration when deciding on the proportionality of intervention (see Box 2.4). While voice-only may not be classified as a legacy product, there is a clear drive to migrate landline customers onto other products, particularly in light of BT's 'all-IP' transformation objectives.



**Box 2.4 Ofcom's approach to the migration of legacy leased lines**

In April 2016 Ofcom published the final statement on the Business Connectivity Market Review: Very low bandwidth leased lines.<sup>72</sup> Ofcom decided to deregulate the prices of these legacy products, and allow BT pricing flexibility (BT pledged to keep price rises below RPI plus 8%).

A key part of Ofcom's consideration in this matter was the fact that prices were a key way of encouraging the migration away from these products:

We also consider that given the context, some price rises need not be an indication of market failure, and may be consistent with a signal to end-users about the need to migrate to alternative services alongside BT's notifications.

We accept that any such pricing signals will not motivate all end-users to migrate onto alternative services, including for the reasons Vodafone suggests. That said, we remain of the view that price rises can play a part in incentivising some end-users to migrate. Alongside any such signals, we have undertaken an extensive programme of engagement to inform [Critical National Infrastructure] operators in numerous sectors of the need to migrate onto alternative services before March 2020.<sup>73</sup>

Therefore, Ofcom took the forward-looking view that price differentials were helpful in encouraging the migration of customers away from certain products.

Another of Ofcom's considerations was that the retail markets to which the customers were migrating are competitive:

The available alternatives are provided in markets which are typically competitive at the retail level, supported where necessary by regulation at the wholesale level.<sup>74</sup>

This is highly relevant to the question of SFV customers migrating to dual play bundles, as the dual play market is highly competitive.

Source: Oxera.

**2.6 Conclusion**

In this section we have analysed the robustness of Ofcom's approach to, and conclusions on, market definition and market power in the standalone landline market review.

Our analysis finds that Ofcom has failed to take account of the principles of price discrimination in the context of market definition, which has implications for its conclusion that SFV constitutes a separate relevant economic market. Robustly viewed, the significant migration of SFV customers towards bundles reveals that the boundaries of the market that Ofcom has identified are not stable, which is an important condition (both theoretically and in practice) for separating relevant markets into narrow segments.

Ofcom has also incorrectly defined split purchase and dual play customers as being in separate relevant markets. Instead, we have presented evidence that they should be part of the same market: We find this on the basis of: i) both sets of customers consuming functionally equivalent services; and ii) both sets of consumers having very similar (demographic, market engagement, and mobile usage) characteristics.

Having incorrectly defined a narrow SFV market, Ofcom then finds that BT has SMP. In relation to this, we find that Ofcom has overlooked the competitive constraints faced by BT in respect of the voice-only customer segment. This results in an overstatement of the degree of market power that BT would have for voice-only customers. In particular, BT faces constraints both from mobile

<sup>72</sup> Ofcom (2016), 'Business Connectivity Market Review: Very low bandwidth leased lines', Statement, 28 April. [https://www.ofcom.org.uk/data/assets/pdf\\_file/0018/63225/final-statement.pdf](https://www.ofcom.org.uk/data/assets/pdf_file/0018/63225/final-statement.pdf)

<sup>73</sup> Ibid., paras. 3.32-3.33.

<sup>74</sup> Ibid., para. 3.12.

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substitution and from the Post Office which is competing actively for voice-only customers.

As a direct result of these shortcomings, Ofcom's proposals to remedy the alleged concerns are inappropriate.

First, SMP has not been properly substantiated for the reasons give above, and therefore there is no clear basis for SMP regulation. Second, Ofcom's approach reduces its flexibility in choice of remedy—market-wide remedies are artificially ruled out. This is inappropriate because the concerns identified by Ofcom (although not properly substantiated) are market-wide in nature.

Second, the remedies proposed by Ofcom are disproportionate and will have unintended consequences. In particular we note that; i) Ofcom's proposals do not address the cost of standalone broadband for split purchase customers. The remedies are targeted solely at standalone voice, when in fact, a significant proportion of the customers Ofcom is concerned about purchase a broadband service from a BT competitor; and ii) Ofcom does not appear to have considered how a deep price cut on standalone line rental might affect the migration towards dual play bundles and digital inclusion. These unintended consequences are likely to be detrimental to consumers.

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