Investigation into Dispute between Cable & Wireless Jersey Limited and Jersey Telecom Limited regarding ADSL broadband takeover charges

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Findings in Dispute and

Final Notice

22 November 2011

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1. Introduction

In June 2011, Cable and Wireless Jersey Limited ('C&WJ') submitted a complaint to the Jersey Competition Regulatory Authority ('JCRA') regarding the charge applied by Jersey Telecom Limited ('JT') for the migration of Asymmetric Digital Subscriber Line ('ADSL') broadband customers from one internet service provider ('ISP') to another. JT's wholesale business ('JT Wholesale') currently charges ISPs £44 if they wish to take over a broadband customer from another ISP. This "takeover charge" is intended to cover the cost to JT Wholesale of the administration of transferring customers between ISPs.

C&WJ has alleged that the takeover charge is not cost-justified and that it is a barrier to effective competition in the market for retail broadband services provided on fixed-line networks in Jersey.

Upon receipt of the complaint, and after consideration of the issues, the JCRA began a formal investigation of the complaint. In July 2011 the JCRA provided JT with a notice of the complaint and JT provided a response setting out its justification for the charge. C&WJ was then asked for its view on JT's response and the JCRA considered this information along with such other information as it believed was relevant to its consideration of the matter.

The JCRA's provisional findings in the dispute, and an Initial Notice of a proposed determination, were published on 3 October. Responses to the Initial Notice were received from Teletech Solutions and JT. On the basis of the assurances provided by JT in its response to the Initial Notice, the JCRA has decided to give Final Notice of its decision to withdraw the proposed determination.

This report summarises the issues involved, and sets out the findings of the JCRA. It also constitutes a Final Notice under Article 11(4) of the Law of the JCRA's decision to withdraw its proposed determination, made under Article 16(3) of the *Telecommunications (Jersey) Law 2002* (the 'Law') and Condition 33.2 of the Class III licence issued to JT by the JCRA under Article 14(1) of the Law (the 'Licence').

2. Details of Complaint and JT's response

C&WJ requested the JCRA to investigate the level of JT's takeover charge for Wholesale ADSL services. This charge is applied when a retail ADSL broadband customer transfers (or migrates) between ISPs, since JT Wholesale is required to take certain steps to facilitate this transfer. Currently JT charges the acquiring ISP £44 per migration pursuant to the Wholesale DSL Agreement between JT and the other licensed operators ('OLOs'). It is alleged by C&WJ that the charge is not cost-based as, in its view, the function should be a quick administrative one and should be capable of being done without the need for a site exchange visit. It is alleged by C&WJ that the charge acts as a barrier to competition, by making it more difficult for retail ADSL broadband customers to switch ISP, and is an abuse of JT's dominant position in the market for wholesale broadband services provided on fixed-line networks in Jersey.

The JCRA provided JT with a copy of the complaint and requested JT's views on the matter. On 8 July 2011, JT provided a response to the JCRA in which it stated that the work required to migrate a customer follows a very similar process to a new order for a broadband service. It provided a schematic diagram of the steps involved in migrating a customer and confirmed that the process and charge applied by JT Wholesale to JT's retail business is the same as that applied to OLOs. JT further provided a cost breakdown which it believes supports the £44 charge currently applied by JT Wholesale, based on an average time of 69 minutes of staff time required to complete a migration.

Upon receipt of this information from JT, the JCRA sought C&WJ's views on the justification provided. In a response dated 25 August 2011, C&WJ stated that it does not accept that the time required by JT Wholesale to complete this work is as claimed by JT. C&WJ agreed with JT that the work required to provision a takeover under JT's current system would follow a similar process to a new order for ADSL. However, C&WJ notes that such work is solely related to system-inputting requirements, and does not entail any engineering tasks.

CW&J stated that operational staff at Cable & Wireless Guernsey Limited ('C&W Guernsey'), which is the main operator of the fixed-line telecommunications network in Guernsey, estimated that the process outlined by JT in its response should take a maximum of 20 minutes (less than a third of the time estimated by JT). The process for transfer of ADSL customers in Guernsey is automated, so customer migrations can be undertaken rapidly. C&W Guernsey does not levy a charge on OLOs for transferring ADSL customers.

C&WJ argued that the application of the takeover charge by JT creates a financial barrier to customers switching between ISPs, given this charge equates to an additional £3.67 per month per customer (assuming a 12 month contract term). It further highlighted that should a customer at the end of their contract with an ISP move to an alternative ISP, a further £44 charge will be levied. C&WJ argued that in such circumstances, the incentives for customers to switch between broadband providers are significantly diminished.

C&WJ also noted that while it might well be the case that JT Wholesale levies an equivalent takeover charge on JT's retail business when it acquires a new broadband customer, JT's 2009 separated accounts suggest that JT's retail broadband activities "cannot afford" this takeover charge, given that these activities alone generated a loss of £266,000. C&WJ contended that this was further evidence that the takeover charge is currently set at an inappropriate level.

C&WJ submitted that, in applying this takeover charge, JT is infringing condition 34.1(b) (Fair Competition) of the Licence.

3. Legal Background

In April 2010, the JCRA determined, as part of its review of the telecoms sector in Jersey, that JT has significant market power ('SMP') in the market defined as

‘Wholesale Broadband Services Provided on a Fixed Network’. As the owner and operator of the main fixed-line telecommunications network within Jersey, JT remains the sole provider of wholesale broadband services provided on a fixed-line network. In addition, at the retail level, the JCRA estimates that JT currently supplies approximately 80% of ADSL subscriptions within Jersey.

As a result of having SMP in a number of the markets in which it operates, JT has certain additional conditions in its Licence which do not apply to non-SMP operators. Licence Condition 34.1 states:

34.1 The Licensee shall:

(a) not abuse any position of Significant Market Power and/or established position in any telecommunications market;

(b) not engage in any practice or enter into any arrangement that has the object or the likely effect of preventing, restricting or distorting competition in the establishment, operation and maintenance of Licensed Telecommunication Systems or the provision of Telecommunication Services; and

(c) comply with any direction issued by the JCRA for the purpose of preventing any market abuse or any practice or arrangement that has the object or effect of preventing, restricting or distorting competition in the establishment, operation and maintenance of Licensed Telecommunication Systems or the provision of Telecommunication Services.

Although not specifically mentioned by C&WJ in its formal complaint, Licence Condition 33 also confers on the JCRA certain powers to regulate, or make directions in respect of, the prices charged by JT for certain telecommunications services.

JT is obliged under Licence Condition 33.3 to ensure as follows:

all published prices, discount schemes and special offers of, or introduced by, the Licensee for Telecommunication Services shall be transparent and non-discriminatory; all prices and discount schemes shall be cost-justified and all special offers shall be objectively justifiable.

Licence Condition 33.4 provides that, in the event that the JCRA, after consulting JT and such other persons as it may determine, is satisfied that any published price, discount scheme or special offer of JT is in breach of the Law or the Licence, the JCRA may, by issuing a direction, require JT to bring the relevant prices, discount schemes or special offers into conformity with the Law and/or the requirements of the Licence.

Licence Condition 33.2 allows the JCRA to determine the maximum level of charges that JT may apply for Telecommunication Services within a relevant market in which JT has been found to be dominant. The determination may:

(a) *"provide for the overall limit to apply to such Telecommunication Services or categories of Telecommunication Services or any combination of Telecommunication Services;*

(b) *restrict increases in any such charges or to require reductions in them whether by reference to any formula or otherwise; or*

(c) *provide for different limits to apply in relation to different periods of time falling within the periods to which any determination applies*."

"*Telecommunication Services*" is defined in Licence Condition 1.1 as meaning "the provision of any telecommunications services to the public". The JCRA is satisfied that this definition encompasses the supply of ADSL takeover services to OLOs under the Wholesale DSL Agreement.

4. The JCRA's Findings

The JCRA believes the availability of an efficient process for enabling customers to switch between broadband providers is essential in promoting effective competition in the retail market for fixed-line broadband services. In order for new entrants to compete in that market - in particular, to compete with JT - it is important that OLOs are able to compete for existing broadband customers; otherwise, OLOs are left to try and compete for potential new broadband customers, and, given that the current level of broadband penetration in Jersey is approximately 80%, it is unlikely that an OLO could build a sustainable business through new custom alone.

The JCRA notes that JT has little or no commercial incentive to design, implement and operate a migration service for broadband customers that is as efficient as possible, given its existing position in the retail fixed-line broadband market in Jersey.

In a market where average monthly retail broadband tariffs are typically in the region of £18 (for a 2 Mbps service) to £28 (for an 8 Mbps service), a price reduction even as large as 10% by an ISP (or an improvement in quality of service equivalent to a price reduction of this magnitude) would only begin to outweigh the £44 fixed charge (and thereby provide an incentive for a customer to switch) after more than 15 months (at 8 Mbps) or more than 24 months (at 2 Mbps). In the JCRA's view, such a significant barrier to switching is very likely to have the effect of reducing the competitive pressure on all retail broadband providers, but particularly JT, which currently supplies approximately 80% of retail broadband subscriptions (and held an even larger share prior to its introduction of a wholesale ADSL product). All other things being equal, the absence of competitive pressure would be expected to reduce the efficiency of provision of these services, and reduce the propensity of current providers or potential entrants to innovate.

There is no evidence currently before the JCRA which would cause the JCRA to doubt JT's claim as to the costs that it actually incurs in handling a broadband migration request. However, the JCRA considers that in performing its functions under Licence Conditions 33 and 34, it must also assess whether such costs are ones that an efficient operator would incur. In so doing, we have looked to other jurisdictions to assess what steps wholesale operators have taken to reduce the cost of this essential service and considered whether it is reasonable to expect that JT, operating efficiently, would itself take similar steps.

The information provided by C&WJ with respect to the manner in which C&W Guernsey handles broadband takeover requests is considered particularly relevant. JT and C&W Guernsey are broadly similar, both in size and in terms of the wholesale broadband service offered. As noted in section 2 above, in Guernsey, the process applied by C&W Guernsey (as the provider of wholesale ADSL services) for transferring customers between ISPs is automated. C&W Guernsey does not levy any charge on OLOs for an equivalent migration service (provided to, amongst others, JT's sister company, Wave Telecom Limited, which purchases wholesale broadband services from C&W Guernsey for its retail operations in Guernsey).

In its response of 25 August 2011, C&WJ contended that even if a takeover charge were justified, and it was reasonable to continue to use a manual process for customer migrations, the actual level of charge applied by JT does not reflect the cost that an efficient operator would incur in performing that function. As noted above, C&WJ estimated that undertaking the processes that JT states in its submission of 8 July 2011 are necessary for transfer of an ADSL customer should take *a maximum* of 20 minutes work.

The JCRA does not accept that an efficient provider of ADSL takeover services would continue to utilise the manual migration process currently adopted by JT. As stated above, the JCRA notes that in Guernsey, C&W Guernsey has adopted an automated process and applies no charge on OLOs for the same service. Even if a manual process remained appropriate, we do not believe that charge levied by JT is reflective of the costs that an efficient operator would incur in providing the takeover service. Given the incentives on JT to keep this charge at a high level, the JCRA believes it is important that, in determining the appropriate level of this charge, it is set with reference to efficiently-incurred costs rather than on the basis of the actual costs incurred by JT. The JCRA considers that the evidence of C&W Guernsey in relation to the time that the process performed by JT should take provides an appropriate benchmark for setting the maximum charge for the takeover service in Jersey.

Applying JT's current implied per hour charge of £38.25 (ie £44 for a 69 minute task) to the benchmark time estimate provided by C&W Guernsey (ie 20 minutes) results in an "efficient" charge of £12.75.

Importantly, the price generated by using C&W Guernsey time estimate does not appear to be an outlier. In the UK, BT Openreach applies a charge of £11 (excluding VAT) for the same service.

5. The Initial Notice

In light of the JCRA's provisional finding that the ADSL takeover charge levied by JT is higher than the charge that an efficient operator, setting a cost-based price, would impose for this service, the JCRA considered whether such conduct could constitute a breach of Licence Condition 34.1. While the JCRA considered, for the reasons set out above, that the level of the ADSL takeover charge levied by JT restricted competition in the provision of retail broadband services using a fixed-line network, it was not satisfied that Licence Condition 34.1(b) is intended to be invoked in situations of unilateral conduct where there is no evidence that the entity in question is setting a price that exceeds the actual costs that it incurs for providing the service.

The JCRA considered that it would be open to it to issue a decision under Licence Condition 33.4 that JT was in breach of Licence Condition 33.3, on the basis that it had found that the ADSL takeover charge is not "cost-justified", as it exceeds by a considerable margin a reasonable benchmark of efficient cost. However, in circumstances where JT holds a position of dominance in respect of a particular service, and the JCRA proposed to instruct JT to set the price of that service in accordance with the costs of an efficient operator, the JCRA considered that the more appropriate power was the ability to issue a determination under Licence Condition 33.2.

On 3 October 2011, the JCRA therefore issued an Initial Notice under Article 11(1) of the Law, advising of its intention to issue a determination under condition 33.2 of the Licence that the maximum charge levied by JT for ADSL takeover services be set at £12.75 per transferred subscriber.

6. Responses to the Initial Notice

Two responses to the Initial Notice were received.

The first, from Teletech Solutions ('Teletech'), was received on 10 October 2011. Teletech agreed with the JCRA that the imposition of a broadband takeover charge is a significant barrier to competition in Jersey, and had the effect of limiting customer choice in this service. It believed that a reduction should be implemented at the earliest possible opportunity, and, indeed, that a move to JT being prevented from levying any charge whatsoever should be pursued. It also submitted that:

- a wider framework of measures should be imposed to reform the overall structure of the market;
- the proposed 'takeover' price of £12.75 was arrived at through somewhat arbitrary analysis, and may be open to challenge now or in the future;
- the determination should ensure there is no migration fee levied against the retail customer;
- the determination should compel the operators to offer a seamless migration process from a customer's perspective (such as the migration authorisation code (MAC) system used in the UK);
- the charges should apply to all broadband providers in Jersey; and
- action should be taken to address the take over charge for migration of Symmetric Digital Subscriber Line ('SDSL') broadband customers, which is currently around £170.

JT submitted a response on 3 November 2011. It advised that the calculations that it had provided to the JCRA on 8 July regarding the time that the customer migration required were predicated on a dual-network environment (ie that wholesale ADSL services were being provided through customer connections to both its legacy System X network, and its Next Generation Network (NGN)), although this had not, in fact, been stated in the response of 8 July. JT further advised that as its ADSL wholesale services were, as of 30 September, provided exclusively through connections to its NGN (ie it now had a single network environment), it had conducted a new time estimate for the customer migration process. Its new time estimate suggested that the cost-justified and efficient charge should be £15.72, and it proposed that the charge could be brought into effect from 1 December 2011. JT stated that it had committed to Newtel in April 2010 to review take over charges once the customer migration had been completed in any case.

JT submitted that no weight should be given to the C&WJ analysis of the time required to conduct the migration process, as it operates on different network architecture to JT and so had no specific expertise in completing this form of migration. JT also considered that a comparison between JT's charges and those levied by Openreach was inappropriate, due to differences in size and product offerings.

In reply to subsequent queries from the JCRA, JT confirmed that it proposed to levy the same £15.72 charge for migration of SDSL accounts.

7. Conclusion

The JCRA noted Teletech's urging for a wider framework of measures to reform the overall structure of the broadband market, although this goes beyond the scope of the Initial Notice. The JCRA will explore with JT and OLOs whether further steps could be taken to implement a seamless migration system in a market the size of Jersey at a reasonable cost. Given that neither C&WJ nor Newtel hold dominant positions in the retail broadband market, the JCRA is limited in its ability to regulate the prices that they charge (including whether they pass on the newly reduced take over charge to customers). However, as this is a charge that is applied by JT Wholesale to OLOs, the JCRA would see that OLOs have every incentive to ensure that the cost of switching from JT to their retail service is as low as possible, and we are therefore confident that consumers should see the benefit of this price reduction. The JCRA would expect that increased competition in this market will lead to the best outcomes for customers.

In considering the proposal put forward by JT, the JCRA has had regard to the following considerations:

- The charge proposed by JT is almost £3 higher per transferred account than the charge set by the JCRA in the determination proposed in the Initial Notice. However, the new charges will be considerably lower than those currently applied by JT.

- JT’s proposed implementation date of 1 December means that the benefits of lower take over charges will be available to OLOs and consumers imminently in respect of both ADSL and SDSL services. By contrast, if the JCRA were to pursue the existing provisional determination, the new charge would only be available, at the earliest, by mid-December 2011 for ADSL accounts. A new determination would need to be proposed for a change to JT’s charge for SDSL account migration, and it would be February or March 2012 before it could take effect.

Taking account, in particular, of its duties under Article 7(2) of the Law:

- to protect and further the short-term and long-term interests of users within Jersey of telecommunication services (Article 7(2)(a)); and

- to impose a minimum of restrictions on persons engaged in commercial activities connected with telecommunications in Jersey (Article 7(2)(d));

the JCRA has concluded, on balance, that the proposed determination set out in its Initial Notice of 3 October should be withdrawn in favour of allowing JT to take unilateral action to reduce its take over charges for migration of ADSL and SDSL accounts.

The JCRA hereby issues a Final Notice advising of that decision to withdraw the proposed determination.

For the avoidance of doubt, it should be noted that the JCRA maintains its view that in markets where JT holds a dominant position and, in particular, the product provided by JT is integral to the efficient operation of a downstream market, then its starting point will be that the price charged by JT should be not only cost-reflective but also efficient. The JCRA is clear that Condition 33.2 of JT’s licence provides the JCRA with the power to set prices based on the costs that an efficient operator would incur in providing that service, and not merely to constrain excessive or discriminatory pricing by JT.

In the event that the JCRA considers wholesale broadband charges more widely at a point in the future, or if JT seeks to increase the take over charge for either ADSL or SDSL accounts in the near future, then the JCRA reserves the right to revisit the level of ADSL and SDSL take over charges levied by JT Wholesale.

By order of the JCRA Board **22 November 2011**