JT (Jersey) Limited

Determination in respect of Wholesale Leased Lines

Final Notice

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TELECOMMUNICATIONS (JERSEY) LAW 2002

DETERMINATION IN RESPECT OF WHOLESALE LEASED LINES - JT (JERSEY) LIMITED

FINAL NOTICE

1. On 26 July 2012, the Jersey Competition Regulatory Authority ("***JCRA***") issued an Initial Notice ("***IN***") under Article 11(1) of the *Telecommunications (Jersey) Law* 2002 ("***the Law***") concerning a proposed determination in respect of the price to be charged by JT (Jersey) Limited ("***JT***") for wholesale on-island leased lines[1] in Jersey.

2. The JCRA received five non-confidential responses to the IN from Teletech Solutions ("***Teletech***"), JT, Newtel Limited ("***Newtel***"), Jersey Airtel Limited ("***JAL***") and Cable & Wireless Jersey Limited ("***CWJ***"). The responses, and the JCRA's comments, are summarised below.

Legal Background & Regulatory Framework

Legal Background

3. Article 16 of the Telecoms Law provides that the JCRA may include in licenses such conditions as it considers necessary to carry out its functions. The Telecoms Law specifically provides that licenses can include:

    - conditions for the prevention or reduction of anti-competitive behaviour; and
    - conditions allowing the JCRA to make determinations.

Regulatory framework

4. In April 2010, following a review of the markets for telecoms services in Jersey[2], the JCRA made the following decision with respect to significant market power ("***SMP***") in markets relevant to this IN:

    - ***On-island Wholesale Leased Lines:*** *JT has SMP in this market;*

5. Condition 33.2 of the licence issued to JT provides that:

    "The JCRA may determine the maximum level of charges the Licensee may apply for Telecommunications Services within a relevant market in which the Licensee has been found to be dominant. A determination may:

    a) provide for the overall limit to apply to such Telecommunications Services or categories of Telecommunications Services or any combination of Telecommunications Service;

[1] Unless otherwise stated all references in this document to "leased lines" refers to on-island leased lines in Jersey.

[2] JCRA, *Response to the Consultation Paper 2009 – T3, "Review of the Telecommunication Market in Jersey" and Decision on the Holding of Significant Market Power in Various Telecommunications Markets*, 21 April 2010, see http://www.cicra.gg/_files/100420%20market%20review%20decision.pdf

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 the determination applies."

6. This condition therefore allows the JCRA to regulate the prices that JT charges for telecommunications services in a way and for a time that it deems appropriate, provided that JT has a dominant position in the relevant market in which those services are supplied.

Summary of representations and objections

7. The section below summarises the issues raised by interested parties in submissions and the JCRA's response. Copies of these submissions have been posted on the JCRA's website, and are available for inspection at the JCRA's offices.

Proposal welcomed

8. The JCRA received no submissions that objected to increasing the discount applied to wholesale leased lines from 9% of JT's retail leased line price to 20%.

9. Teletech, JAL and Newtel's submissions responded positively to the IN, while CWJ's simply stated that the proposed determination must be implemented without delay and JT stated that it "does not object to… basing Jersey on-island leased lines charges at the same 'retail-minus' level as provided by Cable & Wireless (C&W) in Guernsey"[3].

10. While the JCRA received no objections to the proposed pricing, all parties did offer views on a range of issues they considered relevant to the IN.

Bigger discount

11. Newtel and JAL submitted that the discount applied should be greater than 20%. Newtel submitted that a 20% discount should be considered "the absolute minimum discount that should be implemented"[4] and contended that, given the examples provided in the IN, a wholesale charge of retail minus 28% would be more appropriate.

12. JAL requested that the JCRA increase the retail margin even further, advocating a wholesale price methodology of retail minus 40% - 60%.

13. JAL provided the following comparison table, highlighting differences between wholesale prices for particular leased line services in Jersey (offered by JT) and Guernsey (offered by Cable & Wireless Guernsey Limited ("***CWG***")), and showing a significant difference between wholesale prices charged by CWG for certain specific leased line services and those charged by JT for the same services:

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[3] JT (Jersey) Telecom Limited, *JT's Response to Initial Notice Wholesale Leased Lines – Review of Price Controls*, Section 2, 28 August 2012.

[4] Newtel, *Wholesale Leased Lines, Review of Price Controls: Proposed Directions to JT (Jersey) Limited*, paragraph 1, 27 July 2012.

	Guernsey Prices of 1xE1 (per month)	Jersey Prices of 1xE1 (per month) after 20% discount as proposed by the JCRA (inc GST)	Jersey Prices of 1xE1 (per month) after 40% discount (inc GST)
On-Island (same exchange)	£107	£237	£178
On-Island (different exchange)	£193	£237	£178

14. In response, the JCRA observes that different mechanisms for setting wholesale leased line prices exist in Jersey and Guernsey. A result of this is that prices currently differ between the two islands. JT has applied a retail minus 9% price mechanism for wholesale leased lines. In contrast, a RPI-X mechanism for setting wholesale leased line prices has been enforced in Guernsey. The implementation of differing price mechanisms creates unique market dynamics, which can result in different prices (wholesale and retail). The focus of the IN was to implement an interim measure that:

    - Reduces a significant barrier to competition;
    - Can be implemented quickly;
    - Is consistent with the pricing of other regulated wholesale services in Jersey; and
    - Replicates average conditions in Guernsey for leased lines.

15. The JCRA primarily issued the IN because the 9% margin between the retail and wholesale prices for leased lines was considered insufficient to allow OLOs to compete effectively with JT in the provision of retail leased lines, creating a barrier to competition. By retaining the ‘retail-minus’ mechanism, any change can be implemented quickly and will remain consistent with the pricing of other regulated wholesale services in Jersey. The final consideration, replicating conditions in Guernsey, informed the magnitude of the increase in the retail margin.

16. Understanding the dynamics of implementing a ‘retail-minus’ price mechanism is important when comparing leased line markets in Jersey and Guernsey, because increasing the margin afforded to OLOs increases their ability to compete in the retail market. If OLOs “compete away” the additional revenue gained through a reduction in wholesale prices, it is expected that this will lead to a reduction in overall retail prices. Lower retail prices will serve to further reduce the wholesale price and create a cycle in which price reductions may go through multiple iterations. As prices fall, so does the value of the 20% retail margin, until the value of the 20% margin equals the cost of retail provision of the service, plus an economic return on the investment. The JCRA expects these dynamics may result in wholesale prices falling further than the initial value of the additional 11% margin (20% less the current 9%).

17. Setting a new ‘retail-minus’ margin in Jersey informed by benchmarking the difference between prices in Jersey and Guernsey would result in even lower prices, due to the iterative process of ‘retail-minus’ pricing, and could create a risk that wholesale prices would be set below cost. The application of ‘retail-minus’ pricing in Jersey means that replicating the average margin, rather than average price levels, experienced by OLOs in Guernsey is most likely to result in comparable outcomes. CWG submitted in January

2012 that the average retail margin for on-island leased line services in Guernsey is 22%. This figure ultimately informed the JCRA's IN.

18. Newtel's submission advocated implementing the 'retail-minus' percentage given by the upper bound of the jurisdictions benchmarked in the IN. The purpose of the benchmarks in the IN was not to help determine the wholesale discount afforded to leased lines, but to demonstrate that the retail minus 9% mechanism was significantly out of step with other jurisdictions. As noted in paragraph 15 above, the JCRA primarily selected the 20% discount for the purpose of implementing a discount that replicates, on aggregate, the discount enjoyed by OLOs in Guernsey in order to create a degree of pan-Channel Island uniformity for leased line pricing.

Additional measures

19. Teletech urged the JCRA to consider additional measures that permit customers to exit agreements entered into (at least) on or after 1 April 2012, as many customers sign long-term contracts in order to secure discounts.

20. The JCRA notes the concerns raised by Teletech. However, the primary role of the JCRA is to regulate the telecommunications market in Jersey and interfering with private contracts is not something the JCRA would do lightly. As the number of customers who are likely to have signed contracts for leased line services in the last five months is most probably small, relative to the size of the market, the JCRA sees little value in taking the unprecedented step of voiding contracts between telecommunications operators and private customers.

21. The JCRA notes that there is nothing to stop operators adjusting their contracted prices to pass though any price reductions to the customer as a means of building goodwill, an action which the JCRA would encourage.

Customer focused migration

22. Teletech stated that migrating business customers from one operator to another is not necessarily straightforward, requiring coordination between both operators and the customer. It submitted that a customer-focused migration process should be put in place when the new pricing comes into effect.

23. The scope of the determination focuses solely on price terms for the wholesale leased line service. The JCRA issued an Initial Notice addressing some non-price terms for wholesale leased line services (among other things) on 21 September 2012[5]. Submissions in relation to that Initial Notice close on 22 October 2012 and the JCRA encourages Teletech, and others, to outline any concerns they have with the non-price terms of JT's leased line services via responses to that Initial Notice.

Other comments

24. JT identified an error on page 9 of the IN, where it is stated that "copper broadband services are prices at a uniform retail minus 20%, whereas the discount on the recently introduced fibre broadband service ranges from 20% up to 40%." JT noted that it sets prices for wholesale copper broadband at a uniform retail minus 40% and contended that

[5] Jersey Competition Regulatory Authority, *Review of Non-Price Terms for Wholesale Leased Line and Bitstream Products – Initial Notice: Direction to JT (Jersey) Limited*, September 2012.

consequently, the following statement in the IN was incorrect and misleading: "This suggests that the appropriate margin for wholesale services may be increasing over time. These more recent price calculations indicate a step change may have occurred that is not reflected in the current leased line pricing".

25. The error identified by JT does not affect the JCRA's conclusion. That wholesale broadband services are priced by JT on a retail minus 40% basis, rather than retail minus 20%, further reinforces the fact that pricing wholesale leased lines at retail minus 9% is significantly out of step with the pricing of other major regulated services in Jersey and further afield.

Implementation date

26. JT submitted that it will "seriously struggle" to implement the change to wholesale prices with effect from 1 April 2012, as it is currently installing new billing system and work flow processes, which are due to come on stream during Q4 2012. JT asserted that it would be simple to make the change to wholesale leased line prices effective from 29 December 2012, which would allow JT to make the changes at the start of its billing cycle and would avoid adding additional workload for JT's IT and billing teams.

27. Newtel endorsed the JCRA's proposed implementation date of 1 April 2012.

28. The JCRA notes that many national regulatory authorities worldwide backdate regulatory pricing decisions, and that an implementation date of 1 April 2012 had been discussed with operators during the first half of 2012. Additionally, the JCRA is currently in the process of issuing directions or determinations for a range of services, including mobile and fixed interconnection rates. The date of implementation for each of these directions and determinations is 1 April 2012 and for the purposes of consistency, the JCRA considers an implementation date for this determination of 1 April 2012 remains appropriate.

29. The JCRA is not satisfied that the introduction of a new billing system and work flow procedures presents significant barriers to the calculation of any rebates payable to wholesale customers as a result of the backdating of the price change. However, in the interests of reducing the burden on JT of implementing the change, the JCRA is prepared to allow for any rebates for the period 1 April 2012 to 9 November 2012 to be paid by JT to its wholesale customers on or before 29 December 2012. If JT is unable to calculate the value of any rebates, the JCRA would encourage it to invite OLOs to calculate the impact of the price change on previous payments made by them for wholesale leased line services (i.e. the rebate due to them from JT) and to submit their calculations to JT for review. For the avoidance of doubt, the JCRA expects JT to implement the price change for wholesale leased line services resulting from the determination on 9 November 2012 in respect of any leased line services supplied after this date.

Retail Price control

30. Newtel expressed concern that JT may attempt to manipulate wholesale prices by increasing the retail price of on-island leased lines, and submitted that a retail price control of on-island leased lines would be appropriate.

31. Paragraph 16 above outlines the dynamics the JCRA expects might occur on implementation of the new pricing. Any increase in retail prices would be unexpected

and could constitute an abuse of a dominant position by JT. The JCRA is satisfied that Licence Condition 34 of JT's Licence and the *Competition (Jersey) Law* 2005 provide the JCRA with sufficient tools to investigate and, if necessary, punish any anti-competitive behaviour, should it arise.

Changes to the application of the 'retail-minus' pricing mechanism

32. JT submitted that it currently links wholesale prices to the price of the comparable JT Retail service, such that any discounts offered at the retail level for long-term contracts are reflected in the wholesale prices. JT stated that, currently, the 'retail-minus' pricing mechanism for setting wholesale prices uses the equivalent discounted retail price as the retail price from which the 9% margin is removed. JT stated that this practice would be discontinued if a retail minus 20% framework were implemented. JT submitted that this would be consistent with the approach taken by CWG in Guernsey.

33. The purpose of 'retail-minus' pricing is to set the price of a wholesale service by removing the avoidable retail costs of the equivalent retail service, thereby allowing equally efficient retail operators to compete with the retail arm of the vertically integrated operator. The JCRA's view is that setting a wholesale price for a three year wholesale leased line service by applying the regulated 'retail-minus' method to a one year retail leased line price rather than the equivalent three year retail leased line service would not be consistent with this determination.

34. In addition, the JCRA notes that JT's retail prices will remain subject to JT's Licence Condition 34.1 and the Competition (Jersey) Law 2005.

35. JT has submitted that its proposed approach to wholesale pricing is consistent with the approach taken by CWG. If JT has concerns about the pricing behaviour of CWG in relation to leased line services with terms longer than 1 year, then it is encouraged to raise those concerns formally through the appropriate channels.

Determination

36. For the reasons set out in the IN and the paragraphs above, the JCRA has decided to issue the following determination under Condition 33.2 of JT's licence:

    - The maximum price charged by JT for wholesale leased lines shall be the price of the equivalent retail service supplied by JT, minus 20%.
    - The determination shall take effect on 9 November 2012.
    - This determination shall be deemed to have come into effect on 1 April 2012. Any rebates payable by JT in respect of wholesale leased line services supplied between 1 April 2012 and 9 November 2012 shall be paid by JT to its wholesale customers on or before 29 December 2012.

By order of the Board of the JCRA **9 October 2012**