



**Consumer
Focus**
Campaigning for a fair deal

Consumer Focus response to Ofcom consultation on wholesale mobile voice call termination

June 2010

About Consumer Focus

Consumer Focus is the statutory consumer champion for England, Wales, Scotland and (for postal consumers) Northern Ireland.

We operate across the whole of the economy, persuading businesses, public services and policy makers to put consumers at the heart of what they do.

Consumer Focus tackles the issues that matter to consumers, and aims to give people a stronger voice. We don't just draw attention to problems – we work with consumers and with a range of organisations to champion creative solutions that make a difference to consumers' lives.

Wholesale mobile voice call termination

Consumer Focus welcomes the opportunity to respond to volume two of Ofcom's review of wholesale mobile voice call termination. This response is non-confidential and we are happy for it to be published on the Ofcom website.

In view of the benefits that lower Mobile Termination Rates¹ (MTRs) have delivered to consumers to date, Consumer Focus supports the reduction in MTRs being proposed by Ofcom in this consultation paper. We note that the negative consequences for consumers of lower MTRs that have been predicted by some mobile operators have not been widely observed to date, reducing the credibility of these forecasts. However, we urge Ofcom to continue to observe carefully the impact of falling MTRs, particularly on vulnerable and disadvantaged consumers. This response will expand on these points below and will address some of the specific proposals Ofcom has put forward in the consultation paper.

Support for reducing Mobile Termination Rates

Consumer Focus supports Ofcom's continuing regulation of MTRs and the proposed rates that will be applied up to 2014/15.

As Ofcom has identified, the call termination services offered by each individual communications provider are not constrained by competition. We believe that, for the time being, the lack of competitive pressure on MTRs makes the ongoing regulation of termination rates necessary. Given this, we are supportive of Ofcom's approach to defining markets for call termination, in which each market for calls to a given mobile number range for which a provider determines the termination rate will be defined as a separate market.

Similarly, based on the analysis set out in the consultation paper, we do not have any objections to Ofcom designating each communications provider as having significant market power in the market for terminating voice calls over the mobile number range it controls. We do not foresee any significant changes to this situation during the period up to 2014/15.

In our response to Ofcom's 2009 review of wholesale mobile voice call termination, Consumer Focus set out our position in support of a reduction in MTRs. We suggested that MTR reduction should take place as fast as reasonably possible, while remaining predictable and avoiding any sudden changes to the MTR regime that could have unintended negative consequences for consumers.

In keeping with this, we are supportive of the termination rates that Ofcom proposes to set from 2010/11 to 2014/15. We are satisfied that the proposals represent a determination to make a significant cut to MTRs over the next five years, with changes taking place along a consistent glide path that will ensure predictability and alignment across all mobile networks.

Consumer Focus' support for a reduction in termination rates is based on the benefits to consumers that have been delivered against a backdrop of falling MTRs in recent years.

¹ **Mobile Termination Rates** are the charges which one telecommunications operator charges to another for terminating calls on its network.

Falling prices and increased mobile penetration have combined to deliver enhanced competition and investment in new services such as mobile broadband. Our view is that a continuing reduction in MTRs, of the kind that Ofcom is proposing, is likely to further reduce retail prices, drive competition and continue to deliver consumer benefits between now and 2015.

It will be important, however, for Ofcom to monitor the impact of reduced MTRs on retail prices, with a view on ensuring that cuts are passed on to consumers in the form of lower prices. This is particularly the case in the fixed-line market, where lower termination rates increase the potential for a retail price cut.

Predicted negative consumer impact of lower MTRs

Consumer Focus notes that reductions in MTRs in recent years have been accompanied by predictions by some mobile operators of negative consequences for consumers. The experience of recent years suggests that warnings over the impact of lower MTRs have not generally been borne out in reality.

Warnings have come from large mobile operators that revenue lost through MTR reductions will be recouped through reductions in handset subsidies and higher retail prices, leading to low income, predominantly pre-pay, customers losing out. To date, these effects have not been widely observed. The number of mobile subscriptions continues to rise, and although the number of pre-pay subscriptions did record a fall for the first time in 2008, the number of overall subscriptions rose, suggesting a general move by consumers away from pre-pay towards contract mobile packages².

Similarly, no obvious widespread reduction in handset subsidies has taken place in recent years. An increase in average contract lengths has taken place, suggesting a drive by mobile operators to spread the recovery of subsidies over the course of longer mobile deals. However, this has been off-set to some extent by the introduction of one month SIM-only contracts, which now account for 24 per cent of contracts sold³.

Despite a lack of obvious detrimental consumer impact to date, we do urge caution in assuming that further reductions in termination rates do not have the potential to impact negatively on consumers.

We are entering a period in which economic circumstances for mobile network operators are likely to be more challenging than in recent years. Operators will be required to balance a slowing of growth in revenue from mobile services⁴ and the impact of the wider economic climate with the need to invest in infrastructure and newly released spectrum bands. This may make absorbing MTR reductions more challenging than has been the case in the past. These more stringent economic circumstances should be taken into account when looking at past company behaviour as a guide to the likely outcomes of termination rate reductions in future.

² Ofcom, The Communications Market Report (2009) p.233 <http://bit.ly/ddcHMv>

³ *Ibid.* p.217

⁴ Total mobile service revenues grew by 2.2% in 2008, compared to the annual average of 9.6% growth over the previous five years and 15.5% over the previous ten years. (*Ibid.* p.199)

Meeting the needs of vulnerable and disadvantaged consumers

As discussed above, to date we have not been aware of falling termination rates having a widespread negative impact on vulnerable and disadvantaged consumers. However, we encourage Ofcom to ensure that the needs of vulnerable, disadvantaged and low income consumers are taken into account when formulating policy around MTRs.

Consumer Focus supports the reduction in MTRs that is being proposed, but urges Ofcom to remain alert to the potential for mobile operators to introduce policies to recoup lost revenue that penalise low income or low use mobile consumers. Such policies could include increases in the cost of lower priced contracts and pre-pay charges, or the reintroduction of top-up credit expiry dates. For those consumers on the lowest incomes, this could lead to mobile ownership becoming unaffordable, excluding some of the most vulnerable consumers from mobile communications. While such policies have not been observed to date, they remain a possible reaction to further reductions in MTRs, particularly as rates reach low levels closer to 2014/15.

When monitoring the market for signs of negative impacts on vulnerable and disadvantaged consumers, we would expect Ofcom to be aware of the tendency among mobile operators to follow similar behaviour and avoid differentiating themselves when making changes to pricing policies that are disadvantageous to consumers. A lack of differentiation between mobile operators has seen similar policies being adopted around some aspects of pricing, such as the levying of additional charges for itemised bills and calls to customer service helplines. In the context of the merger of Orange and T-Mobile, which will create a single mobile operator with a 37 per cent market share, there is a risk that the adoption by this company or one of its major rivals of an approach that is detrimental to disadvantaged and vulnerable consumers will legitimise its implementation by other providers.

Further proposals for consultation

Three further proposals made by Ofcom are considered here: the requirement for 'fair and reasonable' MTRs to be levied by smaller mobile providers, the move from LRIC+ to pure LRIC charging and action to address MTR 'flip-flopping' by mobile operators.

Regarding the MTR regime that is applied to smaller mobile providers, Consumer Focus is supportive of the approach Ofcom has proposed. Following the recommendations of the European Commission that all termination charges should be symmetrical, our view is that the proposal for smaller providers to set 'fair and reasonable' MTRs put forward by Ofcom is appropriate to be in keeping with the Commission's view. The consultation paper notes that the absence of a 'fair and reasonable' requirement on smaller mobile providers setting their own MTRs led to a number of disputes with large providers, so the action that Ofcom has proposed to address this is a positive step. We would be keen for Ofcom to provide further information on the action that will be taken where significant diversions from rates that are considered fair and reasonable take place, including the compliance incentives and enforcement mechanisms that may be used.

In the absence of substantive reasons for not doing so, Ofcom proposes to adopt pure LRIC instead of LRIC+, to comply with EC recommendations. On the basis that Consumer Focus is supportive of an approach that is in keeping with our overall desire to see lower termination rates, and given a lack of any significant reasons for not complying with the EC's recommendation, we do not have any concrete objections to Ofcom's proposed switch from LRIC+ to pure LRIC. We note that the move is likely to have some positive effects on competition, in terms of the lower costs that will be levied.

Consumer Focus welcomes Ofcom taking action on the size and frequency of changes made by mobile providers to their MTRs. 'Flip-flopping' creates upward pressure on retail

prices, as providers cover themselves against spikes in termination rates, resulting in higher costs for consumers. The practice has arisen through a desire to gain extra revenue by exploiting a loophole in the current MTR regime, and it is appropriate that Ofcom addresses this practice.

Four options, including a counterfactual, are presented for placing limits on the changes that communications providers can make to their rates. Of these, Ofcom recommends option 2, under which a 20 per cent restriction would be imposed on rate changes. The evidence presented by Ofcom demonstrates that mobile providers have made little or no use of the facility, within the current MTR regime, to apply time-of-day flexibility of MTRs to incentivise efficient network use. It is therefore not completely clear why, given that providers' only significant use for adjusting rates has been to practice flip-flopping, why an element of flexibility is being retained within the system. Have alternative ways of incentivising efficient network use been considered?

Based on the evidence presented by Ofcom, we understand that option 2 is likely to address the problems caused by flip-flopping that have been identified, but we are not persuaded by Ofcom's argument that there is a need to retain flexibility in the system. We would therefore be more supportive of option 3, which allows mobile providers to use varied rates within a fixed ratio of rates.

Consumer information

Consumer Focus is working to ensure that the consumer voice is heard in debates around the future of mobile termination rates. There is a lack of information and transparency around the issue of MTRs, leading to gaps in consumers' knowledge and understanding of how termination rates impact on bills paid by phone users. Acknowledging the complexity of call termination regimes and challenges of communicating straightforward, accurate information to consumers, we believe that information on MTRs should be readily available to those consumers who want it. It is important that consumers are able to make use of a full range of tools in order to choose their mobile phone package with confidence.

At the same time, we urge Ofcom to be aware of the need to avoid increasing complexity in the mobile market through future changes to the termination rate regime. Many consumers already struggle with the sheer volume and complexity of tariffs to choose from when deciding on a mobile package⁵. A consumer-focused MTR policy should take account of its impact on the complexity that currently exists in the mobile sector.

Consumer workshop

Understanding the full impact of Ofcom's proposals around mobile call termination can be challenging, particularly for stakeholders who do not have the resources to conduct a detailed economic analysis of the planned regulation. Consumer Focus notes that, during the current consultation period, Ofcom held a workshop aimed at smaller mobile providers, to provide help with their responses to this consultation, in recognition of the fact that many do not have a dedicated regulatory team.

We would suggest that, given the likelihood that consumer groups and other stakeholders representing particular groups of mobile phone users also find it challenging to provide an in-depth response to this consultation, Ofcom should in future consider a holding similar workshop for consumer stakeholders. Fostering a better understanding of the full impact of MTRs on consumers would doubtless lead to a stronger consumer voice and a better functioning market overall.

⁵ Mobile price comparison site billmonitor, the only mobile comparison site accredited by Ofcom, currently compares 6,695,564 different mobile phone deals. www.billmonitor.com

Contact: Nick Hutton, Senior Policy Advocate
Tel: 020 7799 7963
Email: nick.hutton@consumerfocus.org.uk

www.consumerfocus.org.uk

Copyright: Consumer Focus

Published: June 2010

If you require this publication in Braille, large print or on audio CD please contact us.

For the deaf, hard of hearing or speech impaired, contact Consumer Focus via Text Relay:

From a textphone, call 18001 020 7799 7900

From a telephone, call 18002 020 7799 7900

Consumer Focus

4th Floor
Artillery House
Artillery Row
London SW1P 1RT

Tel: 020 7799 7900

Fax: 020 7799 7901

Media Team: 020 7799 8004 / 8005 / 8006