JT (Jersey) Limited's Response to CICRA's consultation on Retail Price Control Review

1 February 2016

NON CONFIDENTIAL VERSION

1 Executive summary

1.1 We are extremely disappointed to see that the JCRA has continued to push ahead with proposed price control for JT. In our view, the JCRA's approach is flawed, its methodology inaccurate and its conclusions, inappropriate.

1.2 Our response to the JCRA's consultation in May 2015 explained how the analysis supporting the proposal was flawed from both a conceptual and analytical perspective. The JCRA has either ignored our concerns or responded to them in a manner that suggests that the entire process is a perfunctory one. This is of course, redolent of the positions and processes previously adopted by the JCRA recently, not least in relation to WLR (the implementation of which has removed or significantly reduced the need for regulation).

1.3 The JCRA has managed to determine that the prices charged by JT need to be reduced significantly, when all evidence is that they are currently below that which they should be. Furthermore, this conclusion has been reached despite JT showing that the original evidential basis presented was flawed. Our response showed that after correcting for data errors, it was clear that JT's line rental price is low by international standards. The JCRA has not sought to correct these errors at all.

1.4 Moreover, the basis of the JCRA's decision is that (allegedly) JT's headline price is higher than Sure Guernsey's price and this apparent differential has been used as the justification for a steep year on year reduction. As a result the JCRA has ended up conducting a circular exercise of setting the price of two operators by comparing one against the other, at a fixed moment in time, and concluding that the higher price must be brought down.

1.5 This insular approach to regulation means that the JCRA does not consider what is apparent when reviewing the corrected international benchmarking; namely that the prices in both jurisdictions are lower than average (using the JCRA's chosen comparators) and no reduction is needed. This irrational approach to setting prices defies both best practice and logic.

1.6 The absurdity of the JCRA's position is highlighted by the fact that it considers that JT's price should now be higher because Sure Guernsey decided to implement a price increase in Guernsey during the consultation period.

1.7 Further, we think it inconceivable that the JCRA can truly believe that the Sure Guernsey price is an appropriate stable benchmark to set JT's price directly against. Sure Guernsey has consistently increased its retail prices, even during the consultation period. These changes were justified because "*Sure has to remove the subsidy from fixed-line rental prices*" and it was *"experiencing a kind of price realignment[1]"*. Sure Guernsey's own response to the consultation explains clearly that *"Fixed line rental and call charges need to increase[2]".*

1.8 The other main issue related to the "benchmarking" conducted by the JCRA is that it focuses only on the headline line rental price, ignoring the fact that 28% of our customers are on the PrimeTalk tariff and only pay a fraction of this price. Our weighted average retail price is significantly lower than Sure Guernsey's average price[3]. If the JCRA considers that the cross-subsidy provided to pensioners to be inappropriate, then it should say this clearly. What is

[1] Guernsey Press, April 10 2015
[2] Sure Guernsey response to CICRA consultation, 8 May 2015
[3] We understand that Sure Guernsey has approximately 300 customers on its £3.99 telephone assistance scheme (TAS) tariff for customers on benefits (details of the tariff are not available on its website). This represents approximately 1% of line rental customers and has much less impact on the weighted average price.

inexcusable is ignoring the current market reality and simply insisting that *"Jersey consumers are paying significantly more for their fixed lines phone services[4]"*.

1.9 Our recent decision to stop offering PrimeTalk for new customers only (misstated by the JCRA) will not bring JT additional revenues (as is misunderstood by the JCRA). Rather, the action of closing PrimeTalk to new customers means that we have merely put a stop to the increasing losses that we were incurring as a result of the tariff remaining open.

1.10 By continuing to ignore the impact of the subsidy for PrimeTalk customers, the JCRA is not taking the multi-million pounds of annual costs associated with providing the heavily subsidised service into account in its analysis. That being the case, the perhaps unintended consequence of this would be to force JT to immediately discontinue the current tariff for existing customers. This consequence, unintended or otherwise, should be explicitly made clear as part of the JCRA's decision making process.

1.11 We would suggest that the JCRA heed the suggestion previously made by the Royal Court in the course of our successful appeal against the implementation to WLR, that the JCRA should work with us rather than against us.

[4] CICRA, Pan-Channel Island Consultation on Retail Price Control Review: Consultation Document, March 2015, p9

2 Previous Submissions

2.1 Given the contents of the Initial Notice, we are concerned that the JCRA has failed to take into account properly or at all, the comments previously made in relation to the Consultation (as occurred previously and most notably in relation to WLR). We therefore repeat and adopt those comments as part of our submission to this Initial Notice.

3 Introduction of WLR makes the proposed retail price control superfluous

3.1 There has been a systematic and universal shift by regulators around the world away from retail price regulation and towards wholesale level regulation, particularly when steps have been taken to reduce market impediments and/or to facilitate competition.

3.2 The introduction of a wholesale line rental (WLR) product in Jersey from June 2015 has removed or significantly reduced the need for retail price regulation in the Channel Islands. Indeed, the European Commission considers that the introduction of WLR has *"significantly reduced the barriers to entry"*[5] in retail line rental markets. Based on the EC's three criteria test, there is no need to regulate the retail market if WLR reduces barriers to entry in this market. The last retail markets were removed from the list of relevant markets susceptible to ex-ante regulation in 2014.

3.3 In Jersey **[Redacted]** customers were connected using WLR in the seven months to December 2015. This represents approximately **[Redacted]** of JT's original line rental customers. The fact that customers were able to and did in fact move in such numbers and with such rapidity clearly demonstrates that the introduction of WLR has indeed reduced barriers to entry and/or allowed competitors to successfully enter the retail market and/or facilitated competition. This strong take-up in only seven months shows that there is now tangible competition in the retail market. Moreover, that competition is only ever going to increase so WLR has achieved its goal.

3.4 Having failed to take into account properly or at all the existence and/or impact of WLR, the JCRA must therefore revisit its original assumption that regulation of this market is necessary.

3.5 Moreover, if following such a review the JCRA were still hesitant to deregulate completely at this stage, it should only set out interim controls and look to step back from intrusive regulation as soon as possible.

3.6 In the initial notice, the JCRA states that *"if the market was considered to be working well for consumers the JCRA would contemplate removal of the price control in advance of the three year control period*."[6] However, whilst the JCRA sets out the different types of evidence that might be analysed at that stage to determine whether to reduce the intervention, it singularly fails to identify or to provide any defined factors that would prompt such a review; nor indeed, does it commit to a review in any event.

[5] "Solving problems at the sources: why telecommunications regulation should focus on wholesale, not on retail, markets" Iratxe GURPEGUI and Przemyslaw KORDASIEWICZ (2007) http://ec.europa.eu/competition/publications/cpn/2007_1_49.pdf

[6] CICRA, 2015, Retail Price Control 2015. Initial Notice. Determination issued to JT (Jersey) Limited. Page 13.

3.7 We think that given the introduction of WLR has a significant impact on the market, such that further regulation is unnecessary. If the JCRA disagrees, it should regulate on an interim basis only and set clear parameters to determine when and in what circumstances, any price control would be reviewed.

4 The JCRA needs to account for impact of PrimeTalk tariff

4.1 The JCRA argues that PrimeTalk should not be included in the fixed line bundle, despite the fact that the majority of our most “vulnerable customers”[7] who only purchase a standalone fixed service will be PrimeTalk customers. We support the need to protect vulnerable customers and consider this a key aim when introducing any regulation. Given this objective, it seems surprising that the JCRA has excluded PrimeTalk from its analysis.

4.2 PrimeTalk, consisting of a heavily discounted price for pensioners, is held by 28% of line rental customers, and 53% of line rental only customers. This is indeed the tariff used by most of the vulnerable customers in Jersey[8]. Yet when implementing a price control policy apparently, the JCRA has ignored the tariff. Not only is this wholly illogical but it produces a patently unreasonable result (and one no reasonable regulator could have reached).

4.3 JT fully agrees that the PrimeTalk tariff is a very badly structured one assuming, as it does, that the elderly are the most vulnerable. This is not a valid assumption in today’s world and its continued provision is fundamentally flawed when assessed against any reasonable criteria. While JT has attempted to deal the matter over the last number of years, it has proved impossible to gain the necessary alignment and consensus to press ahead with the necessary changes. Whatever the answer to this extremely challenging conundrum, like the proverbial elephant in the corner, it is not to simply ignore its existence when analysing the market in which it is a major constituent.

4.4 Further, the JCRA has misunderstood our position in relation to PrimeTalk. Whilst we have stopped offering the tariff to new customers, all existing customers continue to be offered the tariff. There is no reason for any of the existing customers on PrimeTalk to change tariffs given the fact that it is "heavily discounted" and provides great value. Moreover, none of the OLOs provide or indeed want to provide any service at such a discounted price. Therefore, as a matter of logic and practice, we expect that a significant proportion (if not all) of our PrimeTalk customer base (which represents 28% of our line rental customers) will continue to pay the discounted rate for PrimeTalk over the entirety of the course of this three year price control.

4.5 In its report, JCRA states that *“The discontinuation of its Primetalk tariff will increase JT’s revenues by more than £2m over the next four years which will help JT to partly offset the lost revenues from lower retail prices.”*[9] It is not clear how the JCRA have come up with this figure. Particularly since we have not discontinued the tariff.

4.6 Moreover, in continuing to ignore the impact of the subsidy for PrimeTalk customers, the JCRA has failed to take into account properly or at all, the significant amount of annual cost associated with providing the heavily subsidised service such that any analysis carried out by the JCRA is patently and fatally flawed.

4.7 The PrimeTalk tariff is a subsidy that JT offers to a distinct set of (potentially more vulnerable) customers. There are arguments for querying the validity of this cross-subsidy towards these customers. If the JCRA thinks it is inappropriate for some customers to be paying more so that pensioners can get a discounted rate, it should state this clearly and set out who it would be

[7] The JCRA have noted that broadband should not be included in the bundle as it wants to protect vulnerable customers who only take out a standalone fixed service.

[8] Notwithstanding the fact that there are many PrimeTalk customers who are not vulnerable, but benefit from the cheaper price

[9] CICRA, 2015, Retail Price Control 2015. Initial Notice. Determination issued to JT (Jersey) Limited. Page 18.

appropriate to offer a subsidised service for. However JCRA has not done this. It has merely pretended that these PrimeTalk customers do not exist and simply insisted that *"Jersey consumers are paying significantly more for their fixed lines phone services.*[10]*"*

4.8 If JCRA continues to ignore the impact of providing this subsidy to PrimeTalk customers, this will force JT to consider discontinuing the tariff for existing customers and offer a less generous subsidy at similar levels to Sure Guernsey. The JCRA needs to acknowledge that the unintended consequence of the price control it is proposing is to force JT to discontinue this tariff.

4.9 It is worth noting that the last time JT proposed discontinuing the PrimeTalk tariff, the matter ended up being debated in the States Assembly. In light of the responsibilities of the Assistant Chief Minister – Finance, Competition, Innovation and Digital, we are of the view that the JCRA must explicitly raise the consequences of the proposed price control with him so that there is no doubt as to the impact of what the JCRA is directing JT to do.

4.10 Moreover any regulation producing that effect would be contrary to the express statutory obligations and responsibilities applicable to the JCRA. Articles 7(2)(f) and 7(3)(e)[11] of the Telecommunications (Jersey) Law 2002 concern the provision of services to those who are disabled or have limited financial resources and involve consideration of cross subsidies put in place by service providers. The proposed price controls patently ignore the requirements of these Articles.

4.11 Further, in undertaking its market review, the JCRA has deliberately ignored the fact that there are a significant number of customers who are paying a heavily discounted rate and the costs associated therewith. It has also failed to consider properly or at all, the interests of the customers it is required to protect. In addition, it has failed to consider properly or at all and/or to identify properly or at all which customers it wishes to protect and how subsidised services should be incorporated into a price control. It has also failed to consider properly or at all, the full consequences of the proposed price control (i.e. the removal of the PrimeTalk tariff).

5 As our separated accounts show losses for retail services, international benchmarking is necessary to justify JCRA's assertions

5.1 As set out in our independently audited separated accounts, JT has consistently made losses for its retail fixed line services. In 2014, we made a loss of £1,234,000 for the basket of fixed line access and fixed retail calls. Similarly in 2013 JT made a loss of £2,014,000[12]. Despite this, the JCRA still purports to conclude that JT's prices are too high. However no evidence has been presented to support this conclusion.

5.2 Whenever the JCRA has sought to introduce proscriptive changes to prices, it has typically relied on international benchmarking to justify these decisions. When the JCRA consulted on reducing MTRs in July 2015, it relied on a benchmark against the rates in the UK. When it proposed a price control for wholesale broadband prices in April 2014, it used a benchmark of prices from the UK, Australia and New Zealand. In fact the only times the JCRA has not made

[10] CICRA, Pan-Channel Island Consultation on Retail Price Control Review: Consultation Document, March 2015, p9

[11] http://www.jerseylaw.je/law/display.aspx?url=lawsinforce%2fconsolidated%2f06%2f06.288_TelecommunicationsLaw2002_RevisedEdition_1January2013.htm

[12] JT Group Limited Separated Regulatory Accounts: For the year ended 31st December 2014, Page 15

use of international benchmarking was when it was implementing an interim control which extended the previous prices[13].

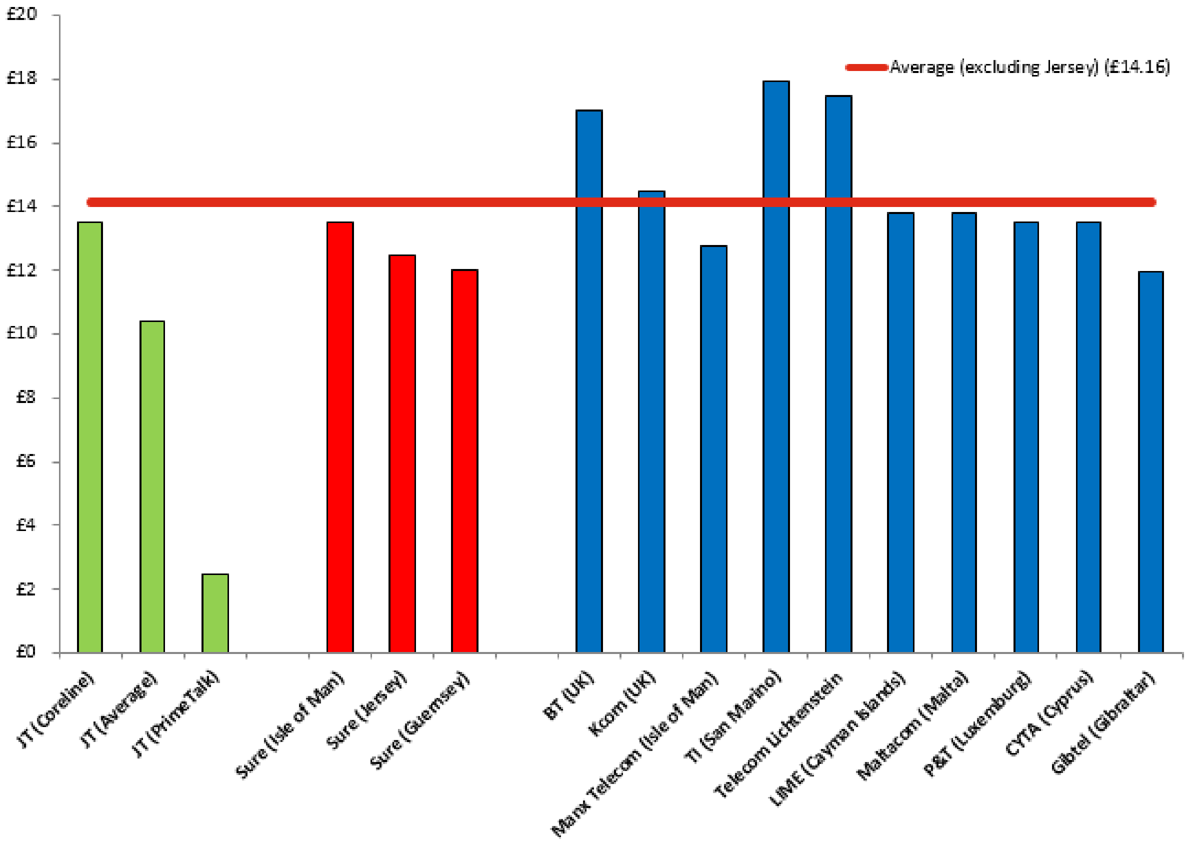
5.3 This is the same process in all the sectors that the JCRA regulates. Yet unilaterally and without any or any proper consideration or consultation, the JCRA proposes to abandon international benchmarking and to adopt single peer benchmarking, without considering properly or at all the suitability of that peer and/or its regulator and/or its regulatory environment.

5.4 In our consultation response we set out a number of flaws with the international benchmarking presented in Frontier's report. The JCRA has acknowledged this but not corrected for it on the basis that the final price was not determined through this international benchmarking.

5.5 It is not credible to decide to simply not correct these errors by claiming that these are not important. The benchmarking was important as it was used initially to support the view that our prices were high. Therefore, attempting to maintain this position without correcting for errors defies logic. The JCRA needs to correct for the errors that JT identified, re-present the updated benchmarking analysis and then explain why (despite this) it still considers that JT's prices are excessive.

5.6 Having corrected for these errors, JT's price for line rental is lower than the average for the benchmark countries.

Figure 1: Updated benchmarking of monthly line rental charges[14]



[13] For example when setting Fixed Termination rates in September 2014

[14] We have used the same comparators here as those in the Frontier report with the exception that we have also added Sure Jersey and Sure Isle of Man to the comparison to show the relative price charged. These are not included in the average benchmark calculated

5.7 Figure 1, the details of which we presented in our response to the consultation, shows that JT's standard price is in line with the average prices charged by a group of relevant international comparators for line rental. Our average price, which accounts for PrimeTalk customers, is not only significantly below the average price of international comparators but also significantly below that charged by Sure Guernsey.

5.8 The JCRA stated in its interim notice that our analysis was focused on line rental, when the relevant measure was the price for the basket of line rental and calls. However, our analysis had focused on this because Frontier's own flawed analysis had already showed JT's price was below the benchmark average for every basket. Therefore, the focus of our analysis was on the benchmark where Frontier considered that our price was higher than the comparators' average price.

5.9 The JCRA did not correct for the flaws in the international benchmarking because it asserts that *"the key basis for the recommended level of control did not ultimately rely on these comparator jurisdictions"*[15] Whilst it is correct that the level of price reduction proposed for JT was based on a simple comparison with Sure Guernsey[16], the international benchmarking was used as the basis for considering that JT's prices needed to be reduced. Without this control set of prices from competitive jurisdictions, it would be inappropriate to conclude that JT's price needed to be reduced. Accordingly, the conclusion reached by the JCRA that JT's prices needed regulation is and was wrong.

6 Inappropriate for JCRA to set two prices on the basis of benchmarking one against the other

6.1 The JCRA propose to set JT's price based on benchmarking against the price charged by Sure in Guernsey. As noted above, this is a departure from previous practice and without any or any appropriate consultation or assessment, a departure from reasonable practice. We are unaware of an instance when the JCRA has conducted such an insular assessment before.

6.2 There is a circularity issue associated with using each operator (JT and Sure Guernsey) as the 'control' benchmark country when regulating the price of both. The idea behind benchmarking analysis is to find comparators whose prices have been set externally – i.e. outside the jurisdiction under consideration. However, the price that Sure Guernsey charges is not externally set – it is instead influenced by regulation put in place by the same regulatory body. By only looking at these two prices, it is unclear whether both prices are expensive or cheap by international standards.

6.3 Moreover, Sure Guernsey's price is an inappropriate price to use as a stable control benchmark. Sure Guernsey have acknowledged, when justifying their recent price increase, that their line rental price was heavily subsidised:

> *"Sure's head of product, Mike Fawkner-Corbett, said the changes were made in line with the new competitive environment. 'It's an exciting time for us,' he said. 'Competition will soon be introduced in the Channel Islands fixed-line market and to ensure that all operators can compete fairly, Sure has to remove the subsidy from fixed-line rental prices.'*
>
> *He explained that the subsidy, that had been developed over a number of years, had been introduced to maintain low prices for fixed-line customers. 'Up until now, fixed-*

[15] CICRA, 2015, Retail Price Control 2015. Initial Notice. Determination issued to JT (Jersey) Limited. Page 20.
[16] Which we will discuss in detail in Section 6

line rental prices in Guernsey have been a lot less expensive than in the UK, so we are experiencing a kind of price realignment through these changes. The subsidy needs to be removed so that we can compete fairly, making sure the retail price is higher than the wholesale price."[17]

6.4 Sure Guernsey's own response to the consultation explains clearly that *"Fixed line rental and call charges need to increase"*[18]. As we stated previously, Sure Guernsey have increased their prices rapidly over the past ten years, whilst our real price has stayed flat. Given these trends, and Sure Guernsey's intention to increase prices, it makes more sense to assume that our prices are more appropriate and the Sure Guernsey price should be allowed to increase rather than the other way around.

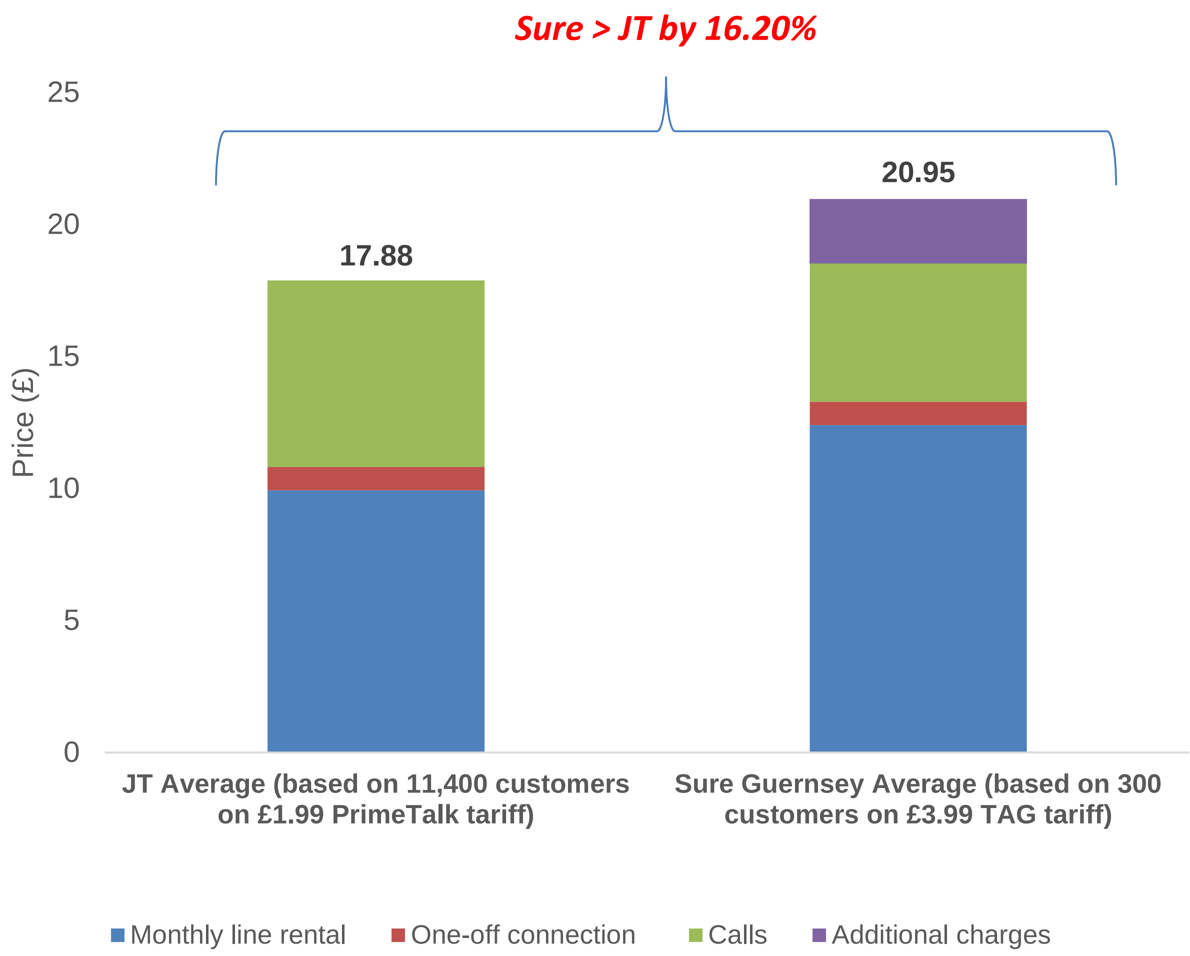
6.5 Moreover if the JCRA wants to focus all its analysis on comparing our price against that of one control operator, it has to look at the entirety of revenues associated, or it is not a fair comparison. JCRA must account for Sure Guernsey's additional charges made to customers that use alternative payment methods to direct debit, receive paper bills and make late payment. We set out in our response how these charges mean that Sure Guernsey can expect to receive £2.42 more per customer. JCRA has ignored our concerns about these additional charges explaining that *"There is a valid argument that such charges improve efficiency of operations and therefore deliver savings and eliminate unfair cross subsidies between late payers and those that pay on time for example. It is open to JT to introduce such charges outside the price control mechanism"*[19].

6.6 Notwithstanding the fact that this support goes against previous CICRA guidance regarding these additional charges, this also explains why the Sure Guernsey price is not an appropriate comparator. Sure Guernsey is able to subsidise the price of its fixed line services because of these additional revenue streams. As JT cannot rely on similar revenue streams, it is not fair to compare these prices against each other. Table 1 shows that after accounting for the additional prices that are charged by Sure Guernsey, JT's price would be only 4.5% higher than Sure Guernsey.

6.7 After taking the JCRA's own analysis[20] and accounting for these additional charges as well as the discounted rates that both JT and Sure Guernsey provide to some customers (PrimeTalk for JT and TAS for Sure), JT's price is actually 11.3% lower than Sure Guernsey's. This is shown in Figure 1 and Table 1. Therefore, even if Sure Guernsey is considered the relevant comparator to JT – the final determination should not be that JT has to lower its prices as the price is not higher than Sure Guernsey's.

[17] Guernsey Press, April 10 2015
[18] Sure Guernsey response to CICRA consultation, 8 May 2015
[19] Frontier, 2015, Retail Price Cap Review in the Channel Islands. A report prepared for CICRA. Page 15.
[20] Monthly line rental, one-off connection and calls figures taken directly from CICRA, 2015, Retail Price Control 2015. Initial Notice. Determination issued to JT (Jersey) Limited. Page 21

Figure 1: Comparison of JT's and Sure Guernsey's prices, accounting for subsidised tariffs and additional charges



6.8 JT's price, after accounting for these factors, is now over 11% lower than Sure Guernsey's. Therefore if this price control is brought into force the price for JT will end up being over 25% lower than the equivalent price charged by Sure Guernsey.

7 **Table 1: Comparison of JT's and Sure Guernsey's prices, accounting for subsidised tariffs and additional charges**

Component (£)	JT Standard Tariff	Sure Guernsey Standard Tariff	JT Average *(based on 11,400 customers on £2.50 PrimeTalk tariff)*	Sure Guernsey Average *(based on 300 customers on £3.99 TAS tariff)*
Monthly line rental	13.50	11.99	9.93	11.91
One-off connection	0.88	0.88	0.88	0.88
Calls	7.07	5.24	7.07	5.24
Additional charges	0.00	2.42	0.00	2.42
Total	**21.45**	**20.53**	**17.88**	**20.45**
Difference (%)	***4.5%***		***-11.3%***	

8 The terms of the proposed price control have changed without explanation

8.1 The revised JCRA calculation in the initial notice has now shown only a 14% difference between the JT prices in Jersey and the prices in Guernsey and the determination is for a price control of RPI – 7% for two years. This is designed to achieve parity in two years. It is not clear why JCRA has determined that parity must be reached over a two year period rather than three. The JCRA has always used a three year glide path when regulating prices in the past and we are surprised that it has shortened this without consulting on its reasoning.

8.2 Initially in the consultation, the JCRA found that prices were 33% higher in Jersey than in Guernsey. Frontier noted that to bring prices in Jersey in line with those in Guernsey, an RPI-12.5% price control over a 3 year period would be needed. However, it was thought that lowering prices by such a steep amount would limit downstream competitors being able to enter the market and compete. Neither Frontier nor the JCRA felt that the price control needed to be at the level to ensure parity, The JCRA proposed a price control of between RPI – 4% to RPI-10% over a 3 year period, with the final figure determined based on the *"relative importance of facilitating downstream competition and achieving greater parity in retail prices across the Channel Islands*"[21].

8.3 In the Initial Notice, the JCRA has chosen to reduce JT's prices by 7%, without explaining why it has chosen this percentage, given the range originally consulted on and accounting for the new price difference identified.

8.4 The rationale for the new price control mechanism has not been explained clearly or indeed, at all by the JCRA whether in the Initial Notice or elsewhere.

8.5 Moreover, the decisions reached by the JCRA in relation to the price control mechanism are illogical and wrong, and the consultation process itself flawed in that, for example:

- the JCRA now considers that JT's price needs to be reduced by the full differential to achieve price parity yet this was not considered as part of the consultation;

[21] Frontier, 2015, Retail Price Cap Review in the Channel Islands. A report prepared for CICRA. Page 18.

- the JCRA has now discounted the option of only applying a 4% reduction yet this was the reduction proposed when it thought that the price difference was much larger;
- the JCRA has used a two year glide path for the price reduction rather than the three year glide path proposed in the consultation.