

Response to CICRA consultations CICRA 15/07 and CICRA 15/08

Review of the price control for Wholesale on-island leased lines in Guernsey and Jersey

This paper is submitted as a response to both the above consultations and provides the perspective of an independent analyst into the impact of the proposals on the markets in both Guernsey and Jersey. As such, and noting the parallel approach and outcome taken by CICRA in both islands, I refer throughout this response to the general term "SMP operator" which shall apply equally to Sure in Guernsey and JT in Jersey as the subjects of the consultations having been found to have Significant Market Power in the respective Wholesale leased line markets. For simplicity, I also refer to the Business Connectivity Market Review (BCMR), from which this designation has resulted, and the above consultations themselves in the singular where appropriate in recognition of the parallel approach taken by CICRA in both markets.

I note that CICRA's primary proposal is to implement a Retail-minus price control mechanism on the SMP operators. In short, I do not believe that this mechanism is appropriate for a number of reasons, not least that it may in fact cause the connectivity markets to stagnate and promote inefficiency rather than achieving CICRA's stated objective of *"encouraging on-going investment and innovation so that high quality communications services are available to [island] customers"*.

In support of this view, I present a brief analysis of the preceding BCMR; the requirement for and definition of Wholesale connectivity services, and the subsequent conclusions drawn in this consultation and then provide responses to the questions presented by CICRA.

In the BCMR¹, CICRA states within its definition of business connectivity, *"Generally, wholesale and retail leased lines are parallel markets – the products are often the same, with the difference being in the pricing. This is in contrast to other communications services, where the wholesale inputs purchased can vary significantly from the retail service provided. For example, a wholesale bitstream input which is used to offer retail broadband does not have the same characteristics or pricing structure as the retail product."*

This may be true as the markets currently stand, but the review makes no reference as to why this is the case, or attempt to challenge whether it should continue to be so. The key to the difference cited compared to broadband services is historic and actually rooted in the origins of the

1 Business Connectivity Market Review Consultation documents CICRA 14/16 (Guernsey) and CICRA 14/17 (Jersey)

particular markets in relation to the introduction of competition and regulation rather than any specific requirement for identical products between wholesale and retail markets. As CICRA will be aware, the introduction of broadband services came at around the same time as the introduction of liberalisation and regulation into the market. The requirement for the incumbent operators to provide access to competing OLOs was therefore built into the products from the very start and is reflected in the pure wholesale components, Service Provider interconnects and associated processes which allow the incumbent's retail arm to operate on equal terms to OLOs.

By contrast, the retail leased-line market existed long before the introduction of regulation. This therefore necessitated the creation of a wholesale market in order to stimulate competition and allow the entry of OLOs into the retail market. The standard "incumbent-breaking" approach of choice at the commencement of regulation was of course to mandate the introduction of a parallel wholesale product set mirroring every retail service on a Retail-minus basis, thus providing OLOs without network infrastructure the ability to buy, use and resell services from the SMP operator and to enter the retail market.

Since that time, the leased-line product set and technology deployed has evolved little over the intervening 14 or so years. While there has been a natural upward shift in terms of bandwidth and from TDM towards Ethernet services, the fundamental concept of the product set being a fixed bandwidth point to point service and the means of delivery has hardly changed. While price controls have changed in focus to a greater or lesser extent, it is of little wonder that the largely parallel product set mandated by CICRA remains, with wholesale connectivity services being essentially white-label versions of the retail equivalents. It does not, however, automatically mean that this should continue to be the case or that the full specifications and functionality of a re-badged retail product are always appropriate at a wholesale level.

During the Channel Islands Wholesale Access Project (CIWAP), a requirement for a more use-agnostic Wholesale connectivity product and model was identified as an evolution for leased lines away from the existing retail-based services. Through the process, this resulted in a proposal for Hub and Spoke Ethernet being developed, which would have provided a model of wholesale-only building blocks on which operators could effectively develop and deploy any downstream products, services or infrastructure without further recourse to the SMP operator.

Disappointingly, this was dismissed from the process by CICRA and its then consultants, despite being the only proposed service in the process related to the business connectivity sector (the rest

such as WLR being primarily consumer based) and amid calls for its retention in the process to allow for pan-island oversight and implementation. The reasons cited by CICRA for this were:

“Hub and spoke Ethernet” was seen as a product of the natural evolution of operator’s networks that would be delivered location by location over a period of time. It was not a product that operators believed could be made available quickly on a pan Channel Islands or an island wide basis. On this basis and given the view that even without the CIWAP, operators could roll out the product locally on an area by area basis, CICRA indicated that it was minded to drop this product from the project altogether and allow it develop outside this framework.²

These reasons indicate that CICRA had simply perceived the proposal as a technology or product enhancement rather than as an opportunity to fundamentally revise the wholesale connectivity model across the Channel Islands. Unfortunately, the presumption that such a change would happen naturally outside of the process even within a single island, let alone on an area by area basis rather overlooks the reciprocal nature of competition between the islands and the stickiness of the existing retail-based product set. Put simply, neither SMP operator was ever going to risk going alone in making such a change with no guarantee of regulatory support or pan-island implementation so inevitably nothing has happened in the last three years.

To understand the significance of this missed opportunity, it is useful to return to review the requirement for a purely wholesale connectivity model which Hub and Spoke intended to fulfil. The simple premise being to provide aggregated point to point connectivity from an operator's own network site (Hub) to multiple remote locations (Spokes). That operator would then be able to make use of the spoke connections for any of four main purposes:

- To connect together one or more other similar connections, either wholesale or on their own infrastructure to create an end to end service for a retail business user.
- To connect to off-island connectivity to serve as a local access tail, again for business users.
- To connect to own-network content and value-added services, such as Internet / IP feed, SIP voice, media and cloud-based services etc for businesses.
- As part of their own network infrastructure such as mobile radio site backhaul.

The active aggregated delivery would allow for the provision of bandwidth on a granular basis, not simply defined by the physical interface, thus allowing for a more linear rather than stepped

2 CICRA 11/01: Pan Channel Islands consultation on Wholesale Access Products

pricing model based on actual usage requirements and providing potential for greater efficiency both in terms of network capacity utilisation and commercial terms.

The key principle of the model is that it provides just the minimum functionality to fulfil connectivity across the SMP operator's network which other operators are not able to replicate. However, it is sufficiently low level to allow an operator full flexibility and freedom to define their own services and differentiators without recourse to or limits of the SMP operator's wholesale or retail products. The same applies of course to the SMP operator's own business which can take the wholesale components on an identical self-supply basis and thus clearly demonstrate that any services built using them have a true Equivalence of Input (EOI) basis reducing the requirement for regulatory oversight.

In the BCMR, CICRA identifies the above cases as uses for leased-lines in its definition of the wholesale market. This is true, but the existing leased-line products are not necessarily the most appropriate or efficient means of providing them – they just happen to be all that exists. In many cases, this can lead to inefficiencies due to unnecessary additional infrastructure, functionality or over-sizing and ultimately cost both on the part of the SMP operator and the wholesale service taker. This can also ultimately restrict the ability of an operator to innovate within the retail market.

It is clear that the requirements for Wholesale and Retail connectivity services are different and diverging which is not compatible with the current parallel product set. Wholesale services are increasingly used for far more than simply white-labelling and reselling as they were at the introduction of competition. Additionally, demand within the business sector for retail services is more towards true differentiation around value-added services, content and management rather than simply price for an identical service. Unfortunately without any motivation to change, the current parallel product sets are highly likely to remain and stagnate in the middle ground, not serving either sector particularly well, with end customers ultimately losing out whether through higher costs or limited functionality. Unfortunately the retail-minus approach currently proposed by CICRA only serves to accept and reinforce this.

Moving to the questions raised by Cicra in this consultation:

Q1: do you agree with [CICRA]'s proposal to implement a retail-minus price control, strengthened by supporting remedies? If not, what alternatives do you suggest?

No, I do not agree with this proposal as it simply perpetuates the existing parallel connectivity product sets. In this consultation, CICRA notes the time and resources required to undertake a cost modelling exercise. As highlighted above, CICRA has already missed opportunities to identify and facilitate a fundamental change to the wholesale connectivity market through the CIWAP and BCMR processes. To once again see this pushed to the "too difficult" pile, is to miss another. However, rather than examining existing legacy services, a cost modelling exercise should be undertaken to understand the implications and facilitate the introduction of a pure wholesale connectivity suite of products. CICRA states that its approach will *support a timely transition to Next Generation access and services*. However for such services to be effective in the market, they will need a regulatory model which is ready and able to support them. Next Generation services should not simply be about new technology or capital investment. Indeed, SMP operators should be encouraged and able to make informed investment decisions with business cases built purely on wholesale requirements (of which the inputs to their retail business should be part) and a defined and accepted commercial model.

A retail-minus approach to price control suggests an inherent acceptance that an SMP operator's retail products and services should lead and define all aspects of both wholesale and retail markets. This would also imply an acceptance that infrastructure investment should be defined purely by the SMP operator's retail requirements. I would suggest that the fallout associated with JT's announcement of its fibre rollout in Jersey serves to illustrate how this simply can not be acceptable.

Q2: do you agree that the control should be set ex ante? If not, why not?

This would appear to be the most sensible approach initially. However, in future with a robust wholesale-first model and accepted and visible principles of self-supply for SMP operators on an EOI basis, there should be no reason why this could not move to ex post with a lighter touch approach to regulation.

Q3: do you agree that the control should apply to all wholesale on-island leased lines? If not what alternatives do you suggest?

& Q4: do you agree that the control should apply to each wholesale on-island leased line? If not, what alternatives do you suggest?

As indicated above, I believe that a new approach to modelling wholesale services should be encouraged and facilitated by CICRA.

Q5: do you agree that every retail on-island leased line product offered by [SMP operator] must have a wholesale equivalent? If not, what alternatives do you suggest?

& Q6: should all retail price discounts and temporary promotions be mirrored in wholesale level pricing? If not, what alternatives do you suggest?

No, since this is a simplistic and legacy approach to regulation which effectively imposes limitations on an SMP operator's retail arm. While there may be some argument for this in Jersey where JT has been deemed to have Retail SMP, in Guernsey where there is no operator with Retail SMP, it would appear to be unfair to require Sure to provide wholesale equivalents of its retail services. Such a control implies that an SMP operator's retail arm does and should continue to lead all aspects of the markets and product specifications, with other operators simply following on a "me too" basis.

The underlying message with such a legacy and heavyweight approach not only to SMP operators but also to OLOs and the wider market is that Wholesale is something that regulators force operators to do. This can instil an unconscious mindset within the SMP operator that there is no benefit in innovating or providing value-added components at a retail level if they are simply obliged to provide them to competitors at a discount. The result is likely to be a stagnation of both wholesale and retail product sets.

It was appropriate at the introduction of regulation, but I would suggest that after 14 years, the competitive environment within the islands is sufficiently mature that it can embrace and indeed deserves a more progressive approach from CICRA in order to realise the efficiencies and innovation expected by the downstream markets. This can be achieved by facilitating a wholesale-first approach to connectivity on a pan-island basis to the benefit of all operators (including an SMP

operator's own retail arm), however they cannot and should not be expected to do it alone.

Q7: do you agree that the control should be set as a fixed percentage? If not, why not?

& Q8: do you agree that retail minus 20% is an appropriate margin? If not, what alternatives do you suggest?

For the reasons above, I do not believe that a retail minus approach is suitable at any level.

Q9: do you agree that it is not appropriate to use the price control mechanism to address differential pricing? If not, why not?

The development of a pure hub and spoke wholesale connectivity model would likely address this due to the ability to aggregate services across shared infrastructure with pricing based on utilisation.

Q10: do you agree that the term of the price control should be aligned with the market review cycle? If not, what alternatives do you suggest?

This would seem to be a sensible approach. However as highlighted above, I suggest that an intervening process is established to develop a new wholesale service model.

Q11: do you agree with [CICRA]'s proposed use of supporting remedies? If not, why not?

As indicated above, I believe that with a suitable wholesale model and principles of self-supply in place, there should be a far lower requirement for supporting remedies and reporting in future particularly where an SMP operator is able to demonstrate an EOI approach on its retail services using the underlying wholesale components.

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