



WILMER CUTLER PICKERING LLP

European Communications Law Update

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UK Strategic Review of Telecommunications

On April 28, 2004, the United Kingdom's Office of Communications ("Ofcom") issued its phase 1 "consultation" on its strategic review of telecommunications in the UK (the "Review"). Ofcom is the regulatory body, established in December 2003, that combined the UK's five separate telecommunications and communications-related regulatory agencies into one.

The Review is part of the vast overhaul of European telecommunications law that began with the EU's adoption of the "2003 EU Communications Regulatory Framework" ("EU Framework"). The EU Framework, comprised of numerous directives concerning specific telecommunications issues, was transposed into UK law by the passage of the "UK Communications Act 2003" (the "Act"). In addition to the inherited powers and statutory duties of the now extinct Broadcasting Standards Commission, Independent Television Commission, Radio Authority, Radiocommunications Agency and the Office of Telecommunications ("Ofjel"), the Act established more than one hundred new functions and duties for Ofcom. The Review is Ofcom's first major step in implementing the telecommunications policies contained in and fulfilling the statutory duties required by the Act.

This update, adapted from a similar update published by our London office, summarizes the contents of the Review and considers its implications for participants in the UK telecom market. According to the first Chairman of Ofcom, "*The Review will enable us to set out a strategic agenda for our activities in relation to [telecommunications], and will create a new settlement between the regulator, the companies we regulate and the citizen-consumer.*"

The Review begins by asking five high level questions:

1. In relation to the interests of citizen-consumers, what are the key attributes of a well-functioning telecommunications market?
2. Where can effective and sustainable competition be achieved in the UK telecommunications market?
3. Is there any room for a significant reduction in regulation, or is the market power of incumbents too entrenched?

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4. How can Ofcom incentivize efficient and timely investment in next generation networks?
5. At varying times since 1984, the case has been made for structural or operational separation of BT (British Telecom), or the delivery of full functional equivalence. Are these still relevant questions?

These five questions are followed by 21 additional ones addressing specific issues. At this stage Ofcom has not considered what it may or may not do. It has only set out the background and invited commenters to speculate on how the telecommunications market will develop. Nevertheless, our senior London telecom lawyers see possible outcomes in Ofcom's questions and its description of certain issues:

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- **Broadband more Important than Voice.** At several points in the Review, Ofcom notes that many of the original aims of regulation (*e.g.*, availability, price, service) have been achieved for voice telephony. Ofcom also recognizes that inter-modal competition from wireless and VoIP will increasingly constrain BT's market power even where it continues to provide access lines for voice telephony. These comments may indicate withdrawal from voice regulation. Conversely, the market performance measures set out in Annex H of the Review indicate that Ofcom considers that for broadband the regime has delivered a relatively low level of competition and therefore of price, availability and service choice. Further, in the near term, Ofcom is

concerned about how to stimulate investment in "broader"-band, next generation technologies such as fiber-to-the-curb or fiber-to-the-home.

- **Regulation Important for Businesses as well as Consumers.** Ofcom has identified that certain segments of the market (business users) have experienced less benefit from competition than others and that Ofcom will continue to address those markets, even if regulation is rolled back in consumer markets. Given the greater buying power of business customers and the focus on these customers by alternative network operators, this may mark a surprising shift from the current assumption that business markets generally require less regulation.
- **Less Wireless Regulation.** Ofcom cites the wireless market as a market where competition has delivered appropriate results. It seems likely that, with the exception of termination charges, further regulation will not be imposed and indeed may be withdrawn.
- **Network Competition Rather than Services Competition.** Both the executive summary and Annex G of the Review suggest that Ofcom may shift its policies away from services-based competition to network-(or facilities) based competition. The Review states: "[F]ixed [telecommunications] regulation has been characterized by tradeoffs, in particular the trade-off between promoting services and network based competition . . . During the mid-1990s, the balance was firmly tilted in [favor] of infrastructure providers, but was interrupted by legal and financial developments of the late 1990s . . . because infrastructure competition has been much more widespread in [wireless telecommunications] the sector has not faced the same degree of regulatory intervention." A return to the network-based policies of

the mid-1990s, in an effort to boost investment in broadband, may positively affect BT, cable companies and network operators. Conversely, it may negatively affect recent non-network based new entrants.

- **Long-term Innovation and Investment Incentives Rather than Short-term Consumer Benefits?** Ofcom notes that technology is driving changes in networks and services that deliver dynamic innovation benefits, but also notes the significant capital expenditure required. Ofcom further notes that retail price controls, or resale-based regulatory intervention, may negatively impact investment decisions by constraining the returns available to those investing in infrastructure. This may indicate the lifting of certain obligations on BT.
- **Regulation at Fewer Intermediate Levels?** Markets such as broadband access have a number of intermediate products: e.g., copper loops, wholesale access delivered over IP, as well as retail products. Ofcom raises the question whether it is desirable and sustainable to regulate at all levels, as a regulatory mandated margin to allow competition at all levels may lead to persistently high retail prices. With Ofcom currently considering margin squeeze issues between various intermediate products, any change of policy in this area is likely to adversely affect those currently purchasing intermediate products from which regulation is removed.
- **BT Separation - a Red Herring?** The UK press has made much of fundamental question five. The *Financial Times* characterized this question as a call for the structural

separation of BT. However, much of the Review asks questions which in fact imply lifting some regulation currently imposed on BT. While the question raised is described as “fundamental,” Ofcom does not discuss this option further or indeed even ask specific questions about the advantages or disadvantages of such a move. In light of other public comments from Ofcom, together with its lack of power to impose such a remedy, it seems that the question is posed to ensure that the issue is viewed as being considered, rather than as a serious option.

- **Additional Price Transparency Obligations on All Operators?** While much of the Review looks at maximizing “consumer” benefits, Ofcom indicates that it may take action to force more price transparency in the interests of “citizens,” as even competitive markets seem to produce confusion among consumers. This may impose additional regulatory burdens on all operators.

Phase 1 of the Review examines the current position and prospects for the sector. Phase 2, expected in the Fall, will identify and assess Ofcom’s options and phase 3, expected towards the end of 2004, will assess these options and set out Ofcom’s plan of action. This Review is one of three major reviews Ofcom is undertaking in its first year. The others are of public service broadcasting and spectrum.

For more information about the Review and/or assistance in preparing your comments, please contact:

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