Reference :T1448J
Please quote in all correspondence

20th December 2019

Daragh McDermott
JT
PO Box 53
No 1 The Forum
Grenville Street
St Helier
Jersey JE4 8PB

BY EMAIL ONLY

Dear Daragh,

Telecommunications Licence – Contravention of Licence Condition 34
Notification of Direction

Thank you for your letter of 28 November 2019.

Your letter does not contain any substantive submissions on the analysis accompanying my letter of 11 November 2019 to Graeme Millar ("the 11 November Letter"). We note your recognition that JT is required to use the Model to assess whether each retail broadband product provided by JT passes a margin squeeze test.

We also note the steps taken by JT to adjust its retail prices to achieve a positive margin between your wholesale and retail prices for the currently contravening products. The Authority is disappointed that compliance has been achieved by means of a retail price increase, and intends to review whether action is required in relation to JT's wholesale pricing of its broadband products as a matter of priority.

Representations have been received from one other party on a confidential basis, but these do not propose that the JCRA revisits its substantive analysis either. Instead, they ask the Authority to open a further investigation and to consider imposing a fine on JT and/or compensation for harm suffered to JT's retail competitors.

The Authority has accordingly decided to make a direction in the terms proposed in the Annex 2 of the 11 November Letter. The date for compliance is fixed at 14 February 2020 (that being the date on which you have advised that JT's final revised pricings will be taking effect). The reasons for the Authority's decision are as set out in Annexes 1 and 3 of the 11 November Letter. A copy of the final Direction is attached hereto as Annex A and will also be published (together with this letter) on the Authority's website. A copy of the 11 November letter is attached as Annex B for your ease of reference.

The Authority will consider separately whether to exercise its powers to impose a financial penalty (pursuant to Article 19A of the Telecommunications (Jersey) Law 2002 ("the 2002 Law") and/or whether to make any further direction in connection with this matter, and will notify JT in due course of any proposed action that the Authority is minded to take.

Yours sincerely

Michael Byrne
Chief Executive

ANNEX A : DIRECTION

1. The Authority directs JT to adjust and maintain the wholesale and retail prices for its fixed-line broadband products such that the combination of those prices does not give rise to a margin squeeze.

2. JT shall ensure that it complies with this direction no later than 14 February 2020.

3. JT's compliance with this direction is to be assessed by means of the excel spreadsheet previously provided to JT using the parameters in that Model (**"the Model"**)[1].

4. JT's prices shall be considered to give rise to a margin squeeze where the Model indicates a negative margin in respect of any retail fixed-line broadband product which JT currently supplies to any of its customers (irrespective of whether that product continues to be marketed) when the retail price of that product and the price of the wholesale input required to supply that product are used as inputs in the Model.

5. JT's prices shall be considered compliant with this direction and shall not give rise to a margin squeeze where the Model indicates a positive margin in respect of each retail fixed-line broadband product which JT currently supplies to its customers (irrespective of whether that product continues to be marketed) when the retail price of that product and the price of the wholesale input required to supply that product are used as inputs in the Model.

[1] As regards average usage, in order to ensure there is not a further contravention JT is strongly advised to ensure its immediate compliance based on the latest average usage figures published in Ofcom's annual Communication Market Report.

ANNEX B :
NOTIFICATION OF A PROPOSED DIRECTION

SECTION 1: INTRODUCTION AND SUMMARY

1. The Jersey Competition Regulatory Authority (**"the Authority"**) hereby notifies Jersey Telecom Limited (**"JT"**) and gives notice that the Authority:

   a. considers JT to be in contravention of licence condition 34 (**"LC34"**) in JT's licence ("**the Licence**") under the Telecommunications (Jersey) Law, 2002 (**"the Telecoms Law"**); and

   b. proposes to give a direction to JT in the terms set out in **the attached Annex 2**.

2. The notification is done pursuant to Articles 11(1) and 19(2) of the Telecoms Law in relation to a direction to be given pursuant to Article 19(1) of the Telecoms Law and LC34.1(c).

3. Pursuant to Articles 11(3) and 19(2) of the Telecoms Law, JT has the opportunity to make representations about the matters hereby notified. Any such representations must be received by the Authority within 28 days of the day following JT's receipt of this notification (i.e. 10 December 2019).

4. Pursuant to Article 19(2) of the Telecoms Law, JT also has an opportunity to comply with LC34 and to remedy the consequences of the contravention identified below within the same period.

5. Pursuant to Article 11(3) of the Telecoms Law, representations may also be made by any other person. All such representations must be received by the Authority within 28 days of the day following publication of this notification on the Authority's website (i.e. 10 December 2019)

6. The Authority will take into account any representations received, and any other steps taken by JT, in deciding whether a remedy by means of a direction is required.

7. The Authority sets out in subsequent sections of this decision its reasons for considering that JT is in contravention of LC34 and for proposing to give a direction in the terms attached. In brief summary:

   a. JT is the exclusive provider of wholesale fixed-line broadband products in Jersey and is one of three retail broadband providers in Jersey (the other two being Sure and Home Net (previously Newtel)).

   b. In November 2018, JT notified the Authority of a number of wholesale and retail broadband and landline price changes. On 20 December 2018, the Authority informed JT that it had cause for concern that the new prices could result in a margin squeeze. Sure (Jersey) also raised concerns about JT's price changes and therefore has a material interest in the outcome of this investigation. JT implemented the wholesale price changes on 28 December 2018; and the retail price changes on 25 January 2019.

   c. This is not the first time the Authority has investigated concerns of this nature. In 2015/16, the Authority investigated whether JT was setting its wholesale and retail prices in such a way as to give rise to a margin squeeze by allowing an insufficient margin for an efficient operator to compete on the retail broadband market.

   d. By decision of 23 June 2016, the Authority concluded that JT's pricing gave rise to a margin squeeze in contravention of LC34. The Authority issued a direction under Article 19 of the Telecoms Law requiring JT to adjust its prices so as to allow a sufficient margin. The sufficiency of the margin was assessed by means of a model (**"the Model"**) prepared with the assistance of the Authority's external economic advisers, SPC Network. The Model was made available to JT.

   e. During the course of 2019, the Authority has again investigated JT's pricing given the latest notifications received in respect of its broadband services. From an early stage of the investigation, it became clear that JT had made a number of amendments to the Model in testing whether its new prices would support a positive retail margin for competitors. The amendments had been made unilaterally, which were not explained by JT either when initially communicating its revised pricing to the Authority or when first responding to the Authority's margin squeeze enquiries.

f. Once it had been able to establish what changes had been made by JT, the Authority took a provisional view that JT's pricing nonetheless gave rise to concerns that a margin squeeze may be taking place, in contravention of LC34. On 3 July 2019, the Authority sent JT a draft direction to that effect providing reasons for that provisional view.

g. In response and through the course of the investigation, JT has sought to defend its pricing on the basis that the Model used in 2016 to assess the sufficiency of the margin between JT's wholesale and retail prices should be adjusted in various respects. JT has requested that the Authority undertake a review of the Model. JT has also made various proposals to in its view address the Authority's concerns, but as matters stand, has not made any changes to its pricing or taken any other steps to remedy the effects of its conduct to date.

h. The Authority has since considered JT's arguments and looked in further detail at the parameters used in the Model to consider whether a margin squeeze has taken place since December 2018. The Authority has again engaged SPC Network to assess the calibration of the Model and to advise on the appropriate parameters for the Model in considering the latest alleged contravention. SPC Network's report (**"the Report"**) is attached as **Annex 3**.

i. Having considered that Report, the Authority remains of the view that JT's current pricing gives rise to a margin squeeze in contravention of LC34. It considers that JT should now be directed:

- to adjust its pricing so as to bring the margin squeeze to an end by ensuring that the Model, applied and updated in accordance with the approach set out in the Report, shows a positive margin in respect of all JT's retail broadband products which are currently supplied to customers, irrespective of whether they are still actively marketed.

8. The terms of the proposed direction are set out at **Annex 2** so that JT and others may make representations to the Authority to inform a decision whether a remedy by means of a direction is required.

9. The remainder of this decision is structured as follows:

   a. **Section 2** sets out some relevant aspects of the legal framework.

   b. **Section 3** describes the procedural context.

   c. **Section 4** assesses JT's pricing; and explains the design and operation of the Model used to establish whether a margin squeeze by JT is in effect. It addresses JT's submissions to date in relation to the Model; and sets out the Authority's responses to them, taking account of SPC Network's recommendations in the Report.

   d. **Section 5** addresses certain other procedural matters that have been raised by JT.

   e. **Section 6** sets out the Authority's conclusions by reference to the applicable legal tests.

SECTION 2: ASPECTS OF THE LEGAL FRAMEWORK

10. The regulation of telecommunications in Jersey is governed by the Telecommunications (Jersey) Law 2002 (**"the Telecoms Law"**). Pursuant to Article 2(1) of the Telecoms Law, a licence is required to run part or all of a telecommunication system. JT's renewed licence was issued by the Authority on 30 June 2017 (**"the Licence"**).

11. Condition 34 of the Licence is entitled "*Fair Competition*". It provides that JT 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 or maintenance of Licensed telecommunications Systems or the provision of Telecommunications 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 Telecommunications Systems or the provision of Telecommunications Services."

12. Article 19 of the Telecoms Law is entitled "*Direction to comply with licence conditions*". Its provisions include the following:

"...

"*(1) Where, in the opinion of the Authority, a licensee is in contravention of a condition contained in a licence, the Authority shall give a direction to the licensee to take steps, or specified steps, to ensure compliance with that condition.*

...

"*(2F) The Authority shall not give a direction or a notification under this Article if it is satisfied that its duties under Article 7 preclude the giving of a direction.*

"*(2G) The Authority shall not give a direction under this Article if it is satisfied that –*

(a) the contravention of the condition is trivial; or

(b) the licensee is taking reasonable steps to comply with the condition and to remedy the effects of the contravention.

"...

"(4) A direction –

(a) shall require the licensee to act or not to act, according to the nature of the condition and the contravention, in a manner specified in the direction;

(b) may require the licensee to take steps, or specified steps, to remedy the effects of the contravention; and

(c) may be modified at any time by the Authority, but only by giving a new direction in accordance with this Article."

SECTION 3: PROCEDURAL CONTEXT

The Authority's 2016 decision

13. On 23 June 2016, the Authority adopted a decision finding that JT was in contravention of LC34 by pricing its wholesale and retail broadband products so as to effect a margin squeeze. The Authority directed JT to remedy the contravention within two calendar months.

14. The investigation followed a complaint by a retail competitor of JT that JT had simultaneously raised the price of its wholesale broadband access products (which are essential inputs for the competitors to do business) and introduced promotional discounts at the retail level. JT's competitor complained that JT's new pricing would force it to price below cost in order to compete. It raised concerns that JT was effecting a margin squeeze during the promotional period that could exclude it from the market.

15. The Authority concluded that the complaint was well-founded. It assessed the sufficiency of JT's margin by reference to a Model devised with the assistance of the Authority's external economic consultants, SPC Network. The Model was based on the costs of a reasonably efficient competitor in the Jersey retail broadband market. It enabled the Authority to determine whether such a competitor would be in a position to cover its costs based on JT's wholesale and retail pricing. If, based on parameters considered relevant to that investigation, the Model showed a positive margin for such a competitor, those prices could be considered consistent with fair and effective competition. If, however, the Model showed a negative margin, JT's prices could be expected to exclude reasonably efficient competitors from the market, and therefore

gave rise to a margin squeeze in contravention of LC34. When applied by reference to JT's 2016 prices and parameters considered relevant to the period of the contravention in question, the Model showed a negative margin.

16. The Authority therefore concluded that JT had potentially contravened LC34 and directed JT "*to amend the combination of JT's wholesale and retail prices*" such that, "*when input into 'the Model*", the combination "*results in a margin that is not negative*".

17. The Authority's reasons for considering that the sufficiency of the margin available at the retail level should be assessed by reference to the costs of a reasonably efficient operator (or "*REO*"), as opposed to JT's own costs, are set out in a provisional decision communicated to JT on 6 November 2015, in §§3.4-3.7. The Authority there explained that entrants in the retail broadband market "*could not be expected to enjoy the same advantages as the incumbent [i.e. JT] and that a REO standard should therefore be used to ensure that sufficient margin is available to new entrants*" (§3.7). JT's advantages included significant economies of scale and scope; and that it did not incur certain entry-specific costs, such as the need for new entrants to offer unlimited data in order to attract consumers in contrast to JT, which was able to apply monthly usage caps and make further charges for data in excess of the cap (known as "*overage charges*").

18. The Model applied the following key parameters:

    a. The reasonably efficient competitor was assumed to have a <u>market share of 10%</u>. This reflected the reality of market conditions in 2016, when JT had a share of around 80% of the retail market, with the remaining 20% shared between two retail competitors;

    b. <u>The average customer lifetime ("ACL") was assumed to be 24 months</u>. The selection of this period took account of indications in other jurisdictions that entrants typically achieve a shorter ACL than the incumbent and so must amortise their customer acquisition costs more quickly: see SPC Report of 16 September 2015, pp.10-11; and

c. Customers' average data usage was taken at 58GB/month. This was based upon the average monthly usage published by Ofcom in the UK at the time, bearing in mind that Jersey residents have access to the same content as residents in the UK, and in particular the data intensive content available on BBC i-Player, ITV-Player and Netflix: see SPC Network Report of 16 September 2025, pp.9-10.

19. By way of sensitivity analysis, SPC Network also considered the margin that would result in various alternative scenarios, including if a 25% market share were attributed to the reasonably efficient competitor; if the ACL were increased by a year to 36 months; and if the average usage per customer were fixed at 22.7GB, which JT had identified as its customers' usage. The margin remained negative when any combination of these three adjustments was applied.

JT's November 2018 notified price changes

20. On 9 November 2018, JT notified the Authority and its retail competitors that it would be increasing the prices of its wholesale broadband products with effect from 28 December 2018.

21. On 12 November 2018, JT notified the Authority of changes to the prices of its retail products to take effect from 25 January 2019. The prices included:

a. a reduction in the landline rental from £12.50 to £11.99; and

b. increases in the prices of JT's retail broadband products.

22. The combined effect of the wholesale and retail price changes notified by JT was likely to reduce the margin available to JT's retail competitors since:

a. The price increases in the retail broadband products were *less* in absolute terms than the increases in the equivalent wholesale broadband products.

b. The reduction in the retail landline rental further reduced the retail margin available to retail competitors: to offer a retail broadband product, such competitors must rent the landline as well as paying the monthly charges for JT's wholesale broadband products. The wholesale line rental price for Jersey has been £11.10 since 1 June 2015 and was not reduced to reflect the retail landline rental reduction.

23. The Authority responded to JT's price notifications by letter of 20 December 2018. It stated that the Authority had "*cause for concern that JT could effect a margin squeeze with the proposed changes*". In this connection, the Authority noted the reduction in available margin that resulted from the changes:

"*In assessing the broadband products JT has increased the price of its wholesale **Standard 250Mb/s download and 50Mb/s upload** by £1.61 however JT has only raised its associated retail products (**250Mb/s download, 50Mb/s upload, 20GB** and **250Mb/s download, 50Mb/s upload, 100GB**) by £1.25. Similar differential price increases are applied to the 250Mb/s symmetrical and 1Gb/s download, 100Mb/s upload.*"

24. The Authority invited JT to explain what had changed in terms of its costs to justify the reduction in retail margin.

The Authority's investigation of the November 2018 notified price changes

25. JT replied to the Authority by letter of 11 January 2019. It recognised that "*we have an obligation to carry out a margin squeeze assessment when changing price, which we have done using the model created by JCRA's appointed consultants SPC Network*". JT said that it had "*updated the model using the new wholesale and retail prices*" and claimed that this "*results in a positive margin*".

26. JT's letter was accompanied by a screenshot showing the output of a version of the Model, apparently applied in respect of a single retail product, *Home Broadband 250Mb: 20GB Daytime Allowance*. While the screenshot did not allow the Authority to interrogate how exactly the Model had been applied, it appeared that JT had made certain assumptions. These included an assumed market share for the competitor of 38.0%; and an average data consumption of 143GB per month. The screenshot showed a positive margin of 0.7% for the product concerned.

27. On 21 January 2019, the Authority wrote to inform JT that it remained of the view that the impact of JT's price changes could be to effect a margin squeeze over the period in question. The Authority noted that, if that proved to be the case, JT would be in breach of LC34 and could be subject to a direction and financial penalty. The Authority therefore requested JT to refrain from introducing the price change pending further investigation; and indicated that it would be requesting further information under separate cover to permit a proper assessment of JT's new pricing.

28. JT replied by letter of 23 January 2019:

   a. JT indicated that "*the wholesale broadband price change has already been implemented*" and that "*the retail price changes have already been communicated to customers... [and] are already in our system to populate at midnight on 24 January 2019*". JT stated that it was "*not in a position to make any changes to these arrangements*".

   b. JT stated that it had "*used the SPC Network margin squeeze model to run the margin squeeze test on the price changes*" and therefore "*d[id] not understand why the JCRA would need to carry out a further assessment*". However, JT stated that it "*would be happy to provide the complete model and output so that the JCRA has complete visibility of <u>the updates made by JT</u>.*"

29. JT subsequently provided its modified version of the Model. The Authority, with the assistance of SPC Network, examined what changes had been made. It transpired that, JT had applied a number of modifications to the Model, unilaterally and without any prior discussion with the Authority. These included, in particular, the following:

   a. JT had assumed a market share for the hypothetical reasonably efficient competitor of 38%. This was the *total combined* share of the two real retail competitors, Sure and Home Net. Taken individually, neither of them in fact operated at this scale; and Home Net's scale was very much smaller.

   b. JT had applied an average monthly usage figure of 143GB per customer.

c. JT had included revenues from "bolt on" tariffs. Such tariffs – which the Authority understands to have been introduced since the Model was developed in 2016 – involve a monthly subscription, payable in addition to the basic package price for a broadband service, to pre-purchase a given allowance of data each month.

30. Running the Model as originally calibrated, the Authority found that a number of JT's retail products gave rise to negative margins. The Authority conveyed these results to JT by letter of 3 May 2019; recorded its preliminary view that JT's pricing was indicative of a margin squeeze, and suggested JT respond at the earliest opportunity to remove the risk of the ongoing effect of a margin squeeze.

31. On 10 May 2019, JT wrote to the Authority, making the following points:

a. First, JT contended that "*there was prior consultation on adjusting the market share figure*". This contention is not accepted by the Authority. It is further addressed in Section 5 below.

b. Secondly, JT argued that bolt on revenue should be treated as part of the monthly price payable by JT's customers, and should be included in the Model's calculations.

c. Thirdly, JT stated that the "*the hypothetical operator / REO approach would be expected to be rolled back*" in view of the current state of competition in the market, to be replaced with an "*equally efficient operator*" (**"EEO"**) approach based on JT's own costs.

32. On 14 June 2019, JT sent a further letter requesting that the Authority "*review the methodology*" of the Model. JT requested that the review should cover the following elements: (1) the market share to be applied; (2) whether to use an REO or EEO approach; (3) whether the monthly average usage should be changed to reflect actual current usage; (4) whether backhaul capacity should change to reflect actual market share changes / usage changes; (5) whether caching should reflect on-island caching and the costs associated with this; (6) whether "bolt on" revenues should be included; and (7) whether the Model should be applied on a per product basis.

33. On 3 July 2019, having considered the period over which the alleged contravention was taking place and the relevant parameters to use in assessing whether a margin squeeze was taking place over that period, the Authority wrote to JT, setting out its provisional decision that JT's pricing amounted to a margin squeeze. It explained the parameters it considered were appropriate, requesting representation from JT on its position.

a. The Authority did not accept JT's contentions that a parameter in the Model used to assess a margin squeeze over the relevant period should be based on the combined market share of JT's retail competitors.

b. The Authority also maintained its view that an REO approach was appropriate in the circumstances of the Jersey market.

c. The Authority, having considered the relevant parameters on which to base its assessment of a potential contravention over the relevant period in question, informed JT that it proposed to issue a draft direction to JT requiring it to adjust its prices so that the Model produced a positive margin based on a 25% competitor market share; an average customer lifetime of 24 months; an average data usage of 190GB/month[2] (it also indicated to JT that future compliance should take the monthly data usage published in the annual Ofcom Communication Market Report); and exclude bolt-on charges.

JT's representations in response to the July 2019 provisional decision

34. By letter of 24 July 2019, JT made the following representations in response to the Authority's provisional decision of 3 July 2019:

a. It maintained that "*JT acted in good faith*" and relied on communications with an officer of the Authority and with SPC Network, and that it kept the Authority "*up-to-date on progress*" and on "*the final updated model*".

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[2] The 190GB/month figure was the average UK usage figure at the time of the November price amendments, as set out in Ofcom's Communications Market Report published in June 2018. As explained below, the latest figure, published in the summer of 2019, shows an increase in average usage to 240GB/month.

b. It stated that it had been "*extremely open and transparent in its communication*" with the Authority in respect of price changes and the use of the margin squeeze model, while acknowledging that it did not "*specifically ask the JCRA to review the model*".

c. It renewed its request for a review of the Model, so that there were "*clear 'rules of engagement' in order to ensure the same mistakes are not repeated*"; but refused to use "*the model that the JCRA now seeks unilaterally to impose*".

d. It alleged that there was an inconsistency of treatment between Jersey and Guernsey, on the basis that no margin squeeze model was applicable in Guernsey.

e. It requested a meeting with the Authority to "*allow some pragmatic discussion on an alternative proposed way forward*".

JT's proposals in August / September 2019

35. On 7 August 2019, JT emailed the Authority. In order to address the Authority's concerns, it proposed the following commitments:

a. to adjust its pricing by raising its retail prices for eight retail products which would fail a margin squeeze test if the Model were applied using a 10% instead of a 25% competitor market share; and

b. to assist the Authority in developing "*an updated margin squeeze model that reflects current market conditions*".

36. On 12 August 2019, JT was informed that views from other licensed operators (**"OLOs"**) affected by JT's pricing in relation to JT's proposed resolution of the matter would be sought. By email of the same date, JT consented to a consultation on its proposed commitments, noting that this was "*without prejudice to the fact that JT does not accept that there has been any margin squeeze*".

37. By email of 16 August 2019, JT reiterated its position that there was not a margin squeeze; and suggested that JT's offer to "*work with CICRA and its consultants to*

update the margin squeeze model" would amount to "*a reasonable step to remedy the effects of the alleged contravention*" for the purposes of Article 19(2G)(b) of the Telecoms Law.

38. By letter to JT of 28 August 2019, the Authority requested further input from JT to demonstrate that the requirements of Article 19(2G)(b) of the Telecoms Law were met by its proposal. As regards the need for the Authority to be satisfied that JT had taken reasonable steps to remedy the effects of the contravention, the Authority noted that "*these effects will have been to your wholesale customers, Sure and Home Net*". In that connection, the Authority asked JT how it intended to remedy the effects of the margin squeeze.

39. A meeting took place between JT and the Authority on 11 September 2019 at which a revised offer was made by JT, which was summarised in a subsequent letter from JT's solicitors, Bedell Cristin, on 12 September 2019 as follows:

    a. "*(1) JT and CICRA proceed on the basis of the 2016 Model*", without clarifying what modifications if any JT was proposing should be made to it; and

    b. "*(2) JT will amend the JT One Lite 250Mb Home Broadband: 25GB Daytime allowance product which has a negative margin under the 2016 Model by making the bolt-on part of the subscription which will allow the revenue from the bolt-on to be included in the model (so price-neutral for the majority of the 1,261 subscribers that take that product.*"

40. Bedell Cristin's letter of 12 September 2019 also asked the Authority to confirm what discussions had taken place with Sure; and whether the Authority had shared "*the pricing information*".

41. The Authority responded to Bedell Cristin's letter on 18 September 2019, requesting that JT set out its new proposals more fully together with an accompanying explanation of how JT considered them to address the Authority's concerns. In response to the questions raised by Bedell Cristin regarding the Authority's communications with Sure, the Authority noted that it had informed JT that it would be consulting Sure, and that it

had consulted Sure, as the original complainant, about the JT's pricing proposal as set out in open and non-confidential correspondence.

42. On the same date, Bedell Cristin provided two further letters to the Authority on behalf of their client, JT:

   a. By the first letter, Bedell Cristin set out various alleged modifications that had been made to the Model over time and described the model as a "*moving feast*".

   b. By the second letter, Bedell Cristin clarified that the "*JT One Lite 250Mb Home Broadband: 25 GB Daytime Allowance*" product had been selected on the basis that it showed the largest margin squeeze, of -10.1%, based on the analysis set out in the Authority's letter of 3 May 2019. JT justified making no adjustment to other products showing a negative margin on the basis (1) that the negative margin for some or all of them disappeared when the Model was adjusted in various ways; and (2) that two of the products were historic and no longer sold.

   c. The second letter also suggested that JT's pricing proposal should not have been shared with OLOs and referred the Authority to Article 61(1) of the Telecoms Law and Article 44 of the Competition (Jersey) Law 2005, which specify criminal offences for the improper disclosure of certain types of information. This insinuation of impropriety on the part of the Authority in consulting affected industry parties is rejected. The matter is addressed further in Section 5 below.

SECTION 4: ASSESSMENT

The current state of competition on the wholesale and retail fixed line broadband markets

43. JT is the exclusive provider of wholesale fixed line broadband products in Jersey. As such, it holds a position of significant market power in the market for such products, which are an essential input for the provision of fixed line broadband products at the retail level. The finding that JT holds a position of significant market power in the market for such products has been in place for some time and most recently set out in

the Authority's decision at the conclusion of the broadband market review, issued on 9 January 2019[3].

44. In the retail fixed line broadband market, JT remains by far the largest supplier. As at the end of 2018, it had a market share of 59.5%. Its two retail competitors, Sure and Home Net (previously, Newtel) had market shares of around 32.2% and 8.3% respectively.[4]

Analysis of JT's price changes notified in November 2018

45. For the reasons set out in the accompanying report of SPC Network (see **Annex 3**), the Authority provisionally considers that the November 2018 price changes give rise to a margin squeeze in breach of LC34.

46. In reaching that conclusion, the Authority has considered the relevant parameters on which a margin squeeze assessment should be based over the period in question. In particular, it considered : (1) whether it remains appropriate to assess the sufficiency of JT's margin by reference to the costs of a hypothetical reasonably efficient operator; (2) if so, what parameters should be applied in modelling those costs; and (3) whether, on an appropriate calibration of the Model, JT's pricing results in negative margins. Those questions are addressed in turn below.

<u>(1) Use of the reasonably efficient operator standard</u>

47. As JT still enjoys a market share of around 60%, if the equally efficient operator (EEO) approach was applied this would mean that the EEO would also require a market share of 60% to benefit from the same economies of scale.

48. Given that one of the Authority's objectives is to promote competition then the REO approach should be used as this allows firms that do not enjoy the same economics of scale as JT to compete in the market. This approach has been recognised by both the European Commission and BEREC and has been applied by many NRAs in Europe.

[3] Final Decision, Broadband Market, Market Review and SMP Finding, CICRA 19/01, 9 January 2019
[4] Telecommunications Statistics and Market Report 2018, Information Notice, CICRA 19/35, 13 September 2019

The rationale for such an approach is set out fully in the Authority's 2016 decision and remains relevant to this assessment.

(2) Parameters to be used in the Model

49. The Authority considers that given the period over which the contravention is being assessed the following parameters are relevant to a margin squeeze assessment and should therefore be used in the Model:

a. Average customer life: 24 months. JT appears to accept that this parameter remains appropriate. In any event, the Authority considers that it is a reasonable and appropriate estimate. As SPC Network notes, there is no reason to expect the average customer life should have changed since the Model was originally produced.

b. Overage and Bolt-On Charges: It is not understood to be in dispute by JT that overage revenues should not be included in the Model. In any event, the Authority considers that they should be omitted for the same reasons given in its 2016 decision: in summary, an entrant, in contrast to an incumbent, will typically need to offer an unlimited package in order to appeal to consumers. Having considered the nature of bolt on revenues and JT's arguments, the Authority has however reconsidered its position and is of the view that bolt on revenues may be included, for the reasons given in SPC Network's Report.

c. Average data usage per customer per month: The Authority remains of the view that the average UK usage levels available are the most appropriate average data usage estimates to apply. They are readily accessible data; and provide a reasonable proxy in view of the similar availability of content for UK and Jersey-based consumers. Using internal JT data would not serve as an appropriate benchmark for several reasons. For example, the data usage of JT's customers may differ from particular competitors, who have typically offered uncapped data packages to their customers. The UK data was agreed upon and used in the 2016 decision, and the Authority considers that it continues to provide a suitable proxy in this context. At the time JT announced the price changes which have given rise to the concern the most recent published figures by Ofcom showed average data usage at 190 GB/month (Ofcom has since then published more recent figures and this is discussed further below). For this reason the appropriate figure to apply over the relevant period of the contravention is therefore 190GB/month (this being the available Ofcom average usage data published up to summer 2019).

d. Market share of the REO: The Authority considers that given the development of competition in the market the assessment of whether a margin squeeze has taken place over the relevant period should be based on the market share of the REO at 25%. This reflects the share used for an REO by other NRAs, notably ComReg (Ireland) and Ofcom (UK) in similar decisions and would reflect a competitive market of around three to four operators.

(3) Application of the Model

50. When applied using the parameters set out above, the Report shows that the Model produced a negative margin in respect of a number of JT's retail broadband products.

51. The inputs used are an average customer life of 24 months; bolt-on revenue is included; and average data usage is set at 190GB/s, being the applicable Ofcom data point at the time of the price changes. The results are set out below:

	Margin
Home Broadband 250Mb: 20GB Daytime Allowance	**3.3%**
Home Broadband 250Mb: 100GB Daytime Allowance	**16.9%**
Home Broadband 250Mb symmetrical	**0.2%**
Home Broadband 1Gb: 300GB Daytime Allowance	**-0.1%**
JT Staff Broadband 1Gb Unlimited	**N/A**
JT Complete 250Mb Home Broadband: 60GB Daytime Allowance	**-1.0%**
JT Complete 250Mb Home Broadband: 160GB Daytime Allowance	**15.0%**
JT Complete 1Gb Home Broadband: 300GB Daytime Allowance	**-3.2%**
JT One 250Mb Broadband: Unlimited Daytime Allowance	**11.6%**
JT One 250Mb symmetrical: Unlimited Daytime Allowance	**15.2%**
JT One 1Gb Broadband: Unlimited Daytime Allowance	**7.9%**

JT One Lite 250Mb Broadband: 25 GB Daytime Allowance	**-2.6%**
JT One Lite 250Mb symmetrical: 25 GB Daytime Allowance	**-3.0%**
JT One Lite 1Gb Broadband: 300 GB Daytime Allowance	**-5.6%**
Retail Professional 250 Mbps and 50 Mbps upload 200Gb	**20.9%**
Retail Professional 250 Mbps and 50 Mbps Unlimited	**52.6%**
Retail Professional 1Gb	**7.5%**

52. By way of sensitivity analysis, SPC Network has run the Model using a variety of alternative average data usage figures, as follows: (1) 58GB/month, which was the original average usage figure from 2016; (2) 143GB/month, which is the level applied by JT in modelling the November 2018 price adjustments, apparently based on JT internal usage data; and (3) 190GB/month, which is the Ofcom data point, which the Authority considers should be used to assess the this alleged contravention. As set out below, each of these inputs produce negative margins for some of JT's retail products:

	58GB/ month	**143GB/ month**	**190GB/ month**	**240GB/ month**
Home Broadband 250Mb: 20GB Daytime Allowance	9.3%	5.2%	3.3%	0.4%
Home Broadband 250Mb: 100GB Daytime Allowance	22.1%	18.6%	16.9%	14.4%
Home Broadband 250Mb symmetrical	4.0%	1.4%	0.2%	-1.6%
Home Broadband 1Gb: 300GB Daytime Allowance	2.7%	0.8%	-0.1%	-1.5%
JT Staff Broadband 1Gb Unlimited	N/A	N/A	N/A	NA
JT Complete 250Mb Home Broadband: 60GB Daytime Allowance	5.3%	1.1%	-1.0%	-4.0%
JT Complete 250Mb Home Broadband: 160GB Daytime Allowance	20.3%	16.7%	15.0%	12.4%
JT Complete 1Gb Home Broadband: 300GB Daytime Allowance	-0.3%	-2.2%	-3.2%	-4.6%
JT One 250Mb Broadband: Unlimited Daytime Allowance	17.1%	13.4%	11.6%	9.0%
JT One 250Mb symmetrical: Unlimited Daytime Allowance	18.4%	16.3%	15.2%	13.7%
JT One 1Gb Broadband: Unlimited Daytime Allowance	10.4%	8.7%	7.9%	6.6%
JT One Lite 250Mb Broadband: 25 GB Daytime Allowance	3.8%	-0.6%	-2.6%	-5.8%

JT One Lite 250Mb symmetrical: 25 GB Daytime Allowance	0.9%	-1.8%	-3.0%	-4.9%
JT One Lite 1Gb Broadband: 300 GB Daytime Allowance	-2.7%	-4.6%	-5.6%	-7.0%
Retail Professional 250 Mbps and 50 Mbps upload 200Gb	24.4%	22.0%	20.9%	19.2%
Retail Professional 250 Mbps and 50 Mbps Unlimited	54.7%	53.3%	52.6%	51.6%
Retail Professional 1Gb	8.3%	7.8%	7.5%	7.2%

SECTION 5: PROCEDURAL ISSUES RAISED BY JT

53. As set out above, JT's representations during the course of the Authority's investigation have raised two procedural matters.

a. First, by letter of 10 May 2019, JT alleged that some of the changes to the Model on the basis of which it had assessed whether the November 2018 price changes gave rise to a margin squeeze had been the subject of prior consultation with the Authority.

b. Secondly, by letters of 12 and 18 September 2019, JT's lawyers have raised questions in relation to the Authority's consultation of OLOs in connection with JT's proposal of 7 August 2019 to amend its retail pricing.

54. These matters are addressed in turn below.

(1) Whether JT's changes which it made to the Model were the subject of prior consultation

55. In its letter of 10 May 2019, JT maintained that "*there was prior consultation on adjusting the market share figure*" in the Model, and that it was therefore justified in applying a 38% market share assumption when determining whether its November 2018 price changes gave rise to a margin squeeze.

56. In support of that contention, JT relies on two particular interactions.

57. First, in August 2016, JT contacted an officer of the Authority to request a meeting with SPC Network "*so that JT could completely understand the parameters of the Model*". The officer in question confirmed that he was happy for JT to speak with SPC Network and provided the relevant contact details. SPC Network was subsequently engaged by JT to assist in advising on how the Model worked.

58. As the correspondence accompanying JT's letter of 10 May 2019 shows, however, this interaction does not provide any support for JT's claim of prior consultation in relation to an adjustment to market share.

a. The underlying correspondence, attached shows that JT's initial approach to the Authority, by email of 31 August 2016, was to request a call with SPC to "*ask questions on where the different inputs [in the Model] are and how we can make changes for price changes/new products*". The purpose was therefore stated to be to understand how to operate the Model in terms of inserting new wholesale / retail prices and new products. There was no suggestion that the purpose was to discuss or agree upon any substantive changes to the underlying parameters of the Model. The Authority approved the interaction with SPC Network on that basis.

b. The purpose of JT's contacts with SPC Network was confirmed in JT's subsequent email to SPC Network. JT explained that "*we are looking to make some changes to our wholesale broadband products and pricing*" and "*would like the changes checked by SPC to make sure that we have change [sic] the model appropriately*": again, there was no suggestion that discussions would extend to the validity or otherwise of underlying parameters of the Model.

c. The limited purpose of the interaction between JT and SPC Network was confirmed by SPC Network's letter to JT dated 12 October 2016, which explicitly stated SPC Network's understanding that "*the support you need would be limited to checking that the margin squeeze model has been used and adapted appropriately and that SPC Network will not be asked to comment on or advise on the inputs to or outputs from the model*" (emphasis added).

59. The second basis relied upon by JT for alleging prior consultation on amending the market share figure is the fact that in October 2016, JT provided a notification to the Authority of a broadband speed uplift, and enclosed a copy of the margin squeeze model, in which the market share percentage had been modified. JT does not allege, however, that it made any attempt to draw the Authority's attention to this modification or otherwise to seek its approval for it; or that the Authority gave any endorsement to such a change.

60. As regards the November 2018 price changes which are the subject-matter of the Authority's provisional decision and attached draft direction, JT made no attempt to explain the basis on which it considered the amended prices to comply with the Model; and did not give the Authority any notice of the changes which JT had made to the Model in order to produce a positive margin.

61. In the circumstances, the Authority does not accept that JT consulted with it in any meaningful way as regards any of the changes that JT had made to the Model.

(2) Whether the Authority acted properly in consulting OLOs in relation to JT's proposal of 7 August 2019

62. The other procedural matter raised by JT in representations received from its lawyers, Bedell Cristin, concerns the Authority's consultation of OLOs regarding the first of the two proposals advanced by JT to address the Authority's concerns.

63. By letter of 12 September 2019, Bedell Cristin alleged on behalf of its client, JT, that JT's proposal to adjust its pricing "*was sensitive*". It asked the Authority to confirm whether the Authority shared the pricing proposal with JT. By subsequent letter of 18 September 2019, Bedell Cristin referred to Article 61(1) of the Telecoms Law and Article 44 of the Competition (Jersey) Law 2005, and requested the basis on which "*<u>any</u> information concerning an alleged margin squeeze which has been received from JT and relates to JT*" was disclosed to an OLO.

64. This procedural matter does not affect the Authority's provisional decisions as to the existence of a margin squeeze and as to the need for a direction in the terms set out at

Annex 1. Given the emphasis placed on the matter by JT's lawyers, it is however appropriate briefly to address it.

a. Following receipt of JT's first proposal, the Authority determined that it was appropriate to consult JT's competitors on the retail broadband market to determine their views as to whether they considered that the proposal would permit them to compete effectively in the Jersey broadband market.

b. JT's proposal was sent in open correspondence and was not flagged as confidential. It consisted of a list of JT's current retail prices for its broadband products, which are a matter of public record; and the amendments to its retail prices that JT was prepared to offer specifically for the purpose of resolving the current regulatory proceedings. It is not accepted that any of this information could properly be characterised as commercially sensitive.

c. The Authority informed JT of its intention to consult as to whether the proposal should be accepted, and no objection was made. The market testing of commitments is standard practice in competition and regulatory investigations of this nature: see e.g. the UK CMA's guidance on its investigation procedures in Competition Act 1998 cases, at para 10.23.

d. JT's lawyers have referred to Art.61(1) of the Telecoms Law and Art.44 of the Competition (Jersey) Law 2005. The present investigation has been conducted by the Authority exclusively under the Telecoms Law. Art.61(1) is, however, not engaged by JT's first proposal: the proposal was voluntarily provided and was not "*obtained*" by the Authority under formal powers. Nor does it relate to the private affairs of a business, but consists instead of public pricing information and a proposal put forward in the context of a regulatory investigation. In any event, Art.61(3) specifies a number of gateways for disclosure including for the purpose of facilitating the performance by the Authority of its functions under the 2002 Law. The consultation of the OLOs falls within that gateway.

SECTION 6 : THE AUTHORITY'S CONCLUSIONS

65. For the reasons set out above, the Authority's provisional conclusion is that JT's pricing which was notified in November 2018 gave rise to a margin squeeze over the period in question. It considers that JT's competitors have been placed in a position where JT's new pricing forces them to price below cost in order to compete and risks excluding them from the market.

66. The Authority also considers that it is appropriate to issue a direction pursuant to Article 19(1) of the Telecoms Law, requiring JT to amend its pricing to address the margin squeeze identified so that the Model shows a positive margin.

a. Article 19(1) imposes an obligation on the Authority to give a direction to a licensee to take steps, or specified steps, to ensure compliance with a licence condition wherever, in the opinion of the Authority, the licensee is in contravention. For the reasons set out above, the Authority considers that JT is in contravention of LC34.

b. The duty under Article 19(1) is subject to two express limitations. First, by virtue of Article 19(2F) of the Telecoms Law, the Authority shall not give a direction or a notification if satisfied that its duties under Article 7 preclude it from doing so. The Authority has considered its duties and is of the view that they favour the giving of a direction and a notification in this case.

c. Secondly, by virtue of Article 19(2G), the Authority shall not give a direction if satisfied that the contravention of the condition is trivial or that the licensee is taking reasonable steps to comply with the condition and to remedy the effects of the contravention.

d. The Authority considers that neither of the alternative limbs of Article 19(2G) is met. In the Authority's view, the contravention cannot be regarded as trivial. The products to which it applies are currently being purchased by 3,113 subscribers in total[5].

e. Nor is the Authority satisfied that JT is taking reasonable steps to comply with the condition and to remedy the effects of the contravention. JT has not adjusted its

[5] JT's data, email from Carol Gunasekara, 14 August 2019

retail prices; under its most recent offer, is proposing to adjust only one product's price; and has made no proposals to remedy the effects of the contravention. JT's proposal to work with the Authority to devise a new margin squeeze model is purely prospective and does not address any effects to date. JT's position is in any event that there are no such effects to address as there is no contravention.

67. The Authority considers that it is appropriate to issue a direction under LC34.1(c). For the reasons set out above and in the Report, the Authority considers that the Model set at the parameters described above is an appropriate basis for assessing whether JT's prices gave rise to a margin squeeze over the period in question[6].

68. The terms of the proposed direction are set out in **Annex 2**.

[6] In order to remedy the effect of the margin squeeze going forward, it is relevant that the source (OFCOM Communication Market Report) of one of the Model's parameters (average data usage per customer per month), indicated that the most recent estimate of usage increased from 190 GB/month to 240 GB/month. If this latter figure were used to assess the contravention, it would have the effect of increasing the extent of the margin squeeze. However, as explained above, JT would not have had access to this updated figure at the time of its pricing changes in late December 2018/early January 2019. The contravention over the period in question is therefore assessed on the basis of the 190 GB/month average. However, in order to ensure there is not a further contravention JT is strongly advised to ensure its immediate compliance based on this revised average of 240 GB/month and subsequent published figures in Ofcom's annual Communication Market Report.

ANNEX C : SPC NETWORK'S REPORT

SPC Network Contribution to Draft Decision on Margin Squeeze
20 Oct 2019

The model applied for assessing margin squeeze

Overview of the model

In 2015, SPC Network developed a margin squeeze test (MST) model for CICRA to determine whether the margin between Jersey Telecom's (JT's) retail prices and the wholesale rate resulted in a margin squeeze being affected on other operators. A detailed description of the model along with the results were presented to CICRA in SPC Network's report *'Report on Jersey Telecom Pricing of Broadband Access'* dated 16 September 2015.

The model was developed on the basis of a Reasonably Efficient Operator (REO) standard. The rationale for adopting this approach was set out by the SPC Network report:

> *"... in a market subject to ex ante regulation where competition is being introduced, there is an argument that the entrant could not be as efficient as the incumbent, in part at least because it does not have the economies of scale and scope enjoyed by the incumbent operator. To overcome this disadvantage and allow competition to develop an alternative REO standard may be used."*

In support of this statement, SPC Network quoted from the European Commission Recommendation on regulated access to next generation networks:

> *"In the specific context of ex ante price controls aiming to maintain effective competition between operators not benefiting from the same economies of scale and scope and having different unit network costs, a "reasonably efficient operator test" will normally be more appropriate."*[7]

Continued Appropriateness of the REO Approach (Point 2 of JT Letter dated 14 June 2019)

In the period since the SPC Network initial report on margin squeeze, there has been a change in retail market shares by volume. Sure's market share has increased from 22% to 32% with a commensurate decrease for JT from 72% to 60%[8],[9]. Now that Sure has a market share of over 30%,

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[7] European Commission (2010) *'Commission Recommendation of 20th September 2010 on regulated access to Next Generation Access Networks'* SEC (2010) 1037
[8] CICRA (2019) 'Telecommunications Statistics and Market Report 2018' p.18
[9] The balance is primarily Homenet and others.

we need to consider whether the REO approach is still valid.

First, it should be noted that the REO (and the Adjusted Equally Efficient Operator AEEO[10]) standard is widely used in the European Union. In a survey of NRAs, BEREC found that 12 of the 21 NRAs that regulate prices on the basis of an *ex ante* margin squeeze test used the REO or AEEO standard[11]. The use of REO is, therefore, quite normal across the EU in a regulated environment.

The fundamental reason for adopting the REO is set out in the quote from the European Commission above: maintaining competition between operators not benefiting from the same economies of scale. This point is also made by BEREC, which explains that the REO is appropriate when:

> *"...competitors could be faced with higher costs compared to the reference charges of the SMP operator, e.g. in terms of (temporary) lower economies of scale and scope."*[12]

When looking at the costs of the REO in the margin squeeze test, we take into account those costs required to convert a wholesale input to a retail product, referred to as the retail margin. The cost of the input, in this case a bitstream access product, is exogenous to the model and assumed to be the same for all operators including the SMP operator. We need therefore to consider the extent to which economies of scale apply to the retail margin.

In Jersey, the most important area where companies can benefit from economies of scale and scope is on-island and off-island backhaul. This is a significant cost to the business in absolute terms but also the element that is most susceptible to economies of scale.

Backhaul circuits are used to transfer aggregated data between the operator's main location in Jersey and the Internet, usually via undersea cables to the UK. As the number of users and the average data usage per customer increases so the bandwidth of the backhaul circuits needs to increase, usually in stepped increments rather than linearly. This means that the ISP is likely to be buying backhaul capacity ahead of demand.

The pricing of backhaul is such that the marginal cost per Gigabit per second (Gbps) of each increment of capacity decreases (although remains positive), thus the more capacity is purchased the lower the average price per Gbps. A larger ISP therefore benefits from significant economies of scale. An ISP with a market share of, say, 10% will have higher average on-island and off-island backhaul costs per customer than a firm with 25% market share.

Jersey Telecom still enjoys a market share of 60%. If the EEO approach were applied, this would mean that equally efficient competitor would also need a market share of 60% to benefit from the

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[10] This is a version of a REO on which the modeled operator is assumed to have all the same costs as the dominant firm but to have lower economies of scale as it produces at a lower volume.
[11] BEREC (2014) 'Guidance on the regulatory accounting approach to the economic replicability test (i.e. ex-ante/sector specific margin squeeze tests)' pp.60-61.
[12] Ibid. p.19

same economies of scale. It is self evident that there cannot be two operators in a market each with 60% market share.

Given CICRA's legal objective to promote competition[13] then it must be the case that a REO standard is used that allows firms that do not enjoy the same economies of scale as JT to compete in the market, as proposed by both the European Commission and BEREC and adopted by many NRAs in Europe.

Detailed Design Issues

Market Share (Point 1 of JT Letter)

If the REO methodology is to be used based on the market share of an efficient entrant, then the level of market share must be considered. It should be noted that the market share used does not reflect any specific operator, but rather the minimum share that a hypothetical operator would need to be reasonably efficient. This could be more or less than a competitor in the market.

The margin squeeze test used by CICRA sets the market share for the hypothetical REO at 25%.

The 2015 report by SPC Network highlighted precedents set by both Ofcom and Comreg in 2013, which set the market share for the REO at 20% – 25%[14]. This level should allow at least three, and up to five, operators to compete within the market and was deemed by both Ofcom and Comreg as a sensible minimum efficient scale for a new entrant. Although Ofcom has subsequently changed the basis of regulated charging in the WLA market away from an *ex ante* margin squeeze approach, Comreg has maintained the same approach and the same market share.

BEREC identified 12 NRAs using the REO or Adjusted EEO approach and asked them what market share they set for the generic operator used in their economic replicability test. Five NRAs answered the question: one used a share of 5%, one of 15% and two of 25%. The fifth NRA used the term "viable competitor" without identifying a market share[15].

Setting the market share of the hypothetical REO at 25% is therefore at the high end of shares used by European NRAs and requires the hypothetical REO to be well established in the market.

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[13] Telecommunications (Jersey) Law 2002, Article 7(2)(a)

[14] Ofcom (2013) 'Fixed access market reviews: wholesale local access, wholesale fixed analogue exchange lines, ISDN2 and ISDN30: Consultation on proposed markets, market power determination and remedies' 3 July 2013. (Paragraphs 11.427 – 11.429) and ComReg (2013) 'Next Generation Access: Remedies for Next Generation Access Markets' 31/01/2013.

[15] Op cit. footnote 12. Note: the NRAs are not identified by the name in the BEREC report, and so it is possible that the two NRAs using 25% are Ofcom and Comreg.

Overage/Bolt-ons

- Overage means a variable charge payable by consumers for using an amount of data in excess of their monthly allowance. This charge is levied in arrears and set as a price per Gigabyte or part thereof.
- Bolt-ons are packages of additional data allowance a user may sign up to during their contract to give an increased amount of data per month.

The model developed in 2015 did not allow overage to be included in the retail price. At the time bolt-ons were not available.

The amount of overage a customer will pay is not known to the customer at the start of the contract. It is probable that the customer's decision will be made in the expectation that he or she will not actually incur overage charges[16] and will therefore make their price decision on the base price alone. It is also likely that the customer will compare the base price against the price offered by other operators. Competitors are therefore in a position that they have to compete with the core price and not the actual price paid by the customer including overage.

It is therefore appropriate that the overage charges remain excluded from the margin squeeze test.

As noted above, bolt-on data allowances were not available at the time the margin squeeze test was designed. However, we have taken into consideration JT's view that since 2016 Bolt-on charges have become a feature of the market and are known to the customer at the start of the contract. It is therefore possible for the customer to compare the price of the JT package including bolt-on charges with the price offered by its rivals. For this reason it is considered appropriate that average bolt-on charges per customer for each package should now be allowed in the price element of the margin squeeze test. To be clear, this means the total revenue from bolt-on sales for each product variant divided by the number of customers for each product variant.

However, for the reasons outlined above, overage charges should still not be permitted in the revenue.

Average Data Usage per Customer (Point 3 of JT's letter)

When the model was developed, no data were available on the average usage per customer across the whole market in Jersey. The only data that were available was for JT's customers who may not be representative of the average user.

As a proxy, therefore, the average data usage per month found in the UK by Ofcom was used. It was CICRA's view that this was a relevant benchmark as (i) Jersey consumers were likely to have the same tastes and UK consumers and (ii) Jersey consumers were able to access the same content, in

[16] Referred to as an "optimism bias".

particular catch up TV services from the BBC and ITV.

The UK average at the time was 58GB per month and so this level was used in the test. In the period since SPC Network's first report, the average usage in the UK has increased almost fourfold and is now 240GB/month.

Application of the margin squeeze test to products no longer marketed

The question arises as to whether a margin squeeze test should apply to products with an existing customer base but which are no longer marketed to new customers. There remains a significant risk to competition if the margin squeeze test does not apply to such products.

The dominant firm could launch a product that is priced in such a way that it causes a margin squeeze and then withdraw that product from market once it has a customer base but before it is forced to take any corrective action. Competitors wanting to attract customers of that product to one of their own products would still face a margin squeeze to set a competitive price. The same anticompetitive conditions exist, therefore, whether a product has been withdrawn from sale or not.

For this reason, therefore, a margin squeeze test should apply to all products for which there is a customer base, whether or not it is actively marketed.

Updating the Model for the Future

There are some elements of the model that are based on empirical evidence that may vary over time. For the model to remain relevant, it should be able to reflect such changes. We have discussed these below.

However, the market share of the REO is not one of these variables. The market share of a REO should reflect the minimum share an ISP needs to be a viable competitor in the market and not the share of any specific competitor.

Backhaul Costs

The increase in data usage per month has a knock-on effect on the cost of on and off island backhaul. If the number of customers stayed constant, each ISP would still need to have trebled its backhaul capacity to cope with the increased demand. This may lead to a decrease in the average cost of backhaul per Gbps as discussed above, but would also lead to an increase in the average cost of backhaul per customer.

The model therefore needs to take account of the increased amount of backhaul capacity needed by the REO.

SPC Network

Average Customer Lifetime (Point 4 of JT Letter)

The Average Customer Lifetime (ACL) used in the model is that expected for a customer of an entrant rather then the dominant operator. There is no reason to expect the ACL for entrants' customers to have changed since the original model was produced. At the present time, there is therefore no basis for revising this aspect of the model.

Margin Squeeze on a per product basis (Point 6 of JT Letter)

Allowing JT to set the margin across the portfolio could allow them to set prices and margins strategically to foreclose some of the portfolio to competition. It could set prices at a positive margin where it faces little competition and use that excess profit to set effect a margin squeeze where it faces more competition. Requiring each product in the portfolio to have a positive margin ensure a level competitive playing field and so does not foreclose any segment of the market to competition.

Commentary on Margin Squeeze Test Results

SPC Network has applied the margin squeeze test using the wholesale and retail prices the prices set out in the LC33 Notices from Jersey Telecom dated 9th and 11th November 2018 respectively, using the following parameters:

- Market share: 25%
- Average usage per customer: 190GB per customer
- The ACL has been maintained at 24 months
- The model is applied on a product by product basis.
- The model has been run including revenue from bolt-on fees.

The results are shown in the table below. The results show that the model produces a negative margin when applied to JT's prices in respect of six of the 16 retail products.

CICRA

CHANNEL ISLANDS COMPETITION & REGULATORY AUTHORITIES

Market share = 25%	With bolt-on
Home Broadband 250Mb: 20GB Daytime Allowance	3.3%
Home Broadband 250Mb: 100GB Daytime Allowance	16.9%
Home Broadband 250Mb symmetrical	0.2%
Home Broadband 1Gb: 300GB Daytime Allowance	-0.1%%
JT Staff Broadband 1Gb Unlimited	N/A
JT Complete 250Mb Home Broadband: 60GB Daytime Allowance	-1.0%
JT Complete 250Mb Home Broadband: 160GB Daytime Allowance	15.0%
JT Complete 1Gb Home Broadband: 300GB Daytime Allowance	-3.2%
JT One 250Mb Broadband: Unlimited Daytime Allowance	11.6%
JT One 250Mb symmetrical: Unlimited Daytime Allowance	15.2%
JT One 1Gb Broadband: Unlimited Daytime Allowance	7.9%
JT One Lite 250Mb Broadband: 25 GB Daytime Allowance	-2.6%
JT One Lite 250Mb symmetrical: 25 GB Daytime Allowance	-3.0%
JT One Lite 1Gb Broadband: 300 GB Daytime Allowance	-5.6%
Retail Professional 250 Mbps and 50 Mbps upload 200Gb	20.9%
Retail Professional 250 Mbps and 50 Mbps Unlimited	52.6%
Retail Professional 1Gb	7.5%

GUERNSEY COMPETITION AND REGULATORY AUTHORITY
Suite 4, 1st Floor, La Plaiderie Chambers, St Peter Port,
Guernsey, GY1 1WG
T +44 (0) 1481 711120 E info@cicra.gg

JERSEY COMPETITION REGULATORY AUTHORITY
2nd Floor, Salisbury House, 1-9 Union Street, St Helier
Jersey, JE2 3RF
T +44 (0) 1534 514 990 E info@cicra.je