Three's Response to Ofcom's policy position on Simplifying Non-geographic Numbers and 080 and 116 number ranges and the Consultation on proposed dispute resolution guidance, both published 15 April 2013.

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Executive Summary

Hutchison 3G UK Limited (“Three”) welcomes the opportunity to respond to Ofcom’s consultation on simplifying non-geographic numbers including the policy position on the introduction of the unbundled tariff and changes to 080 and 116 number ranges (the “NGCS Consultation”) and the: consultation on proposed dispute resolution guidance (the “Dispute Resolution Guidance”), both published 15 April 2013.

Three continues to support Ofcom’s overall policy goal of improving transparency and consumer confidence in the non-geographic number range. Subject to our concerns, detailed in this response, we broadly agree that it is right to introduce the unbundled tariff mechanism and to make 080 and 116 numbers free to caller.

We strongly disagree with Ofcom about certain elements of its proposals in relation to 080 numbers, specifically:

- Ofcom should set a single, industry wide gradient of fair and reasonable mobile origination charges;
- Ofcom’s proposals will benefit a small number of vertically integrated operators, ✂;
- Three has serious doubts as to Ofcom’s ability to regulate retail prices in the absence of a finding of significant market power (“SMP”).

Ofcom should set a single, industry-wide gradient of fair and reasonable (“F&R”) mobile origination charges in the 080 number range.

We have two main concerns regarding the proposed terminating call provider (“TCP”) access condition and Ofcom’s derivation of its F&R mobile origination charges:

- **the range of F&R 080 mobile origination charges proposed by Ofcom (1.5-2.5ppm) is too low** – a decision to make the 080 number range free-to-caller means that mobile operators will only receive payment from TCPs when their subscribers call 080 numbers. In consequence, it is crucial that Ofcom sets mobile origination charges at an appropriate level;
- **Ofcom’s reliance on commercial negotiations will inevitably lead to disputes** – in our view, all parties will benefit if Ofcom determines a single, industry-wide gradient of F&R mobile origination charges.

Our analysis shows that Ofcom has set the maximum average service provider (“SP”) payment at too low a level (1.5ppm, a 1ppm increase on the current 0.5ppm charge) because it has underestimated the extra benefits from the tariff package effect (“TPE”) when weighing them against the negative consumer impact of reduced service availability.

Furthermore, Ofcom’s reliance on commercial negotiations informed by a wide range of F&R mobile origination charges (“OCs”) set out in its dispute resolution guidelines will inevitably lead to disputes and uncertainty in the industry.

For that reason, Three proposes a single, industry-wide gradient of F&R mobile OCs of 3.3ppm in 2015 and 2.5ppm in subsequent years (based on a long run share of mobile calls of 45-50%, consistent with DWP's experience and with the proportion of UK residential calls originated from mobile to 080 number ranges).

Ofcom's proposed 080 access condition may adversely affect the wholesale market.

Three believes that the 080 access condition may have an adverse effect on the wholesale market. In particular:

- Ofcom is overly optimistic in assuming that operators will agree on F&R charges;

- The structure of BT's Standard Interconnect Agreement will inevitably result in mobile origination charges set towards the lower end of Ofcom's reasonable F&R range;

- ✂.

The outcome is likely to be the realisation of any combination of the consumer risks already identified by Ofcom, for example;

- delays and uncertainty arising from dispute resolution, which may impact on SP's and mobile OCP's willingness to innovate or invest;
- increased prices for other services; or
- the reduced ability of smaller operators to compete on other propositions because of eroded revenues from origination charges.

Three continues to have concerns about Ofcom's ability to regulate retail pricing in the absence of a finding of SMP.

We reiterate our reservations about Ofcom's approach to regulating retail pricing.

Three accepts that Ofcom has consumer protection powers and that Ofcom may regulate via the National Telephone Numbering Plan ("NTNP"). However, given the draconian nature of regulating retail pricing in an otherwise competitive market, Ofcom must be more explicit about the borderlines and the limits Ofcom sets on itself to impose retail regulation absent an SMP finding. In particular, in relation to the precise boundaries between the exercise of a consumer protection-based power under s58(1)(aa) of the Communications Act 2003 and Ofcom's SMP-based powers.

We believe that Ofcom's policy goal is at risk from appeals on points of legal principle.

In respect of Ofcom's proposals for the introduction of the Unbundled Tariff we observe that:

- Ofcom must ensure consistency between the general condition ("GC") modifications under the NGCS Consultation and the proposals for Price Rises in Fixed Term Contracts[1].
- Some of the proposed changes to the legal instruments may confuse customers and be impractical to implement.

Ofcom must ensure that the GC modifications in respect of non-geographic numbers are considered in the context of the proposals for Price Rises in Fixed Term Contracts.

The example of multiple changes in service charges ("SCs") under the NGCS Consultation proposals must be more broadly considered by Ofcom when finalising its position on Price Rises in Fixed Term Contracts.

Specifically there is nothing preventing SPs from increasing charges (within the specified cap) numerous times during the course of a customer contract. Where this happens CPs will be forced to absorb (what maybe a very detrimental) cost if Ofcom takes a purist approach and drafts regulatory changes (in respect of price rises) in a way which captures any kind of price increase scenario i.e. including changes to the SPs service charge. We assume this cannot be Ofcom's intention when formulating the new NGCS regime.

Some of Ofcom's proposed changes to the legal instruments may confuse customers and be impractical to implement.

- Ofcom's proposals do not impose an obligation on SPs to ensure customers are proactively notified about SC changes. We believe this will lead to complaints to CPs and a poor customer experience. Ofcom should remedy this or at least ensure structures and sufficient timescales exist to enable CPs to manage this risk.

- We remain of the opinion that the requirement to support 100 price points on originating call provider ("OCP") billing systems is excessive and will cause notable (unnecessary) ongoing expense to operators.

- Ofcom's has proposed amendments to GC14 and GC23 that compel communication providers ("CPs") to publish the location of access charge information in a variety of advertising, promotional and pre-sale scenarios. We support the overall goal of transparency but fear that these obligations will lead to a counter productive situation in which consumers are overloaded with information and confused as a result.

The remainder of this response contains Three's more detailed comments on the Dispute Resolution Guidance and NGCS Consultation, including responses set out against a number of the questions Ofcom has raised.

[1] http://stakeholders.ofcom.org.uk/consultations/price-rises-fixed-contracts/

080 and 116 number ranges: Consultation on proposed dispute resolution guidance.

Question 1: Do you have any comments on how we have applied these three Principles to generate the draft guidance in Annex 1?

Application of Principles to 080

Ofcom adopts three cumulative principles to estimate a range of F&R mobile and fixed origination charges in respect of 080 calls: cost recovery (Principle 1), benefits to consumers/impact on competition (Principle 2) and practicality (Principle 3). We agree with this analytical framework but not with the proposed application of Principle 2, which Ofcom has separated into two analytical steps:

- **Step 1, derivation of the appropriate average SP origination payment** – Three finds that the average SP payment that strikes the right balance for consumers is greater than the 1.5ppm level set by Ofcom;

- **Step 2, calculation of the appropriate level of mobile and fixed origination charges that results in the average SP payment in Step 1** – Ofcom's reliance on commercial negotiations informed by a wide range of F&R origination charges in its dispute resolution guidance will inevitably lead to disputes between operators. We propose that Ofcom determines a single, industry-wide gradient of F&R mobile origination charges instead.

We provide our comments on Ofcom's assessment of each step in turn.

Step 1 – the average SP origination payment that strikes the right balance for consumers is greater than 1.5ppm.

Summary of Ofcom's approach

Ofcom considers how different average SP origination payments may affect consumers. The analysis focuses on the trade-off between two offsetting impacts of higher origination charges:[2]

i) **Reduced availability/quality of services on the 080 range** – in Ofcom's view higher origination charges are ultimately passed on to SPs, which may prompt SPs to migrate to other number ranges;

ii) **Tariff Package Effect** ("TPE") – higher origination charges are likely to increase OCP's profits for calls to 080 numbers which, in Ofcom's view, is likely to reduce prices for other telecoms services and/or access.

Ofcom will only consider an origination payment to be F&R if it results in an average SP out-payment between 1 and 1.5ppm (i.e. an increase between 0.5ppm and 1ppm on the prevailing

[2] Para 12.59

0.5ppm origination rate). In its view, that range achieves the "right balance" for consumers between reduced service availability and the TPE.[3]

Ofcom relies mainly on the evidence presented in its April 2012 consultation,[4] with particular emphasis on the 2011 SP Survey (reproduced in Table 1).

Table 1. SP likelihood of "getting rid of" free to caller 080 number in response to higher origination payment (% of all 080 SPs).

Increase in origination payments	0.5ppm	1ppm	1.5ppm	2ppm
Very likely	8%	11%	18%	24%
Fairly likely	10%	7%	10%	12%
Unsure	10%	13%	14%	15%
Fairly unlikely	16%	24%	19%	15%
Very unlikely	55%	44%	38%	34%
Net likely[86]	19%	19%	28%	36%
Net unlikely[87]	71%	68%	57%	49%

Source: Ofcom

In particular, in April 2012 Ofcom found that:[5]

- increasing the average SP origination payment by 1ppm (instead of 0.5ppm) would likely be beneficial for consumers – i.e. would not affect the proportion of SPs likely to "get rid" of their 080 numbers (19%) but would lower retail prices for consumers via the TPE; but

- increasing the average SP payment by 1.5ppm would no longer be beneficial – i.e. would result in a significant reduction in service availability (to 28%), to be set against the "*moderate*" consumer benefits via the TPE.

In the current consultation, Ofcom continues to believe that an increase above the 1ppm level would have negative effects on consumers through a steeper reduction in service availability, which would "outweigh" the moderate consumer benefits in terms of lower prices for other mobile services (via the TPE).[6]

Ofcom's analysis indicates that the appropriate increase in the average SP origination payment is greater than 1ppm.

In Three's view Ofcom has set the maximum average SP payment at too low a level (1.5ppm, a 1ppm increase on the current 0.5ppm charge), because it has underestimated the extra benefits that consumers would derive from further increases in the average SP payment via the TPE, when weighing those benefits against the negative impact of reduced service availability.

[3] Para 12.60
[4] Para 12.110. Ofcom also considers other factors like the asymmetric risks and the potential for a caller externality which in its view support setting the maximum average SP payment below 1.5ppm
[5] Paras A23.80-A.23-82 of the April 2012 consultation and para 12.97 of the current consultation.
[6] Para 12.110

Ofcom's TPE is triggered by a change in an OCP's profits from calls to 080 numbers.[7] This change has two sources:

- the zero-rating of 080 calls (a negative effect on OCPs' profits) and
- the higher origination charge (a positive effect on an OCPs' profits, but also a negative effect on an SP's profits of equal magnitude – the SP pays the increased origination charge received by the OCP).

As Ofcom explains, calls to 080 numbers would remain free regardless of the level of the origination payment.[8] Hence, for the purposes of determining F&R origination charges, the assessment must take zero-rating of 080 calls as given and focus on the impact of different levels of the charge on service availability and the TPE.

Table 2 presents our estimates of the potential magnitude of the mobile and fixed TPEs and the change in SP 080 origination costs for different levels of the origination charge, based on Ofcom's main modelling scenario (which assumes no increase in overall 080 call volumes, no SP migration to other number ranges and a complete TPE). Ofcom presents similar figures in Tables A.28.7 and A28.9 of the Consultation.[9]

[7] A28.27
[8] Para A23.38 of the April 2012 consultation document.
[9] Our SP cost estimates are different from Ofcom's figures in Table A28.7. Ofcom estimates the increase in SP costs following an increase in the mobile origination charge, the fixed origination charge being fixed at 0.3ppm (if the share of mobile originated calls is 45%) or 0.6ppm (if the share is 60%). In contrast, we estimate the change in SP costs arising from a 0.5ppm increase in the average SP origination charge.

Table 2. Impact on mobile OCPs, fixed OCPs and SPs of different levels of the origination charge in Ofcom's main modelling scenario.

Change in mobile OCPs 080 profit following implementation of free to caller regime							
Share of 080 calls from mobiles	**Mobile 080 volumes (million minutes)**	**Mobile charge = 0.5ppm**	**Mobile charge = 1ppm**	**Mobile charge = 1.5ppm**	**Mobile charge = 2ppm**	**Mobile charge = 2.5ppm**	**Mobile charge = 3ppm**
45%	**2,973**	-£54m	-£39m	-£24m	-£9m	£6m	£21m
60%	**3,964**	-£57m	-£37m	-£17m	£3m	£22m	£42m
Change in fixed OCPs 080 profit following implementation of free to caller regime							
Share of 080 calls from mobiles	**Fixed 080 volumes (million minutes)**	**Fixed charge = 0.1ppm**	**Fixed charge = 0.2ppm**	**Fixed charge = 0.3ppm**	**Fixed charge = 0.4ppm**	**Fixed charge = 0.5ppm**	**Fixed charge = 0.6ppm**
45%	**3,634**	-£29m	-£26m	-£22m	-£18m	-£15m	-£11m
60%	**2,643**	-£30m	-£27m	-£25m	-£22m	-£19m	-£17m
Change in SP 080 costs following implementation of free to caller regime							
Share of 080 calls from mobiles	**Total 080 volumes (million minutes) – fixed and mobile**	**Avg SP payment = 0.54ppm**	**Avg SP payment = 1.04ppm**	**Avg SP payment = 1.54ppm**	**Avg SP payment = 2.04ppm**	**Avg SP payment = 2.54ppm**	**Avg SP payment = 3.04ppm**
45%	**6,606**	£0ppm	-£33m	-£66m	-£99m	-£132m	-£165m
60%	**6,606**	£0ppm	-£33m	-£66m	-£99m	-£132m	-£165m

Source: Three based on Ofcom data

The following conclusions can be drawn from Table 2:

i) Zero-rating of 080 calls (i.e. fixed and mobile origination charges at the current level of 0.5ppm) would reduce fixed and mobile OCP profits on 08 calls by £69m-£76m per annum (depending on the share of 080 calls from mobile)[10] – this is the TPE due to zero-rating;

[10] £69m is the total loss if the share of 080 mobile calls is 45%, and it equals the sum of £54m plus £15m (respectively, the changes in mobile and fixed 080 profits along the 45% row and corresponding to a 0.5ppm charge). Likewise, £76m is the total loss if the share of 080-originated calls is 60%, equals to £57m plus £19m.

ii) Every 0.5ppm increase in the charge raises the mobile and fixed TPEs by a constant amount (e.g. £15m and £18m p.a. respectively if 45% of calls to 080 numbers originate from mobiles). Correspondingly, a 0.5ppm increase in the average SP payment raises SP costs by the same amount (e.g. £33m p.a. if fully passed on by the TCP);

iii) Increases in the TPE are exclusively due to the higher origination charge, the impact of zero-rating being invariant with the level of the charge – i.e. in each case the TPE rises by an amount equal to the increase in the origination charge (0.5ppm for mobile, 0.1ppm for fixed) multiplied by the assumed volume of 080 calls.[11]

This analysis sheds light on the merits of Ofcom's assessment. Since the TPE increases linearly with the level of the origination charge, we agree with Ofcom that there must be a cut-off point above the 1ppm increase level where the negative effect of steep reductions in service availability would outweigh the (constant) maximum additional benefits arising from the TPE.

However, we see no basis for its conclusion that the cut-off point is at the 1.5ppm increase level – i.e. that at that point the negative effects of reduced service availability would "outweigh" the "moderate" consumer benefits of the TPE. First, Ofcom has not estimated the consumer impact of reduced service availability. Each additional 0.5ppm increase in the origination charge raises OCPs' profits on 080 calls and SPs' costs by the same amount: £33m p.a. (0.5ppm multiplied by 6,606m minutes to 080 numbers). Whether that figure overestimates or underestimates the change in the TPE and associated increase in SP 080 costs is unclear:

- on the one hand, Ofcom's main scenario assumes a complete TPE (i.e. full pass through of consumer benefits) and no SP migration to other number ranges, both of which tend to overestimate the magnitude of the TPE; but

- on the other hand, the impact on SP 080 costs and the reduced service availability reported in the 2011 SP Survey are also exaggerated, because Ofcom assumes full pass-through of higher origination charges from TCPs to SPs, yet it finds that the "precise scale and speed" of that pass through is "uncertain".[12] In addition, Ofcom's main scenario assumes no increase in overall 080 call volumes (which in fact are likely to increase due to improved price awareness and lower call prices from mobiles), which tends to underestimate the potential change in the TPE.

Second, Ofcom appears to have grossly underestimated consumer benefits from the TPE. It finds the benefits from the TPE to be "moderate" because, inter alia, "*higher origination payments mitigate the rises in the price of other mobile services that may otherwise occur as a result of making number ranges free to caller*".[13]

In effect, Ofcom has erroneously discounted the TPE by £69m-£76m per annum, the negative effect of zero-rating on OCPs' profits from 080. What matters is not the absolute level of the TPE for any given origination charge (i.e. the TPE figures in Table 2 above, which reflect the

[11] For instance, the £15m p.a. increase in the mobile TPE if 45% of calls to 080 numbers originate from mobile equals 0.5ppm multiplied by 2,973m minutes.
[12] Footnotes 96 and 61.
[13] Para 12.110, relying on paras A23.80-A23.82 of the April 2012 consultation.

offsetting effects of zero-rating and the assumed origination charge), but the change in the TPE due to an increase in the origination charge (i.e. the increase in the TPE figures as one moves to the right, which reflect solely changes in the origination rate).

In other words, Ofcom must take zero-rating as given. OCPs will suffer a large loss of profits from zero-rating (£69m-£76m per annum in Ofcom's main scenario), a "significant" proportion of which would be passed through to callers via the TPE according to Ofcom. The relevant question is whether the extra consumer benefits for every increase in the SP origination payment, a "significant" proportion of which would be passed on to consumers (via reduced prices or smaller price increases than would otherwise be the case), would outweigh the associated consumer loss due to reduced service availability.

Step 2 – Ofcom should adopt an industry-wide gradient of mobile origination charges.

In Step 2 Ofcom considers the level of mobile and fixed origination charges that would yield an average SP payment between 1ppm and 1.5ppm, taking into account its assumption that the share of calls to 080 numbers originated from mobiles is likely to increase from the current 5% to 45-60% after implementation of the free-to-caller regime.

Ofcom concludes that mobile origination charges between 1.5ppm and 2.5ppm (and fixed origination charges between 0.3ppm and 0.6ppm) would be F&R, whereas mobile origination charges in the 1.3-1.5ppm and 2.5-3ppm ranges would only be F&R "in a more restrictive set of circumstances" which it does not specify. Ofcom expects operators to draw on its guidance on F&R charges in any commercial negotiations on revised origination charges.

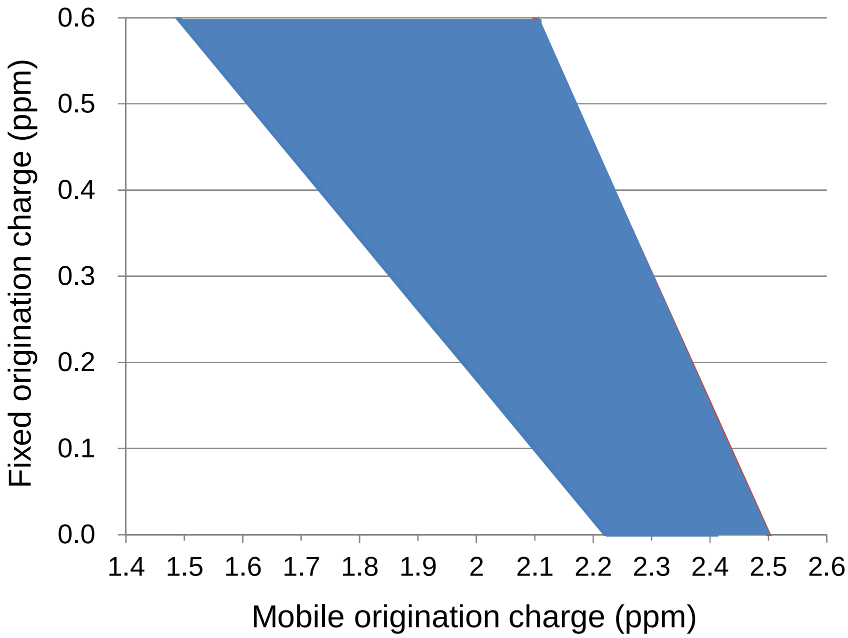
We explain in this Section why this approach will inevitably lead to disputes unless Ofcom adopts a single, industry-wide gradient of F&R mobile charges.

Ofcom's approach will inevitably give rise to disputes between operators

The blue-shaded shape in Figure 1 represents all combinations of fixed and mobile origination charges that are guaranteed to yield an average SP out-payment between 1ppm and 1.5ppm, provided the share of mobile-originated 080 calls is between 45% and 60%.[14]

[14] The boundaries of the blue-shaded shape are given by the range of the cost reflective fixed charge set by Principle 1 (0-0.6ppm) and two equations: $0.45x+0.55y > 1$ and $0.6x+0.4y <1.5$, where x and y represent the mobile and fixed origination charges respectively

Figure 1. Combinations of fixed and mobile origination rates that yield a 1ppm-1.5ppm average SP payment, for a share of 080 mobile originated calls between 45% and 60%.



By contrast, points immediately outside the blue figure represent charge combinations that would yield an average SP payment inside the 1-1.5ppm range in some cases but not others, depending on the values assumed for the share of mobile calls in the 45%-60% range (and beyond).[15]

Several problems with Ofcom's approach to F&R charges are apparent from Figure 1:

- The range of mobile and fixed origination charges preferred by Ofcom (the top-half of the figure, 1.5-2.5ppm and 0.3-0.6ppm) creates a very large number of possible F&R charge combinations;[16]

- Whether a given mobile origination charge yields an average SP payment within the required 1-1.5ppm range (i.e. whether a point on a vertical line falls inside the blue figure) depends on factors outside a mobile OCP's influence – i.e. the fixed origination charge (given the share of 080 calls from mobile phones in the 45%-60% range); and

[15] For instance, any point immediately to the left of the figure (e.g. 1.8ppm mobile charge, 0.3ppm fixed charge) yields an average SP payment within the required range in some cases (e.g. if the share of 080 calls from mobile is 60%), but one that is below 1ppm in other cases (e.g. if the share of mobile calls is only 45%). Likewise, a point immediately to the right of the figure (e.g. 2.3ppm mobile charge, 0.5ppm fixed charge) would yield an average SP payment within the required range in some cases (e.g. if the share of 080 calls from mobile is 45%) but one above 1.5ppm in other cases (e.g. if the proportion turns out to be 60%).

[16] As an aside, in our view Ofcom has not adequately justified narrowing the fixed origination charge to 0.3-0.6ppm in paragraphs 12.131-12.133 and Table 12.5 of the consultation.

- if the share of mobile-originated 080 calls is outside the 45%-60% range (as it is bound to be in the short term), even charge combinations inside the blue figure may yield average SP out-payments outside the 1-1.5ppm range (i.e. because the figure would shift to another position).

In Three's view these problems will inevitably lead to disputes between operators and create uncertainty in the industry. We discuss each issue and our proposed solutions below.

Ofcom should not rely on commercial negotiations

Three notes Ofcom's preference for mobile origination charges set by commercial negotiation and indicates in the Dispute Resolution Guidance that these charges will be F&R if they fall within its preferred 1.5-2.5ppm range. However, we do not anticipate that this approach will work in practice.

First, given the large range of possible F&R charges bilateral negotiations would be costly and lead to multiple charges reflecting the bargaining position of each pair of operators.

Second, as the largest TCP and transit provider BT is likely to set a mobile origination charge unilaterally towards the lower end of Ofcom's range, likely leading to endless disputes and appeals as witnessed in respect of BT's tiered termination charges.

Third, it seems to us that there is a fundamental problem with Ofcom's proposal to only consider an origination payment to be F&R if it results in an average SP out-payment between 1 and 1.5ppm, when all fixed and mobile charges agreed by the industry will simultaneously determine the average SP payment (given the share of mobile 080 calls). The fairness of an individual charge may then turn on the level of charges agreed by other OCPs. Suppose that Three disputes the charge paid to it by BT, which yields an average SP payment below 1ppm given all other charges agreed by the industry. On what basis would Ofcom rule against the bilateral BT-Three charge, instead of any other fixed and mobile origination charge that is not the subject of the dispute?

In Three's view these problems can be avoided if Ofcom narrows the range of potential F&R mobile origination charges. Figure 1 shows that a mobile origination charge set at 2.15ppm would yield an average SP out-payment in the 1-1.5ppm range regardless of the level of the fixed origination charge, provided the share of mobile 080 calls falls between 45% and 60% - i.e. a vertical line from 2.15ppm would be almost entirely inside the blue figure.

Table 3 confirms that result. If the mobile charge is set at 2.15ppm, the average SP out-payment lies within 1.0-1.5ppm for any level of the fixed origination charge and share of mobile-originated 080 calls in the 45%-60% range, with two minor exceptions (in red).

Table 3. Average SP payment for different levels of fixed origination charge and share of 080 calls from mobiles, mobile origination charge set at 2.15ppm.

Fixed origination charge (ppm)	45%	50%	55%	60%
0.0	0.97	1.08	1.18	1.29
0.1	1.02	1.13	1.23	1.33
0.2	1.08	1.18	1.27	1.37
0.3	1.13	1.23	1.32	1.41
0.4	1.19	1.28	1.36	1.45
0.5	1.24	1.33	1.41	1.49
0.6	1.30	1.38	1.45	1.53

Source: Three (based on Ofcom data)

Ofcom should set an industry-wide gradient of mobile charges

The previous section shows that it possible to derive a single, industry-wide mobile origination charge for a given range of shares of mobile-originated calls to 080 numbers. A final problem with Ofcom's approach is that the share of mobile-originated 080 calls will change over time – and with it the range of potential F&R charges.

Ofcom assumes that the share of mobile-originated 080 calls will rise from 5% in 2009 to 45-60% by late 2014 following implementation of the free-to-caller regime. This is based on evidence from the Department for Work and Pensions ("DWP") showing that the proportion of mobile calls to the 080 DWP number has grown to c.45-50% since calls were made free in Jan 2010). Ofcom also considers the estimated share of all UK voice calls and of UK residential voice calls originated from a mobile phone by late-2014 (58% and 47% respectively), and some anecdotal evidence.[17]

In Three's view:

- The 58% mobile share of overall voice calls (including business calls) seems irrelevant for the purpose of determining F&R origination charges – Ofcom's intervention is only aimed at residential consumers;

- We agree that, <u>in the medium term,</u> there is no reason to expect that the mobile share of 080 calls will differ significantly from the 47% share of mobile-originated UK residential voice calls – once fixed and mobile calls are free, callers can be expected to use whichever device is more convenient.

Hence, we think it reasonable to assume that 45%-50% of 080 call minutes will eventually originate from mobiles, which is also consistent with the evidence from DWP. Importantly, that level of mobile-originated 080 calls will not be reached immediately as Ofcom assumes. If confidence in the 080 range is as low as Ofcom suggests, the short run effect of zero-rating on

[17] Paras 12.121-12.127

mobile 080 volumes is likely to be limited, as consumers learn about the zero price from mobiles and adapt their call patterns accordingly. In the medium to longer term, once consumer confidence in the number range is restored, a 45%-50% range looks reasonable.

It follows that, if the share of mobile-originated 080 calls is outside Ofcom's current 45%-60% range (as it will be in the short term), origination charges within the ranges proposed by Ofcom (0.3-0.6ppm for fixed, 1.5-2.5ppm for mobile) are likely to yield an average SP payment outside the required range and so will not be F&R.[18] To avoid future disputes, it seems advisable to set a single gradient of (industry-wide) mobile origination charges corresponding to different shares of mobile-originated 080 calls over time.

Conclusion

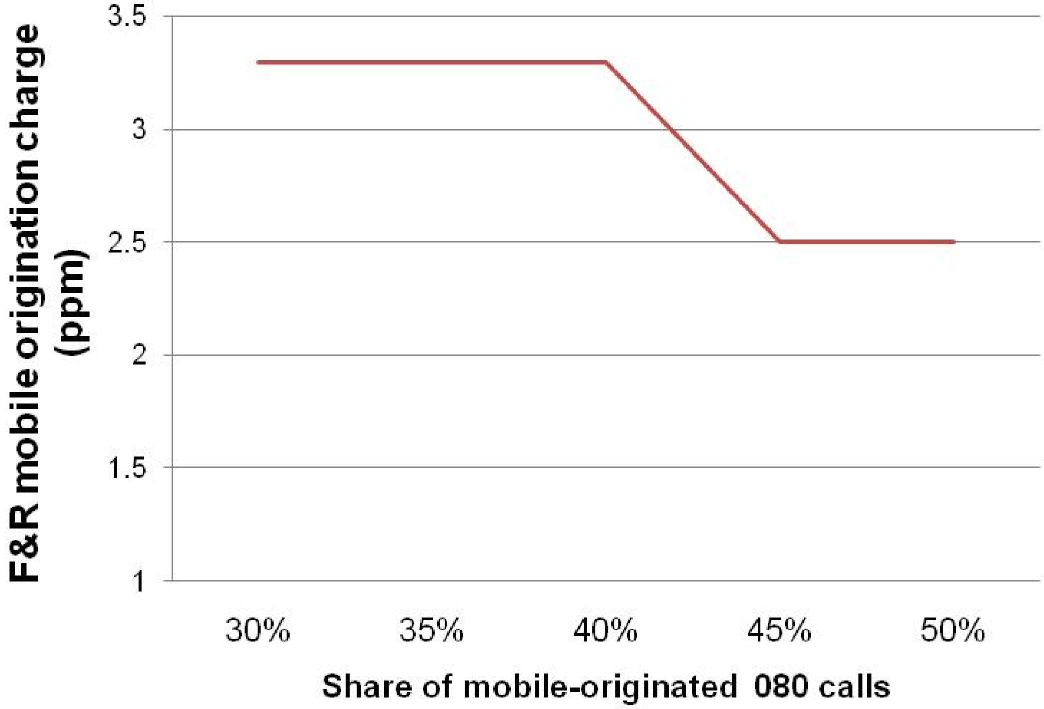
In summary, Three finds that Ofcom has set a maximum average SP out-payment that is too low (1.5ppm) and has assumed a range of the share of mobile-originated calls to 080 numbers that is too high. In consequence, Ofcom has derived a range for the F&R mobile origination charge that is unacceptably low (1.5-2.5ppm). In Three's view Ofcom should adopt a single (industry-wide) gradient of F&R mobile origination charges, based on a long run share of 45-50% of mobile-originated calls to 080 numbers, with smaller shares assumed in the short term.

Figure 2 presents Three's proposed gradient of F&R mobile origination charges based on the following assumptions: i) the average SP payment that strikes the right balance for consumers is between 1ppm and 1.7ppm (instead of 1-1.5ppm); and ii) the share of mobile-originated 080 calls rises quickly to 30-40% within the first few months, and stabilizes at around 45-50% after a year, consistent with DWP's experience.[19]

The resulting mobile OC would be 3.3ppm in 2015, going down to 2.5ppm in subsequent years. Those charges would yield an average SP out-payment between 1ppm and 1.7ppm, regardless of the level of the fixed origination charge within the 0-0.6ppm range.

[18] For instance, a 2ppm mobile charge and 0.5ppm fixed charge would yield an average SP out-payment of 0.875 if the share of mobile calls is only 25%, and so would not be inside the blue figure in Figure 1
[19] Paras 12.122 of the current consultation, and 16.86 of the April 2012 consultation

Figure 2. Three's proposed gradient of F&R mobile charges



Source: Three (based on Ofcom data)

Ofcom is in danger of breaching its own principles and missing an opportunity to reduce service provider (SP) costs in the 116 range.

Ofcom acknowledges that mobile OCPs currently recover origination payments of 0.5ppm for calls to 116 numbers and that this rate is below their efficiently incurred costs. We believe that in practice Ofcom's fair and reasonable guidance (as it relates to 116 calls) will ensure this situation persists under the new regime regardless of whether MNOs agree with the outcome.

The second scenario detailed in para 3.69 of the Dispute Resolution Guidance suggests that Ofcom will allow mobile OCPs the opportunity to negotiate an origination payment of 0.8-0.9ppm, the corresponding fixed payment being 0.0 – 0.1ppm.

We know from long experience of negotiating with powerful fixed providers integrated across the whole market (such as BT), that smaller mobile OCPs (such as Three) will be at a significant disadvantage in trying to secure OCs that recover our efficient costs.

Simplifying non-geographic numbers - Policy position on the introduction of the unbundled tariff and changes to 080 and 116 ranges. (The NGCS Consultation)

Before turning to Ofcom's specific questions, Three has a number of comments and observations on the content of Ofcom's NGCS Consultation and the Dispute Resolution Guidance as they relate to the proposals to make 080 free to caller.

In parallel we are concerned that the practical effects of Ofcom's proposals will negatively affect the wholesale market and may result in some serious delays and risks to Ofcom's timetable and overall policy goals.

Ofcom's proposed 080 access condition would adversely affect the wholesale market.

Ofcom is being overly optimistic in assuming that TCPs and OCPs will reach agreement regarding the fair and reasonable origination charge to apply bilaterally between them. We fear that the dynamics of the market will mean that OCPs and TCPs are unlikely to reach agreement, not least because of the wide range of potentially fair and reasonable mobile origination charges Ofcom has set out in the Dispute Resolution Guidance.

In the likely event that OCPs and TCPs reach deadlock in their negotiations, Ofcom will inevitably be required to opine on bilaterally negotiated origination rates for calls to 080 ranges via the dispute resolution process provided for under the Communications Act 2003. In our view, Ofcom's preference for using a dispute-resolution based wholesale remedy rather than the rigours of the market review and SMP process to address industry concerns about the wholesale market, is:

a. A poor use of Ofcom's finite resources,

b. will increase costs to industry and

c. will lead to uncertainty amongst operators regarding the actual origination charges to be levied.

Whilst Ofcom's proposed approach may seem more expedient and efficient in the short term, in the longer term it puts Ofcom in the position whereby it will need to use a further limb of regulatory intervention (namely, dispute resolution) to determine numerous OCP origination charges, all within the confines of the 4 month dispute resolution timetable. In our view, the better approach would be to set the mobile origination charge, rather than simply suggest a wide range of possible fair and reasonable possibilities. As explained in our response to the Dispute Resolution Guidance (above), we have identified the mobile origination charge gradient that will best achieve Ofcom's objectives as being 3.3ppm in 2015, falling to 2.5ppm in subsequent years.

BT's Standard Interconnect Agreement and use of the F&R Guidance results in a huge imbalance of power.

As Ofcom is already aware, all CPs wishing to interconnect with BT must sign the Network Charge Control Standard Interconnect Agreement ("the SIA"). The SIA, together with its various annexes and schedules, provides for the terms and conditions on which calls between BT and the respective CP's networks are connected, including charges.

For example, pursuant to the SIA:

- Three sends calls originating on its network to BT for termination either: a) on BT's network; or b) on the network of other TCPs, whereby the call transits via BT's network. The charges for these services, referred to in the SIA as "BT service or facility" are set as between Three and BT under Paragraph 12 of the SIA.

- BT sends calls to Three for termination on Three's network that either: a) originate on BT's network; or b) originate on a third party operator, whereby the call transits via BT's network. The charges for these services, referred to in the SIA as "Operator service or facility" are set as between BT and Three under Paragraph 13 of the SIA.

BT therefore plays a crucial role not only as an OCP and TCP, but also as a provider of transit[20]. Three, together with the other MNOs, are currently in dispute with BT with regard to the way in which Paragraph 12 of the SIA operates, and the unequal contractual balance of power that it creates. In February 2012 Three referred this dispute to Ofcom. This remains an open case, and Ofcom has not yet published its final determination[21] (the "SIA Dispute").

The mechanisms for introducing price changes under Paragraphs 12 and 13 of the SIA have important commercial and legal implications for the way in which the origination charges for 080 calls to be set under the TCP access condition will be set. Further confusion is added by the fact that, under Ofcom's proposals, the origination charge to be proposed by BT (and the other TCPs), can also be categorised as a negative termination charge to be paid by operators to BT, similar to the charges that were previously set by BT under NCCN 911. The difficulties of accurately categorising such a charge were discussed in detail in Three's submission in the SIA Dispute and in the Competition Appeal Tribunal's judgment in the 08 ladders litigation[22]. Therefore, determining whether the mobile origination charge is a "BT service or facility" under Paragraph 12 or an "Operator service or facility" under Paragraph 13, is far from clear.

Notwithstanding this inherent tension and confusion when categorising the charges to be introduced for 080 calls, we are particularly concerned that BT's power under Paragraph 12 of the SIA to unilaterally introduce changes to charges for BT services even if such charges are not agreed by the counter-party CP, will result in: a) BT introducing mobile origination charges

[20] CPs also have the option to directly interconnect their network to that of other CPs, entering into bilateral interconnect agreements. However, in our experience, such arrangements are only likely to be feasible financially if large volumes of traffic are likely to be exchanged between the two networks.

[21] http://stakeholders.ofcom.org.uk/enforcement/competition-bulletins/open-cases/all-open-cases/cw_01083/

[22] Paragraphs 68 and 69 of CAT's judgment, see http://www.catribunal.org.uk/238-7221/Judgment.html

that are not fair and reasonable; b) deadlock between the parties; and c) dispute referrals to Ofcom, with the consequent uncertainty that such delay will bring.

In the NGCS Consultation Ofcom references the SIA Dispute as having a bearing on the decision to use the draft access condition[23]. We agree that these two issues are linked, however, we suggest that a third issue is also of key importance, namely Ofcom's proposed wide range of mobile origination charges of 1.5ppm to 2.5ppm[24] which, it suggests, could be found to be fair and reasonable in the event of a dispute. ✂

Ofcom proposed the access condition as a way to reduce the reliance on commercial negotiation and introduce some ex-ante regulation to address the risks it sets out in the NGCS Consultation[25]. For the reasons explained above the proposed Dispute Resolution Guidance undoes any benefit that may have been realised by the access condition (ex-ante- regulatory intervention) and it is in our opinion likely to be ineffective in practice.

Ofcom's approach hands significant advantages to vertically integrated CPs.

In addition to the inevitable (protracted) disputes at the outset of the implementation of the new free to caller regime, the evolving scenario specific factors that will be considered by Ofcom in determining what it deems to be F&R means vertically integrated CPs (e.g. BT) will be conferred a significant ongoing advantage in setting future OCs.

This situation comes about because Ofcom will conclude a dispute by reference to an average SP payment that is contingent on a number of variable factors (such as the levels of fixed and mobile OCs and the split of 080 traffic between network types). It is these data points that will be considered in the specific disputes about what constitutes a F&R OC on which Ofcom will adjudicate.

✂

We urge Ofcom to give detailed consideration to these risks when formulating their final conclusions.

[23] Para 14.16.3

[24] Para 3.51 080 & 116 the Dispute Resolution Guidance.

[25] Para 14.11 2013.

Three continues to have concerns about Ofcom's ability to regulate retail pricing in the absence of a finding of SMP.

Three would like to reiterate our reservations about Ofcom's approach to regulating retail pricing. Three accepts that Ofcom has consumer protection powers and that Ofcom may regulate via the NTNP. However, given the draconian nature of regulating retail pricing in an otherwise competitive market, Ofcom must be more explicit about the borderlines and the limits Ofcom sets on itself to impose retail regulation absent an SMP finding.

Failure to do this jeopardises Ofcom's overall policy programme by unnecessarily inviting an appeal by a party concerned at Ofcom's erosion of the fundamental principle that price regulation is a measure of last resort, contingent on a finding of SMP.

With respect to the retail pricing of calls to 080 numbers, we reiterate our concerns about Ofcom's approach to using the Rights of Use regime to impose regulation on OCPs also.

Three has already set out a number of comments on Ofcom's proposed use of its legal powers.[26] In relation to the NGCS Consultation, Three remains unconvinced by Ofcom's assertion that its power to impose conditions on *"rights of use"* for numbers under Part C of the Annex to the Authorisation Directive ("Part C") grants Ofcom a wide power of retail price control absent a finding of SMP, including the right to regulate the retail price of OCPs.

When interpreted in light of the scheme and language of the Authorisation Directive and the wider context of the European regulatory framework, Part C cannot properly be understood to cover the activities of originating and conveying a call to a non-geographic number (and s58(1)(aa) of the Communications Act 2003 should be interpreted accordingly). Three considers that its narrow interpretation of Part C is correct and therefore encourages Ofcom to drop this wholly avoidable contortion of the regulatory regime and its interpretation.

In addition, Three remains of the view that greater clarity is still required on Ofcom's consumer-protection based power to regulate retail prices, absent a finding of SMP. Three notes Ofcom's comment that it is unable to fetter its discretion on exercising its power under section 58(1)(aa), and welcomes the fact that Ofcom would "*in principle…only expect to use it in limited circumstances and where clearly necessary to protect consumers*" and the requirements for Ofcom to observe important safeguards such as ensuring any conditions set or modified under this power would be objectively justifiable, proportionate, not unduly discriminatory, transparent and subject to best regulatory practice principles.[27]

[26] See, for example, Three's Response to Ofcom's Second Consultation on Simplifying Non-geographic Numbers of 4 April 2012.

[27] See A13.97 of the 2013 Consultation.

However, Three remains concerned that the precise boundaries between the exercise of a consumer protection-based power under s58(1)(aa) and Ofcom's SMP-based powers are still unclear.[28]

Ofcom has gone some way to addressing this concern by pointing out that "*section 58(1)(aa) cannot be used as an alternative approach to regulating undertakings identified as having SMP on a relevant market*"[29] and noting that the exercise of SMP powers will require a SMP finding and must be based on the nature of the problem identified (e.g., typically relating to the potential for an undertaking to SMP to engage in excessive pricing, predatory pricing, etc), with SMP remedies having the twin objectives of promoting effective competition and "*pursuing public interest needs*" (i.e., to protect consumers).[30]

However, how this will work in practice remains unclear since, as Ofcom rightly notes on the exercise of its powers, "*all of our regulatory interventions can be ultimately traced back to the consumer interest*."[31] It would be helpful if Ofcom could provide some further guidance on how and when it proposes to use its s58(1)(aa) and/or its SMP-based powers to regulate pricing going forward. Three is concerned about the risk of potential wide-ranging (and inappropriate) use of s58(1)(aa) in practice if no SMP-finding is required.

We believe Ofcom's policy goal is exposed to appeals on points of legal principle.

[28] As Vodafone has pointed out, retail intervention triggered by a competition objective is by its very nature designed to protect consumers: A13.44, 2013 Consultation.

[29] See footnote 425 of the 2013 Consultation

[30] See A13.100 of the 2013 Consultation.

[31] See A13.99 of the 2013 Consultation.

Additional Consultation Questions.

Legal instruments (Section 6, Annexes 14 to 18)

Q6.1: Do you have any comments on the notifications in Annexes 14 to 18 and the draft modifications set out within them? Where you disagree with any of the proposed modifications, please explain why.

Ofcom must ensure that the GC modifications in respect of non-geographic numbers are considered in the context of the proposals for Price Rises in Fixed Term Contracts.

Before turning to the specific modifications to legal instruments proposed in the NGCS Consultation we believe it is important that Ofcom properly consider the interdependencies with the Price Rises in Fixed Term Contracts consultation.

In our response to that document[32] Three argued that there are charges and costs passed on by a CP which are beyond their control. It follows that these should fall outside the scope of any regulatory changes that Ofcom is considering in respect of price rises.

An increase in SC for an unbundled tariff number illustrates perfectly the kind of situation which may result in a customer experiencing an increased cost part way through a contract but the cause of which cannot be controlled by the operator. It would be unreasonable for Ofcom to take a purist approach and direct that CPs should simply absorb the cost of such increases.

It is important that Ofcom ensures the teams working on the respective initiatives (NGCS and price increases) properly consider the interdependencies between the two matters to avoid inconsistencies, inequality and confusion.

We further discuss the practical difficulties of SC changes in our comments on GC14.14 below.

Three's comments on proposed changes to General Conditions (GC).

We have the following observations in respect of the notifications and draft modifications detailed in the NGCS Consultation:

General Condition 14

GC14.10 – Three is concerned that the requirement set out in GC14.10 is not only an unnecessary duplication of regulation governing advertising and promotional material but may be unworkable and confusing for consumers in practice.

Existing regulation of advertising and promotional material[33] already requires advertisers to ensure that consumers are given sufficient information to make an informed decision and to ensure that we don't make misleading omissions.

[32] http://stakeholders.ofcom.org.uk/binaries/consultations/gc9/responses/Three.pdf

[33] For example the Consumer Protection from Unfair Trading Regulations & CAP Code.

It seems disproportionate and unnecessary for Ofcom to impose another very specific, duplicitous condition via the General Conditions on CPs alone (and not the service providers) which relates to non-geographic numbers.

Moreover when applied in practice to above the line advertising campaigns this requirement adds yet another level of detail which has to be incorporated. There is a danger that the level of information that would have to be conveyed to a consumer in what is normally a very narrow time window will not only overshadow the key point of the advert, but that it will overwhelm and confuse people trying to understand what is being offered. It is likely to detract from other, arguably more important terms or charges that might apply to the contract/service being advertised – for example, the minimum term, monthly line rental or inclusive allowance.

This problem is particularly acute when we consider the application of GC14.10 to TV or radio advertising, which goes through a pre-clearance process to ensure compliance with the already substantial amount of existing regulation. For example if a CP has a 20 second ad – is it proportionate or even appropriate to specifically reference the Access Charge (over and above any other important terms or charges that might apply to the contract).

GC14.11 – We note that there is now a requirement to ensure that consumers are given information at the point of sale about where to find the AC for “non-GC23” mobile tariff sales, i.e. 1-month SIM Only and pre-pay tariffs. We question whether this is realistic given that these are often unassisted sales which take place in a variety of (often non-mobile) retailers. We struggle to understand how in practice this information could be usefully communicated to a consumer, along with the other (arguably more) important facts a customer needs before reaching a purchase decision.

Three believes Ofcom should delete the mobile element of GC14.11 on the basis of it being impractical to implement.

GC14.14 – CPs will naturally provide customer service support which would (by its nature) have to handle complaints and enquiries about access charges and calls to unbundled tariff numbers regardless of the presence of a GC requirement.

However Three is particularly concerned that where an SC changes, customers may not be immediately aware given there is no requirement on SPs to proactively notify them of such an event, this should be rectified and a relevant obligation should be imposed on SPs[34].

Moreover Ofcom (as part of the implementation & communication phase) should ensure that SC information is readily accessible to customers by way of an easily understandable central reference point (e.g. website).

Given the burden currently rests with CPs to handle the complaints even where the cause of the issue is beyond their control we believe Ofcom should more clearly specify the requirements in GC14.14 to reflect the fact that in the case of complaints about SCs, CPs are likely to only be able to direct customers to either the SP or the centralized list of SCs being managed by Ofcom.

[34] E.g. where a customer uses a number regularly without referring to the SPs website or other literature.

On the basis that we believe the real world customer experience may be poor under the current proposals OCPs may decide to introduce mechanisms to ensure customers are informed about changes in SCs.

This process would need the assurance of pre-agreed intervals at which SCs change and at least 8-10 weeks lead time prior to such an update. We believe it would to Ofcom's benefit (in respect of its overall policy goals) to specify a SC change minimum notice period to make it more feasible for OCPs to design and implement a better customer experience should they so wish[35].

However, given introducing such a process would confer yet further cost and operational burdens on OCPs, we strongly believe that our initial proposal of ensuring SPs are obligated to proactively notify consumers of SC changes combined with the centralized (customer friendly) publication of information is a fairer distribution of effort and cost.

General Condition 17

GC17.20 – We are concerned that the addition of the phrase "as Ofcom may direct" empowers Ofcom to make onerous demands and requests of CPs during the implementation phase. Three recognises the importance of timely introduction of the systemic changes needed to support the new regime but would like Ofcom to understand that this project will be among many other critical projects (some also initiated by regulatory changes) which have to be managed using limited resource.

We are concerned that the addition of the wording above means Ofcom will set interim deadlines and make demands which suit their own purpose but that subsequently cause disruption or changes to an individual CPs resourcing and sequencing of this and other programmes.

Beyond setting a deadline for introduction of the new regime and high level milestones (such as billing system delivery), Ofcom should allow CPs to manage implementation in the way that suits them best. With this in mind, and to give more comfort to CPs, we believe GC17.20 should simply read:

17.20. In preparation for the fulfillment of its obligations under paragraphs 17.22 to 17.32 from (and including) the Effective Date, the Communications Provider must take all steps it considers necessary prior to the Effective Date.

GC17.31 – Three has previously contended that Ofcom should limit the number of SC price points that must be provided by CPs to a maximum of 60. We disagree with Ofcom's decision to specify the minimum as 100 and again point out that this creates the risk of a notable ongoing operational cost to CPs.

As Ofcom's research shows most SCs are likely to be in a narrow range of charge bands (probably near the cap) and therefore the requirement to build (and resource) the high level of flexibility demanded by Ofcom suggests the solution is being somewhat gold plated at CPs expense.

[35] We note Ofcom's current preference to leave it for industry to negotiate.

Indeed it could be argued that by adding many multiples of price points could be self defeating in the context of Ofcom's overall policy objective of simplifying the customer experience. There is a of course balance to be struck between simplification and encouraging competition between SPs, but we think this is more than achieved by mandating 60 prices points in OCP billing systems.

General Condition 23

GC23.5 C (ii) – Whilst we agree that transparency is important; we question whether it is necessary for Ofcom to explicitly require that the AC is provided in detail at the point of sale in addition to the other key charges that operators provide.

Regulatory changes in recent years have resulted in an ever increasing level of detail that must be given to consumers at the point of sale – which whilst well intended – often has the effect of overwhelming them with information and creating more confusion for customers. Specifically requiring CPs to give the AC adds to an overload of information that we are concerned may in the end become unhelpful and counterproductive.

Furthermore the points we raise in respect of GC14.14 are applicable because whilst MNOs may be required under GC23 to provide details about the AC the possible variable nature of the SC is as likely to cause customer dissatisfaction and MNOs have no control over that element of a customer's costs.

In conclusion we believe that whilst the AC may be a "key charge" for some tariffs, CPs should have the discretion to tailor the key charge information to the customer rather than being incentivised to adopt a tick box approach which is likely to result in unnecessary confusion. On this basis we believe Ofcom should delete the specific reference to ACs from GC23.

Assessment of costs (Annex 10)

Q10.1: Do you agree with our estimates of the billing costs for implementing the unbundled tariff? If not, please explain why and provide evidence to support your response, particularly of the level of costs you are likely to incur as a result of our approach.

As detailed in our answer to Question 6.1 (GC17.31) we disagree that the imposition of a requirement to support 100 SC price points is "reasonable" and reiterate our view that 60 price points is sufficient and more proportionate.

More generally we welcome Ofcom's engagement with the industry to assess differences in costs depending on CPs' size and other characteristics. However, we were not in a position to review Ofcom's calculations in detail due to confidential nature of the data used as inputs.

Q10.2: Do you agree with our estimates of the level of misdialling costs for calls to service providers who may migrate as a result of making 080 free-to-caller? If not please explain why and provide evidence.

We agree that the costs presented in Table 10.18 are likely to overestimate the misdialing costs for calls to SPs who may migrate as a result of making 080 free-to-caller. More specifically, if some SPs migrate away from the 080 range, the misdialed calls will not be connected and therefore there will be minimal network costs associated with these calls.

Q10.3: Do you agree with our estimates of the level of consumer time costs as a result of making 080 free-to-caller? If not please explain why and provide evidence.

We do not have any comments on Ofcom's estimates of consumer time costs as a result of making 080 free-to-caller.

Quantified benefits assessment (Annex 11)

Q11.1: Do you agree with our assessment of the impact of implementing the unbundled tariff on the 09 range is likely to be positive overall? If not please explain why.

Three broadly agrees with Ofcom's analysis. We consider that if Ofcom implements tariff unbundling for 084/087 number ranges, the same tariff principles should be applied to 09 number range in order to improve transparency and minimize confusion among customers.

Framework for assessing free-to-caller origination payments (Section 12)

Q12.1: Do you agree that we should rely on our estimates of the cost of BT's call origination in the Narrowband Market Review to derive the fixed origination payments for the Impact Assessment Range for origination charges? If not, please explain why.

In the context of zero rating of 080 and 116 numbers Three has no specific comment on this point.

Q12.2: Do you agree that the upper bound of non-network costs that are relevant to recovery through origination charges to 080 numbers should be LRIC+ excluding A&R, billing and bad debt costs? If not, please explain why.

Please refer to our answer to Question 1 to The Dispute Resolution Guidance.

Q12.3: Do you agree that the asymmetric risk of the level of payments supports limiting the increase in SP average outpayments below 1ppm? If not, please explain why.

No. We do not believe that Ofcom makes the right comparison where it concludes that "the *potential adverse effect on consumers of origination charges that are too high is likely to be more significant than those arising from origination charges that are too low*".[36]

As set out in our response to Question 1 to the Dispute Resolution Guidance, Ofcom's analysis focuses on the trade-off between the TPE and reduced service availability. We understand that Ofcom is concerned about the potential for asymmetric risk if Ofcom sets the cut-off point at a level that is "too low" or "too high".

For instance, if the 2011 SP survey overstates (or understates) the actual reduction in service availability that would result from a given increase in the average SP payment, then Ofcom's assessment would set too low (or too high) a charge – i.e. the average SP payment that strikes the right balance for consumers would be higher (lower) than the one determined by Ofcom.

By definition, if Ofcom's average SP payment is "too high" consumers would lose more by way of reduced service availability than they would gain from the lower prices (or smaller price reductions than would otherwise be the case) arising from the TPE. Conversely, if the payment is set at "too low" a level, then consumers would benefit from further increases in the average SP payment, as they would gain more from the TPE than they would lose via reduced service availability. A priori, there is no reason to believe that an average SP payment that is "too high" would be more detrimental to consumers than one that is "too low". Hence, we do not believe that Ofcom has adequately justified its conclusion in relation to the alleged asymmetric risk.

Q12.4: Do you agree that the potential for a positive caller externality supports limiting the increase in SP average outpayments to below 1ppm? If not, please explain why. Simplifying non-geographic numbers - Part A Annexes 1 to 7 7

No. Ofcom (correctly in our view) dismisses the potential for a positive network externality that would justify a higher average SP payment, on the basis that a certain proportion of that increased revenue is likely to be retained by the OCP as profit, while the remainder may be dissipated in competition for non-marginal subscribers.[37]

However, Ofcom does not consider whether similar arguments apply in respect of the "positive caller externality" at the other end of the market. In effect, Ofcom proposes to reduce the average origination charge payable by SPs, to induce them to take callers' interests into account when deciding whether to remain on (or move to) a free to caller 080 range. But Ofcom does not enquire whether TCPs, who would benefit from the reduced origination charge in the first instance, would pass on those benefits to SPs.

In that context, Ofcom appears to ignore the rulings of both the Competition Appeal Tribunal and the Court of Appeal in relation to BT's tiered termination rates, where they conclude that the extent to which TCPs may pass-on any additional benefit received to SPs (i.e. what Ofcom

[36] Para 12.100
[37] Paras 12.36-12.42

called the "Indirect Effect") is "so *speculative as to be incapable of being weighed in the balance*".[38] In consequence, Three invites Ofcom to dismiss the potential for a caller externality.

Q12.5: Do you agree that SPs are likely to resort to alternative measures to mitigate the costs of calls from mobile (e.g. routing the mobile calls to a recorded announcement) at higher mobile origination payments? Do you agree that this supports a Base case scenario range towards the LRIC differential? If not, please explain why.

Three does not host SPs and therefore does not have the visibility that BT, C&W or other TCPs have in respect of SPs realistic likelihood of using alternative mitigation measures in response to increases in mobile OCs.

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Wholesale free-to-caller regulation (Section 14)

Q14.1: Do you agree that the notice to be given by TCPs of initial revisions to origination charges (as set out in the draft access condition):
(i) should be given to OCPs; and
(ii) should be given within one month of the condition being set?
If you do not agree, please explain why.

For reasons set out in detail in earlier sections the access condition as proposed (in combination with The Dispute Resolution Guidance) is likely to result in a mobile OC that is too low and result in adverse effects on the wholesale market.

In respect of point (ii) we agree that the notice of proposed origination charges should be given to OCPs within one month of the access condition being set.

We believe the solutions proposed by Ofcom will lead to a large number of disputes which may take a considerable time to resolve. The earlier the notice is served the sooner the dispute processes can begin; this may reduce the likelihood of delays to Ofcom's preferred (overall) timetable.

[38] http://www.bailii.org/ew/cases/EWCA/Civ/2012/1002.html