



OFCOM STRATEGIC REVIEW OF
TELECOMMUNICATIONS

COLT TELECOMMUNICATIONS

Response to the consultation on undertakings offered by
British Telecommunications plc in lieu of a reference
under Part 4 of the Enterprise Act 2002

12th August 2005

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I Executive Summary

COLT Telecommunications welcomes the opportunity to respond to this consultation. We would also like to offer our support and congratulations to Ofcom for a remarkable achievement in combining strategic thinking with detailed operational measures during the very complex procedure of the Strategic Review, and an intensive consultation process.

COLT recognises the unique nature of the consultation that has gone on during the Strategic Review process over the last year, and is pleased at the progress that has been made by all participants during the Review. COLT supports the adoption of the undertakings approach and encourages the idea of continued assessment of the undertakings as a work in progress.

Overall COLT believes the presented undertakings are a step in the right direction and have the potential to bring about regulatory change. However, COLT is also concerned that various omissions and weaknesses apparent in the undertakings create gaps between the intentions of the Ofcom announcements from June 23rd 2005 and the actual settlement proposed.¹

It is COLT's view that an effective settlement between Ofcom would fully reflect a minimum set of overall goals such as:

- There should be no weakening from the principle of input equivalence in 21 CN; input equivalence is insufficiently clearly defined in the undertakings;
- Premature deregulation should be avoided, particularly in sub-national geographic markets;
- There must be appropriate follow-up from the undertakings: Ofcom must not neglect its ongoing role as a regulator especially in areas where the undertakings look weak and where Ofcom's existing powers are quite strong (for example, compensation for the move to 21 CN and prices for 21 CN products to be based on efficient cost);

¹ Two examples of areas where the detailed wording of the undertaking does not fully match the original aims of the TSR are in relation to outcome equivalence and the Equality of Access Board. We had understood from the Ofcom statement of 23rd June that the undertakings would contain explicit commitments on outcome equivalence. Ofcom said: "BT's undertakings give commitments to resolve outstanding issues in relation to each of these products to achieve 'equivalence of outcome'". In fact, the undertakings given no such commitment -- they do not even mention outcome equivalence. In relation to the Equality of Access Board, Ofcom said that it would have "powers and teeth". This is at odds with the provisions of the undertakings, which make it clear that "The role of the EAB is a general one of monitoring, reporting and advising BT..."

- The implementation and effectiveness of the undertakings must be audited;
- Sufficient commitments have to be made regarding outcome equivalence and there must be demonstrable progress in achieving it;
- A formal mechanism for appointments to the BT Equality of Access Board must involve industry;
- BT must meet the cost (or at least the majority of the cost) of implementing the undertakings, as promised by Ofcom.
- BT wholesale must work effectively

COLT recommends that Ofcom - in co-operation with BT and industry - devises Codes of Practice that are agreed by all industry players and which facilitate the proper application of the settlement at a practical level.

In order to achieve this, COLT believes that it will be necessary to change some of the wording in the draft undertakings as they stand today. However, we do not believe that many of these changes will be fundamental as these changes in the wording are intended to reflect underlying intent more accurately.

II Introduction

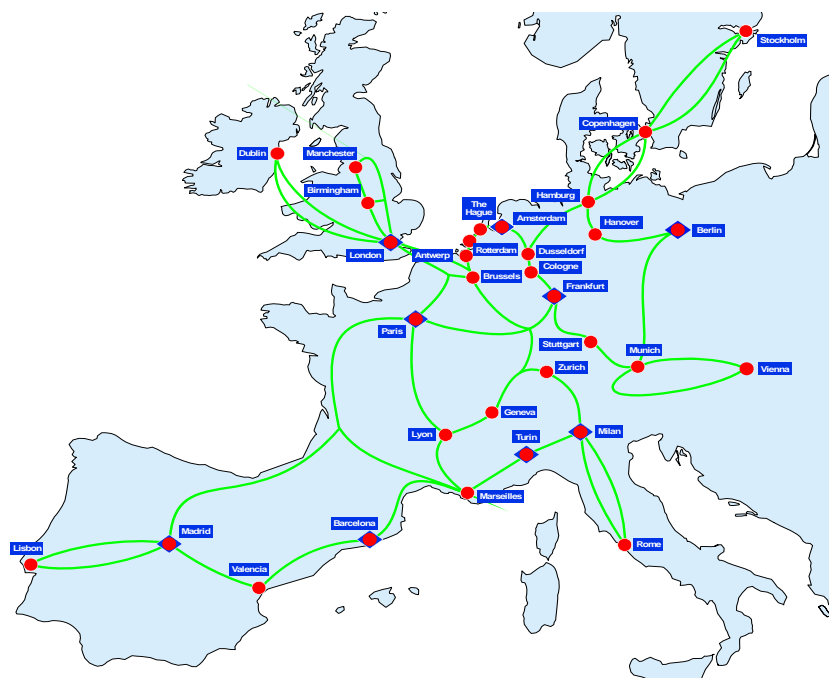
II.1 About COLT

COLT was established in 1992 with the assistance of Fidelity Investments, one of the world's largest privately-held mutual fund and investment management companies, with assets under custody of circa.\$1.8 trillion. Fidelity remains COLT's majority shareholder today.

COLT built its first 15km of London fibre network in 1993 and over the following three years expanded its London network and offered services in major European cities, with local sales, service and support capabilities. From 1997-2001, COLT raised over £2bn of new capital to fund the construction of a 15,000km pan-European backbone network

COLT is unusual in having followed a clear strategic path to the development of its network. First came the dense, last-mile fibre network in London, then in the other first-tier European cities. Once the local networks were deployed, all the COLT metro networks were connected over a wholly-owned backbone. COLT has predominantly built its own network and infrastructure. Only in a very few cases is the COLT backbone network reliant on elements leased from other carriers. In total, COLT has invested almost £3bn in creating its pan-European local and long-distance network.

COLT's European network



COLT has also been at the forefront of regulatory developments across Europe. COLT's founding President and CEO, Paul Chisholm, was a founder of the UK OLO Group and its former UK Managing Director, Simon Vye, was President of the UK Competitive Telecommunications Association. COLT has been among the leaders of the first wave of altnets to enter the markets of continental Europe as they liberalised. Today COLT is a leading pan-European provider of business communications services offering unrivalled end-to-end network security, reliability and service. COLT has a strong customer base with more than 52,000 customers - 42,000 of which are in the small/medium enterprise sector and 10,000 of which are in the corporate customer sector where it is a leader in a number of industry sectors, particularly the professional services and the financial services segments. The company owns an integrated 20,000 kilometre network that directly connects 32 major cities in 13 countries augmented with a further 42 points of presence across Europe and 11 Data Solution Centres.

A new CEO, Jean-Yves Charlier, was appointed in September 2004 and the senior management team was further strengthened with a number of other key appointments.

Jean-Yves Charlier has put in place an enhanced set of strategic initiatives designed to re-establish COLT as an innovator and as one of the top three players in each of the metropolitan markets in which it operates across Europe, taking the company forward into its next phase of profitable growth.

II.2

Overview

Reference to the Competition Commission or settlement?

The settlement seems to go in the right direction; however, it is difficult to predict whether it will work: the proof of its success will only really be if we create a fairer environment in which it is conceivable that altnets might gain market share in the UK, leading to increased profitability for altnets in the future. This is important to ensure that consumers benefit from a competitive market.

Overall COLT cautiously welcomes the undertakings offered by BT but believes that certain omissions and weaknesses (in form and content) apparent in the undertakings create gaps between the intentions of the Ofcom announcements from June 23rd 2005 and the actual settlement proposed.

COLT believes that it would be expedient for Ofcom to accept the undertakings rather than make a reference to the Competition Commission using its Enterprise Act powers. We believe that a reference would create a formidable administrative burden on the industry and result in operational, legal and financial uncertainty for all players in the medium term. As a result, we think that an approach based on undertakings in lieu of a reference is preferable.

An improved regulatory framework

The principles of the settlement were negotiated by BT in conjunction with Ofcom, combining the strategic, commercial and technical aspects of an improved regulatory framework.

Over time, it is expected that the wording of the proposed undertakings will be interpreted by legal experts who have a different regard for the commercial implications and strategic intentions which lie behind the undertakings, and who are expected to interpret the letter of these undertakings, without always knowing what the spirit of it might have been.

COLT is concerned that due to the ambiguous wording of some sections the undertakings could be interpreted and consequently implemented in ways that are counter-intuitive to the original spirit of the undertaking. In particular, we are concerned that although the reasonably generic wording could well be understood by the people who agreed it, a third party to these negotiations reading the undertakings for the first time in two years time may not appreciate what they were originally intended to mean.

Therefore COLT recommends that Ofcom - in co-operation with BT and industry - devises Codes of Practice that are agreed by all industry players and facilitate the proper application of the settlement.

COLT has raised its concerns regarding the present undertakings at several occasions through UKCTA and directly with Ofcom and BT, in various levels of detail. The response to this consultation will however mainly focus on the core problems and shortcomings of the proposed undertakings. A more detailed analysis of the undertaking itself can be found in Annex A to this document.

Ofcom's objectives for regulation

This new approach to regulation by Ofcom is forward-looking in its objectives. These objectives aim to generate better services at lower cost and innovations to benefit consumers through competition. COLT supports both the approach and the set objectives.

In its statement on 23rd June on the aims of the new regulatory approach, Ofcom foresaw the provision of a certain amount of regulatory certainty for altnets and investors, in order to enable innovation and investment and re-focus regulation. Additionally, there will be remedies for anti-competitive behaviour and the development of a market which delivers equivalence within specific timescales. This is extremely encouraging. As Ofcom has recognised, effective regulation of the telecommunications market needs to encourage competition and be forward-looking.

The introduction of a new Access Services Division (hereafter ASD) is particularly welcome. Not all operators are the same and there is a need for a matrix of wholesale products and services in communications markets. COLT's focus is the business market, and this engenders other needs than companies which are focused on the residential market. COLT was initially concerned that ASD would only contain LLU and not involve the other elements such as, WES and PPCs, which are important for continued progress of the telecoms industry and for ensuring that businesses benefit from the choice and innovation needed for the continued growth of the economy as a whole. COLT believed that it was necessary for ASD to have a broader scope and we are delighted that this has been recognised by Ofcom. Notwithstanding our comments about the detail and implementation of the settlement, COLT therefore welcomes the establishment of the ASD. COLT believes that ASD contains mainly the right products, and would not support any move to narrow its scope. Ideally, COLT would like to see Datastream included in the ASD.

Outcome of the Strategic Review

Concerns still remain for COLT regarding the outcome of the Strategic Review:

Despite the elements mentioned earlier, regarding re-focusing regulation and improved confidence on the market, the settlement which results from the Strategic Review delivers, on balance, only incremental changes. It is not ultimately a full overhaul of the regulatory framework. This does not mean that it is flawed, but it

does have important implications for Ofcom's ongoing role and ongoing sector-specific regulation.

The proposed TSR settlement falls short of the full structural separation supported by many commentators and it does not incorporate the hybrid structural/organisational approaches recommended by COLT (and UKCTA) at the previous consultation stage. This does not devalue Ofcom's and BT's work in getting this far -- on the contrary, we recognise the very real steps that the undertakings represent. However, this does mean that extreme care will be needed when considering Ofcom's forward-looking role. A strategic shift would perhaps be more likely to generate an environment in which deregulation -- or refocusing of regulation -- might then come to be justified by market circumstances. COLT does not believe that the current settlement will create an environment which can justify anything less than a completely rigorous application of market review principles to any proposed deregulation.

The settlement seems to go in the right direction; however, it will only be a success if altnets gain market share in the UK, and if we see increased profitability for altnets in the future. This will ultimately result from correct implementation and thorough monitoring of the undertakings, and full participation from all sides. (See our point below on the monitoring of the settlement).

A particularly serious concern is that, we do not at present have full clarity over how this implementation will be carried out and assessed. One element of concern to COLT with regards to this is equivalence - it remains to be seen whether implementation can fulfil all the promises made in Ofcom's announcement on 23rd June 2005. COLT understands that Ofcom intends to conduct periodic reviews of the implementation and effectiveness of the undertakings and fully supports that. COLT would welcome an opportunity to be involved in developing the process, which must be fully transparent. Additionally, it should be conducted on a regular basis, certainly for the first years of the implementation of the undertakings, to ensure swift reactions from Ofcom in case this implementation is deemed to be inaccurate or not performed in due time.

The Access Services Division

With regards to equivalence, Ofcom and independent auditors must have a clear system of audit for ASD. This must include ad hoc, unannounced audits and/or checks.

COLT supports Ofcom's request that ASD be required, through a set of formal rules on governance and separation, to support all providers' retail activities (including those of BT Retail) on a precisely equivalent basis. This is termed "Equivalence of Input" (hereafter EoI) by Ofcom. Equivalence of Input means that all providers will benefit from the same products, prices, processes and development opportunities.

This has been sadly lacking so far, and this is a welcome improvement. However, we remain concerned about some of the details relating to Equivalence of Input.

As COLT believes BT intends, ASD must be set up as quickly and simply as possible, so that assets and products can be moved into it easily. The transfer of assets is, of itself, a very straightforward process. We appreciate that the transfer of staff is less straightforward, but BT has all the processes in place to make this a reasonably smooth transition, that should be dealt with as speedily as possible. Moreover, BT should have the incentive of proving its goodwill to the market and to Ofcom.

Risk Assessment

As part of its assessment of the draft undertakings, COLT has identified certain risks which could threaten the effectiveness of the settlement if the undertakings were to be accepted. These risk factors do not necessarily address the question of whether the undertakings should be accepted or not. Many of them are about possible unintended consequences of the undertakings: they are not intended as a list of likely consequences or as a critique of the settlement. COLT would expect Ofcom to prevent unintended consequences by monitoring (and, if necessary, enforcing) the undertakings and by using its sector-specific and competition law powers. This would include instances such as:

- a. The need to divert resources to comply with the undertakings may be used as a rationale for BT to fail to correct existing problems with its regulated product set or to fail adequately to respond to, for example, new statements of requirements.
- b. If the undertakings are accepted, this may stimulate BT to request an accelerated programme of deregulation in other markets in a manner which is not warranted; BT may also use the settlements to argue that Ofcom should be less willing to use its sector-specific and Competition Act powers.
- c. There may be other less foreseeable consequences of the proposed settlement. For example, BT may use the argument that, with a more arm's length relationship between the Access Services Division and its downstream businesses, it is open to the ASD to offer volume discounts to its largest customers. Its largest customer would obviously be its own downstream business and the resulting situation would once more disadvantage a level playing-field.
- d. Unforeseen circumstances may arise which are not covered by the drafting of the settlement and this may mean that BT could circumvent it. For example, the definition of equivalence of inputs could perhaps be strengthened and the commitments given in relation to 21 CN contain extensive carveouts. Equivalence of Inputs appears only to apply to certain specified products which are downstream of the relevant SMP products (rather than all downstream products) and this may mean that it is less effective as a tool for fostering competition than at first it would appear.

- e. The process for Ofcom to enforce the undertakings through the courts is considerably more complicated than an exercise of Ofcom's normal enforcement powers. For a third party, it is more difficult, as BT has a statutory defence that they "took all reasonable steps and exercised all due diligence to avoid contravening the undertaking". Difficulties in enforcement may therefore mean that breaches may not result in enforcement action, particularly where they appear comparatively minor, and yet their impact is far from negligible.

Whilst COLT supports the majority of the work on the settlement, there nevertheless remain a number of specific areas of concern regarding the Strategic Review. These are described in the next section.

III COLT concerns

COLT's concerns can be summarised under the following headings:

III.1 Equivalence

III.2 Access Services

III.3 The Equality of Access Board

III.4 21 CN: the development and rollout of the 21CN, and how it relates to the settlement.

III.5 Cultural change within BT

COLT feels there is a lack of clarity and content surrounding these areas, and would like to set out why it considers this to be the case:

III.1 Equivalence of Input

COLT wholeheartedly welcomes the recognition of the principle of Equivalence of Input. We have concern about how it might work in practice, however. Some of these concerns relate to 21 CN and are dealt with below. Otherwise, they are explained in more detail in our comments on the draft undertakings which are annexed in section 4.

We had also understood that Equivalence of Inputs would mean that all products downstream from the wholesale SMP product would need to use that product as an input. In fact, that only seems to be true for a very limited set of downstream products. An example of this would be in relation to private networks. The undertakings as drafted required BT to use WES as an Eol input to "retail Ethernet-based local area network extension services". This would mean that BT need not use WES as an input to, for example, corporate private networks. From our perspective, this undermines the principle of Equivalence of Inputs; we would expect an upstream SMP product to which Eol applies to be the input for all downstream BT products.

a) How the settlement will be monitored and whether the provisions made for the establishment of the EAB are sufficient to safeguard their independence.

We understand from talks with Ofcom that there will be quarterly reviews run by Ofcom. It is important is that these reviews are comprehensive and transparent; they should not only deal with the implementation of the undertakings but should also look at whether the new regime is fundamentally effective. COLT and most other players feel that we will need to submit our requirements to Ofcom regarding this in more

detail. COLT also welcomes BT's offer to hold monthly progress-update meetings with selected industry representatives.

In addition, COLT is happy to engage directly or through UKCTA in dialogue with the Investigations Unit at Ofcom regarding the enforcement procedure.

With regard to the implementation of the settlement, Ofcom and independent auditors must have a clear system to audit BT's compliance with its obligations under the undertaking. This must include ad hoc, unannounced audits and/or checks.

The provisions in the draft undertakings for an audit of the summarised version of the EAB annual report do not go far enough: since they apply only to the summary of the EAB's annual report there is no indication of how substantial the audit will be. Consequently, the provisions need depth.

Additionally, there is a need to draw up a set of indicators for use in monitoring the settlement's success, ideally to establish terms of reference for the ASD and the performance scorecard for ASD staff.

It is important that the success of the settlement is monitored in the broadest terms. This means that BT's performance in implementing the undertakings need to be reviewed. An important part of this is establishing Key Performance Indicators (KPIs), and we look to Ofcom to do this. But a wider exercise is also needed to ensure that the TSR settlement creates an environment in which all competitors can compete on a fair basis. This is something which we feel is lacking from the current framework and which we welcome the opportunity to work with Ofcom on in the future.

Industry should be heavily involved in helping to devise an objective performance scorecard for ASD, since our combined industry experience is ideally suited to draw on best practice.

Finally we urge Ofcom to foresee a process of collecting aggregated details of breaches by BT as there is concern in industry about the cumulative effect of minor breaches.

A detailed proposal will be submitted later.

b) Outcome Equivalence

The existing commitments in the undertakings, which were designed to help move to equivalence of outcomes, do not fully specify what they are intended to achieve. Herewith is our definition of outcomes, in order to help the debate progress:

"Equivalence of Outcomes" means that a product or service is provided by BT ASD or BT Upstream (as the case may be) to all Communications Providers (including other division of BT) in a way which:

- (i) where reasonably practicable, is Equivalence of Inputs; and
- (ii) to the extent that it is not reasonably practicable that the product or service be provided on the basis set out at (i) above, produces an outcome which is as close as possible to provision on the basis set out at (i) above at a reasonable and efficiently-incurred cost and in any event delivers such an outcome that any differences from provision on the basis set out at (i) above are not material.

c) Deregulation

Ofcom has agreed that the settlement alone will not justify deregulation and COLT fully supports Ofcom's position on this. The settlement might put in place a framework which would create an environment in which deregulation would eventually be appropriate -- again, we believe that this is correct. COLT recommends that Ofcom follows a cautious and considered approach to any deregulation, and asks that any deregulatory measures be considered on their own merits. We reiterate the need for deregulation to be carefully considered but also to be carried out in logical stages in order to protect those who have invested in their own access networks.

The market review process mandated by the 2003 European framework is designed specifically to generate an objective, transparent means of achieving fair, proportionate regulation. While market developments deriving from the TSR settlement may generate circumstances relevant to a market review, we would not expect the settlement *of itself* to be a factor in the market review, e.g. SMP definitions and declarations will not change as a result of the TSR.

One particular form of deregulation which would concern COLT would be the deregulation of sub-national geographic markets: as has been mentioned in earlier consultation with industry, the creation of de-regulated sub-national geographies carries the danger of creating geographic "black holes" without regulation or competition. Defining markets on a geographic and per-service basis is thoroughly complex. In defining markets on a sub-national basis, there is a danger of unintended consequences.

This is particularly important because it carries two risks:

- BT could gain the power to crush any competition based on alternative networks by pricing below cost in limited geographies – a rational strategy which it could carry out at low cost because of the its

competitors' limited network footprint. This could still happen despite the existence of the ASD.

- Secondly, if BT can effectively engineer geographic “black holes”, it could destroy the ability for any player to compete for opportunities which require genuinely national coverage.

There is always the possibility of re-regulating a market, should deregulation fail. COLT questions the viability and practicality of re-regulation since it is not ideal, and would cause upheaval and uncertainty for altnets. COLT's view is that, before deregulation can even be considered, there must be proper upstream products from BT on an equivalent basis, and a properly functioning downstream market at the right level. A series of vertically integrated providers is not sufficient; a healthy wholesale sector must exist and BT must have lost enough market share for it to be clear that upstream solutions are working.

III.2

The Access Services Division (ASD)

a) The external relationships of BT ASD:

COLT understands that BT has committed to the fact that ASD will not become vertically integrated. However, the undertakings do not actually restrict the ASD from selling directly to end users and thereby creating a vertically integrated operator. Therefore COLT is concerned that ASD could potentially re-gain the benefits of vertical integration and circumvent COLT and other suppliers by selling directly to end-users. Industry has indicated that it is particularly concerned about a downstream unit within ASD gaining access to confidential information. The settlement as drafted does not contain any Chinese wall requirements within the ASD.

Although BT has made verbal assurances to COLT and industry that it does not intend to create this vertically integrated operator within ASD, these do merely remain informal assurances at present and we assume that any decision in this regard will ultimately rest with the executive management of BT. This means that if there is a competitive advantage to be gained by creating a downstream services unit within ASD, it will happen.

Ofcom has suggested that it would consider the settlement to have failed if ASD became a vertically integrated entity in its own right. This is clearly in no sense a binding statement by Ofcom, but is useful as an indication of what is intended.

COLT therefore proposes that this informal understanding should be set out in writing in the final settlement.

b) Internal organisation of remaining BT units

BT does not explicitly state where BT's wholesale assets will sit – it is not possible to assume these will be ring-fenced. COLT therefore requests BT wholesale assets are ring-fenced and that when transactions between BTWS and BTS are concerned, Chinese walls are put in place between product teams and the teams running the assets. It is important that the head of BTWS and BTS has enough independence to help carry out the provisions of the undertakings.

There has been no detail provided by BT over how it will ensure BTS product development is not prioritised over BTWS product development, or over how product development requests from BTR will be dealt with by BTWS. COLT therefore requests a detailed proposal on BTWS/BTS product development processes and suggests that all product development proposals in BTWS are overseen by the EAB.

As regards BT Retail, the proposed organisational change cannot be complete if BT's relationship with BTR is not made sufficiently distinct.

III.3

The Equality of Access Board (EAB):

Ofcom announced on June 23 2005 that the EAB will have extensive powers to seek access to information from wherever in BT Group plc it deems necessary to do its work. The undertakings, however, use very vague terms to describe the role and powers of the EAB (e.g. "shall review, shall have the right to review, may review, ..."). Additionally it appears that this body does not have the requisite 'teeth' and prescribed powers to ensure full compliance. Therefore, COLT recommends that the EAB remit explicitly include policing powers. COLT suggests also that an obligation be put on BT to react to any recommendation from the EAB.

It is very important to establish what the Board really represents, what its purpose ultimately is, and what powers it is granted to enforce BT's obligations.

COLT is concerned that the so-called "independent members" are appointed by BT, since BT is merely obliged to do so "in consultation" with Ofcom. This does not give confidence about the selection and appointment procedure of the independent members of the EAB, since Ofcom has no actual veto against unsuitable candidates. We welcome a verbal offer made by BT to industry to be closely involved in the selection of the EAB independent members. However, an informal offer is not really sufficient in this instance, and should be formalised.

COLT recommends that the correct term of office for EAB members, should be around three to five years in order to give them sufficient time to effect real change and to deliver on their objectives. These terms of office should include rolling terms so that all members don't change at the same time.

COLT recommends that in order to ensure the independence of the EAB members, altnets should agree to pay part or all of the salary of at least one or more EAB members. A body representing the alternative sector should have the right to appoint and remove those independent members. Those independent members would be contracted directly to the alternative representative body as well as to BT. Their contract will contain the necessary provisions to ensure that they don't disclose confidential information to anyone they shouldn't -- but they will have a clear dual duty and that will help them to act fairly.

III.4 21CN:

The TSR undertakings, when cross referred with the work Ofcom is doing on 21 CN, may well have some unintended unfortunate consequences. COLT appreciates that a separate consultation is underway on 21 CN and will comment fully on 21 CN in that arena. Nonetheless, there are 21 CN issues which stem directly from the TSR, or which impact upon it, and we feel it is important to comment on them briefly here:

Enterprise Act vs. Sector Specific regulation

The offered Undertakings are a compromise between Ofcom and BT under the auspices of the Enterprise Act.

Some of the 21 CN-related provisions stipulated in the undertakings deviate from current Ofcom sector specific powers, (e.g. compensation and charges based on effective design) which potentially create disadvantages for altnets compared to sector specific regulations.

Despite the arrangements made in the undertakings, Ofcom has an obligation to make full use of its remaining sector specific powers to prevent a distortion of the competitive landscape

Not reasonably practicable

Section 11 of the proposed undertakings was intended to set out clear principles for the design, procurement and build of BT's next generation 21st Century Network. Ofcom stated in its press announcement on 23rd June that 'these principles will help ensure that other providers who will depend upon interconnection with BT's 21CN do not suffer competitive disadvantage.'

COLT however believes that the proposed undertaking does not live up to this promise as some of those principles do not apply when this is 'not reasonably practicable'.

The vagueness of the term 'not reasonably practicable' creates a significant carveout that has the potential to undermine the spirit of the settlement with regards to 21 CN principles in particular where it is stated that:

- BT has to ensure that the 21CN design supports competition, by allowing other operators unbundled access to key bottlenecks
- BT has to design the 21CN in a way which will support Equivalence of Input.
- BT's charges have to reflect a network that is efficiently designed for the above purposes.
- BT to launch retail products only when equivalent wholesale products are available.

Potentially, there are very real problems pending as a result of the (lack of) definition of 'not reasonably practicable'. A very good example is illustrated by the narrowing of the applicability of Equality of Inputs in Annex F of the settlement:

F.20 ...the application of Eol to Network Hooks might be problematic. This is because the internal interfaces within BT's network between the network intelligence layer and the higher layers of the service stack may be proprietary. Exposing these proprietary interfaces to the alternative providers, as would be required by the application of Eol, may be a complex and costly process.

This may mean for example that it is "not reasonably practicable" in the context of the TSR undertakings, to guarantee end-to-end quality of service for real-time video and voice. This would be a serious problem for industry and for innovation more generally. The undertakings are a fairly sensible set of commitments, but Ofcom cannot afford to relax its monitoring of the market, because if equivalence of input is not available to important things such as end to end quality of service, it will be of limited use. Additionally, when looking forward to 21 CN, equivalence of inputs could end up looking a lot more like equivalence of outcomes, which is something Ofcom should be very careful over.

The additional issues where 21CN and the Settlement are closely interrelated are in the areas of :

- Compensation
- Whether equivalence in 21CN is found to be generally "reasonably practicable" within the Settlement
- Pricing equivalence: it is crucial that 21CN remain part of the pricing equivalence debate. Equivalence must exist and continue on the market, and 21CN is part of the development surrounding this.
- Systems ownership - there is an absence of vital detail on info systems ownership, sharing and development across ASD and the rest of BT, which is especially relevant to 21CN developments
- Cost recovery – cost recovery should be specifically NOT part of the Settlement as this is something which industry is not required to pay for; the re-organisation is entirely part of BT's strategy. It is something that BT has anticipated for years, as part of an upgrade of its network in general. It is also tied to the fact that BT, as the incumbent, is fully aware of its position as the 'sole provider'/sole owner of the most complete and extensive network in the UK. BT revealed it had made £1bn in cost savings a year, and this could (and probably should) be ploughed into funding the necessary 21CN network upgrade project.

COLT has highlighted some additional specific issues regarding 21CN:

"No foreclosure of unbundled network access"

This principle is welcomed. However, we remain concerned that the two key operative provisions which are designed to put it into effect are weak. The first, at 11.3, is simply a three-month negotiation window -- a procedural hurdle. The second ignores the importance of intermediate wholesale markets: alternative providers need to be able to compete at wholesale level because they derive a large proportion of their revenues from wholesale markets.

"Charges to be based on efficient design"

Again, the principle is excellent but it is devalued by some carveouts. For example, the principle ceases to apply if the 11.3 procedural hurdle has been jumped over, and it is not appropriate to establish the principle if BT can escape it by procedural means. In any event, Ofcom has powers to set charges based on efficient design under its sector specific jurisdiction. It is imperative that those powers continue to be exercised in a robust way.

"Equivalence of input for next-generation SMP products"

Once again, we endorse this principle wholeheartedly. However, it only applies "in so far as is reasonably practicable". This is a problem on two levels. First, it generates uncertainty -- it is not easy to construe now in a practical sense and so we cannot readily assess what it will mean when the principle is applied. Secondly, Ofcom has already made some statements about what might not be reasonably practicable (see annexes F. and G. to the 21 CN consultation). These imply strongly that the "not reasonably practicable" carveout will mean that aspects of services which rely on levels three and above of the OSI stack will not benefit from equivalence of input. This is extremely significant because it makes equivalence of input in a 21 CN world look much more like equivalence of outcome and jeopardises the possibility of competitors providing innovative products to end-users.

"No retail services without wholesale inputs"

This principle is warmly welcomed and, while there are questions of detail, there seemed to be no specific points which fundamentally undermine it. The outstanding areas of concern include the time in advance of retail services at which the wholesale inputs must be launched and the question of whether those wholesale inputs are fit for purpose.

"Broadband dial tone not to undermine LLU"

This principle seems sound although, again, we have questions about what it will mean in practice.

Compensation arrangements for 21 CN implementation

We welcome the attempt to clarify what compensation will be available but we find the principles weak. They appear to neglect the approach to cost recovery endorsed by the Monopolies and Mergers Commission in the number portability inquiry and used by both Oftel and Ofcom since 1995. They also seem to detract from the rights of parties to the standard voice interconnection reference offer under clause 4; and they only apply to network costs in any event. This is perhaps the quintessential example of a case where, while there is no objection in principle to the inclusion of these ideas in the TSR settlements, that is absolutely not an alternative to Ofcom using its sector specific powers. We would expect Ofcom to do that in a highly effective manner.

There remains the outstanding issue of paragraph 11.20 of the draft undertakings. The first sentence of paragraph 11.20 seems to distance the whole of the undertakings (apart from section 11) from BT's 21 CN. Apart from contradicting some explicit drafting elsewhere in the undertakings, this also dramatically restricts the effect of some generic obligations such as those relating to migration (3.7) and the ones about successor products (3.1.2). COLT believes this confusion must be rectified in the final undertakings, to avoid inaccurate interpretations of the settlement.

III.5

Cultural change within BT:

a) Cultural change within BT:

There should be a real and fair test of BT's commitment to cultural change within BT and an understanding of BT's plans in this area, with metrics developed to measure this development, so that altnets can maintain sufficient pressure to motivate BT, and so that BT makes advances, and achieves its goals throughout. This cultural shift should extend to BT Retail.

Cultural change does not obviously only mean a constructive change in attitude, in processes and in systems, but would also be a re-branding exercise for certain elements (stationery and buildings, and ultimately uniforms and vehicles).

b) Cultural change between BT and external stakeholders:

COLT looks forward to working with BT to define how to put this Settlement into practice. COLT believes that there is fundamental importance in working together constructively. This is a test of the new cultural approach within BT (a move towards greater openness).

COLT has already made various suggestions in conjunction with industry to this end, such as getting product working groups to agree equivalence roadmaps and the introduction of a systems working group (with the potential use of independent outside consultants to sign off the underlying IT plan and delivery).

IV Conclusion

Now, more than ever, effective engagement between BT, Ofcom and industry is crucial, as the proposal enters the implementation phase.

Close cooperation between industry representatives and BT is essential to ensure that success is achieved and that expertise is shared. Milestones for achievement should be set and monitored, with clear delineations of accountability and timescales. Post-implementation, a system of positive monitoring and review should be put into action. It should be feasible to use this to develop and improve equivalence and organisational activities undertaken by BT, potentially modifying the undertakings and avoiding future dispute.

As Ofcom has said, the aims of the new regulatory approach are:

- Forward-looking regulation to cover transition from PSTN to IP
- Certainty for the market
- Clarity for operators / investors about direction of future investment
- Focused regulation with effective sanctions to ensure delivery; allowing for:
 - Deregulation where regulator is a substitute for market competitiveness; = less, focused, tougher
 - Which supports competition to drive down prices for consumers / businesses
 - And supports innovation and competitive new products / services (e.g. next generation broadband, IPTV, VOIP)
 - Ensure a strong communications sector able to underpin UK competitiveness

It is extremely important that all areas of the undertakings fully reflect all of these goals in a transparent and objective manner. Ultimately, COLT urges Ofcom to carefully consider all the ramifications of the settlement, but also to fully embrace this change in the sector.

COLT has included other areas of slight confusion, conflict or perceived opacity in Annex A below, which we feel necessitate comment. Some of these points draw on elements raised at discussions surrounding the legal definitions of the undertakings :

V

Annex A Table of amendments :

This section includes COLT's detailed comments on the undertakings, notably regarding areas of conflict or perceived opacity. Some of these are particularly significant and necessitate discussion :

Paragraph number	Amendment/Text	COLT comment
Recital C	"pursuant to section 154 of the Enterprise Act 2002"	To make it clear the undertakings are binding.
2.1	"ASD Headquarter Management Team" comprises the ASD CEO and his London-based direct reports.	But no requirement that members of ASD management team should be based in London. For example all key direct reports, if based outside London, would not fall into definition and would not be subject to undertakings 5.30 on separate office space. In practical terms this could mean all the regional managers would continue to be integrated with BT Wholesale/Retail
2.1	"Associated Services" means those products and services supplied from time to time ancillary to the provision of Metallic Path Facility and Shared Metallic Path Facility. At the date these Undertakings take effect they are listed in section B6, part 6.03 of the BT Carrier Price List and include: a) comingling space (variable exchange space footprints and rack space units); b) power (AC & DC); c) vent & cooling; d) internal tie cabling; e) external tie cabling (for distant location); and f) cable link for Metallic Path Facility and Shared Metallic Path Facility (installation of third party backhaul).	What happens after the date of Undertakings? Is the list set in stone? It would be better to use a generic definition from market review, with the carrier price list being the then current list.
2.1	"BT's backhaul network"	We are concerned that this inclusive definition may include parts of the trunk network. Will trunk costs be allocated to ASD? How can this be avoided?

2.1	“Commercial Information”	“relates to” should read “includes” because other types of information could be commercial information
2.1	“Communications Provider”	It should be made clear whether BT is intended to be included whenever this term is used – otherwise it is ambiguous.
2.1	Equivalence of Inputs	The definition needs re-working; exclusions are too wide and should specify “next best possible” as their fall-back; (d) must be narrowed to apply only to explicit carveouts from Eol principle.
2.1	Migration Process	(e) should read “and/or two or more” rather than “or two”.
2.1	NGN	We are not convinced that the definition works – that service-related functions will always be independent of transport related technologies – what about MPLS?
2.1	Wholesale... Line Rental	Use of “ordinary maintenance” problematic – intended to exclude prompt/total care? Should say “all classes on maintenance”.
2.1	General – use of OSI stack and similar terms	It is recognised that these are difficult, but current approach may generate some odd results; we look to Ofcom to monitor and enforce to ensure that does not happen.
2.1	“RFS” means the ready for service date from which an Equivalence of Inputs product is available for use <i>[and fit for purpose]</i>	Without the inclusion of ‘fit for purpose’ there is no incentive on BT to ensure that products detrimental to BT (such as migration) actually work.
3.2	Notwithstanding the dates specified in Annex 1, BT will as a gesture of good faith:	It is unclear whether BT thinks “as a gesture of good faith” means that this isn’t enforceable undertaking. If it is not part of Undertaking shouldn’t be here. Best view is that the “will” is clear and that the obligation to pay is an enforceable undertaking. What are Ofcom’s / BT’s views on the effect of this?
3.2.2	any dispute over the provision of any such allowances may be referred to Ofcom and BT agrees to be bound by Ofcom's decision	Does Ofcom have the power to do this?
3.7	To the extent that the Migration Processes are either internal to BT or are otherwise within BT’s control, BT	See earlier comments - it needs to be clear that BT is obliged to actually do something, and Eol should be used as

	shall apply Equivalence of Inputs to BT's Migration Processes where such processes involve at least one product or service for which BT must apply Equivalence of Inputs, and, where relevant, at the same time as BT is required to supply RFS for Equivalence of Inputs in accordance with the timetable in Annex 1.	a description of what it needs to do, and fully included here.
4.1.2	use its reasonable endeavours at all times to resolve any outstanding issues with any other Communications Provider concerning its provision of the products and services referred to in section 4.1 (including the systems and processes used to supply such products and services) to that Communications Provider <u>including in order to achieve Equivalence of Outcomes.</u>	See main body of text – this clause is relatively “toothless” without this addition; and does not implement Ofcom’s statement of 23 June 2004 that BT would commit to working to implement EoO.
5.6 (e)	Deleted “MSANs do not contain any Network Layer functionality”	We expect that they will
5.11	ASD shall control and operate the assets contained within the Physical Layer of BT's Access Network and the Physical Layer of BT's Backhaul Network including such items needed to support this, such as line testing and remote diagnostics.	But not own... Given that the divisions of BT are part of the same legal entity perhaps the correct question is to which division is the investment decision, the capital asset balance sheet entry, depreciation and opex allocated, as well as the ability to control? Does control mean the ability to say no, or to choose between conflicting priorities? Can the controlling division, sell, lease or outsource activities and assets? This drafting seems to be right, but more detail on the accounting procedures for ASD is needed to be sure.
5.12.1	and volume forecasts which shall be agreed with relevant platform managers	Where do platform managers sit? What controls are there over information flows to platform managers? Are they making network decisions (including access network products) on the basis of BT's group best interests?
5.13.1	ASD shall comprise all field engineers	This does not include all access field engineers - for example field engineers concerned with transmission and network layer. Who is <u>not</u> being

		transferred to ASD?
5.13.3	people who carry out activities which are ancillary to those described in section 5.13.1 and section 5.13.2 and those who support and manage them	Is this cleaners and PAs, or is this intended to include all staff necessary for fully functioning business unit (e.g. finance, HR, etc)? If the latter, they should be specified. ASD should also include sales staff and IT managers etc. Better also to include general obligation: "ASD must include the people needed to do the job."
5.14.2	"daisy chain"	Should be an example rather than a definition
5.14.4	"managed transmission service"	Not necessarily possible without controlling layers three and above.
5.17	Where assets controlled and operated by ASD, as described in section 5.11 above, are not used in connection with any SMP Product, such assets may be re-allocated to another part of BT	What does "allocation" mean - is this control and operate as well as accounting cost allocation?
5.22	The ASD CEO shall report to the BT Group plc CEO	The addition of " <i>solely and directly</i> " after "report" would ensure no dotted line reports to other parts of BT
5.25	Add "and the EAO" to the end....	... otherwise EAB may not be able to get secretariat help with this
5.27	(a)... calculated on the same basis	Must not allow bulk discounts to BT downstream
5.27	c) charges made for products and services which are a form of Electronic Communications Service provided to ASD from other parts of BT as inputs for SMP Products provided by ASD will be separately identified and cost orientated [<i>and made available to other Communications Providers</i>]	What services will they be? Should CPs have access?
5.27	d) the accounts [<i>will</i>] include the relevant parts of BT's Access Network and BT's Backhaul Network assets[.]	Is there an element of doubt about this? Undertaking should be clear and unequivocal
5.28	c) <i>the ASD shall publish accounts equivalent to those it would be required to publish if it were a separate legal entity</i>	Needed to give transparency to other CPs, who will not see ASD management accounts. These are initial thoughts and will need further discussion
5.30	The ASD Headquarter Management Team shall move to:	This obligation is much looser than it appears as it only applies to those based in London. See revised definition
5.32		Should also include a ban on

		secondments and gardening leave provisions
5.33	All employee share plan	Operation must be reviewed WRT quantum of rewards for most BT employees – this could turn out to be quite a significant incentive in relative terms. We have relied on Ofcom’s assurances that this is <i>de minimis</i>
5.35	Save as set out in section 5.36, no employee, [<i>director</i>] or agent of BT (including its external advisers and subcontractors), who is not working for ASD	What about where they work for both ASD and the rest of BT. For example, if a consultancy firm is retained to study BT’s strategy and make recommendations across group, if they are making recommendations for ASD, they would not be excluded by this clause. However, if the majority of their fee is paid by other parts of BT this may introduce conflict
5.36.1	sections 5.35.1 and 5.35.2 shall not apply to the nominated individuals, and individuals occupying the roles and functional areas (and their relevant external advisers, sub-contractors and agents)	If these advisors, sub-contractors and agents work for other parts of BT, since those divisions are part of the same legal entity there is no restriction on those agents from sharing the information with other parts of BT
5.38	“...on a non-discriminatory basis in relation to products and services where Equivalence of Inputs applies and on a not unduly discriminatory basis where other SMP Products are involved.”	If this distinction is to remain, “undue” should be interpreted in line with Ofcom’s guidance from time to time
5.40	Logical partition of systems doesn’t apply to OSS	It should apply to OSS
5.41	“ASD will not generally supply any product or service to any other part of BT unless it also offers that product or service to other Communications Providers on an Equivalence of Inputs basis...”	Delete word “generally” and ensure that Eol applies to internal supply too; otherwise, a clear get-out for products not names in Annex 1.
5.42	For the avoidance of doubt this section does not apply to BTs Operational Support Systems [<i>where such partition is not reasonably practicable</i>].	Does this imply that undue discrimination is permitted if due to OSS integration? If so, shouldn’t this be prohibited? See wide definition of OSS
6.17.1	“Alternative Communications Provider Operational Area” means a Communications Provider Operational Area at another Exchange other than that requested by the Communications Provider	If the intent is that charges for all services will be the same as if the space is in the operational area, then the definition is not the right place to put that obligation on BT. As drafted, BT could say that no such space exists, because the charges would be

		greater which I don't think is the intended result. The definition should just read "means a Communications Provider Operational Area at another Exchange other than that requested by the Communications Provider", then the obligation that charges are no higher should be dealt with in main text of undertakings
6.17.2	(b) is not bona fide reasonably required by BT at any time for the purposes of BTs business	Very broad provision, and means that BT has preferential call on space, since it can forecast use and have "first call" on space, whereas other CPs cannot
6.17.2	"Communications Provider Property Users Group" means a group representing Communications Providers made up of 3 representatives appointed by the Communications Providers	CPs including BT, or other than BT? How are members elected and what responsibility do they have to act in interests of industry as a whole (as opposed to companies reps come from)? Using this as a mechanism seems flawed and potentially discriminatory to non-members of group
6.17.2	"Equipment" means equipment listed in Annex 4, owned by the Communications Provider (but not its customers or any other third party) used to provide Electronic Communications Services that make use of Network Access and which is connected to the BT network	What about leased equipment, or equipment subject to RoT?
6.17.3	The Undertakings in these sections 6.16-6.23 are given on the basis that BT will be deemed to be acting reasonably if its actions are materially consistent with its corporate property strategy and its objectives for NGN deployment	Both of these policies are entirely within the control of BT and could quite legitimately be formulated in a way that favours BT over its competitors. As such, these equipment location undertakings are not helpful
6.18	Within six months of these Undertakings taking effect and on an on-going basis thereafter and subject to sections 6.18-6.23 below, BT shall provide other Communications Providers with the facility to occupy on reasonable commercial terms	If the first draft of the ANF collocation provisions are anything to go by what BT considers to be reasonable commercial terms may be some way short for what other CPs would consider to be reasonable commercial terms
6.18	b) identifies the Equipment	Why is this relevant? Provided the equipment meets objective criteria (floor-loading, heat, fire resistance) this is of no concern to BT, unless BT want to gather competitor intelligence and/or target its services directly against

		competitors
6.18.2	This section 6.17 does not apply to co-location as defined for the purposes of Metallic Path Facility and Shared Metallic Path Facility	Why is what is essentially the same product treated differently? Wouldn't the easiest way to address this to be remove restrictions on co-location provided under ANF?
6.20	If the Communications Provider does not contract to locate its equipment at the BT site with one month of BT offering reasonable commercial terms	What about bona fide disputes over whether terms are reasonable?
6.21	BT may at its discretion	BT is free to charge what it likes and could charge something very different.
6.23	Within six months of these Undertakings taking effect, BT will deliver to Ofcom <i>[and inform other Communications Providers by including within the NIPP]</i>	Why will this not be provided to other CPs for planning purposes? As drafted, they would not be able to plan, and would incur costs of site survey and contract negotiation before being told that site is due to be vacated. Process seems designed to inhibit CP planning and to raise their costs
6.24	{It will be part of the reasonable commercial terms offered by BT under section 6.19 that if any Communications Provider seeks to remain in an Exchange after BT has vacated the Exchange then the Communications Provider will fully indemnify BT against all compensation, damages, actions, costs and claims howsoever arising under the terms of the BT and Telereal property transaction completed on 13th December 2001}	The Undertakings are offered by BT to address competition concerns. It is not appropriate to protect BT's commercial interests by means of the Undertakings. In our view this is unreasonable. Is a summary of the key terms of that deal to be provided?
9.2	The Code of Practice shall include specific guidance for the BT employees in the following areas	Why is BT Retail excluded?
10	EAB	General comment – EAB is an enhanced compliance mechanism; we do not believe that the provisions are as strong as they should be
10.1	consisting of five people, namely three independent members	Is independence to be judged according to Combined Code rules? How will these members be paid? Will they become BT employees on appointment?
10.4 <i>et passim</i>	"consultation with Ofcom"	Needs further explanation; veto would be better
10.6	The Chairman of the EAB, following agreement with BT Group plc Chairman and consultation with	<i>for gross misconduct only</i> : to ensure that independent minded members are not removed to avoid embarrassing BT

	Ofcom, may remove the independent members of the EAB	
10.16	BT shall inform the EAB	Shouldn't BT inform Ofcom as well, indicating that the matter has also been referred to EAB?
10.27.1	"KPIs"	What KPIs will they be?
10.31	BT shall apply to the operation of the EAB those principles of the UK Combined Code on Corporate Governance which it considers appropriate and relevant	The Combined Code is really designed to deal with the agency (governance) problems experienced by owners (shareholders) of public companies with respect to boards and management. As such it is questionable (esp given BT's discretion as to what is applied) how much benefit this provision will provide in practice. The EAB is not a board, it doesn't have function of board and BT's competitors are not in the same position vis a vis EAB as BT's shareholder to main board
10.23	BT shall ensure that the EAO has reasonable access to information held by BT that it needs to fulfil its role, regardless of where such information may be held by, or within, BT.	Not full and unrestricted access. What about access to people and systems?
10.30	The EAB annual report shall be audited	Must be full, rigorous, substantive (not quality assurance) audit of main report not just summary
10.36	Procedural provisions	Independent members must get reasonable notice
11	21CN - general	See main body of response – the ideas are good but there are too many ways in which BT can circumvent certain conditions. We rely on Ofcom to ensure this does not transpire in practice
11.9	"not reasonably practicable"	An unclear carveout from one of the most important provisions in the undertakings. COLT suggests that "not reasonably practicable" shall mean only reasonable circumstances in which provision on an EoI basis is either technically impossible or would fail an industry-wide cost benefit analysis
11.18	The principles BT will use making compensation to a Communications	Ofcom (based on MMC's recommendations in its report into

	Provider taking Network Access from BT as part of BT's implementation[...]	<p>number portability) historically used 6 principles when looking at cost allocation:</p> <ul style="list-style-type: none"> – <i>causation costs</i>: should be recovered from those whose actions cause the costs to be incurred where there are externalities; – <i>distribution of benefits costs</i>: should be recovered from the beneficiaries especially where there are externalities; – <i>effective competition</i>: the mechanism for cost recovery should not undermine or weaken the pressures for effective competition; – <i>cost minimisation</i>: the mechanism for cost recovery should ensure that there are strong incentives to minimise costs; – <i>reciprocity</i>: where services are provided reciprocally, charges should also be reciprocal; and – <i>practicability</i>: the mechanism for cost recovery needs to be practicable and relatively easy to implement. <p>It is not clear why BT should use different principles, and in fact the suggested principles may be more favourable to BT than would be the case otherwise</p>
11.18	b) the extent to which these changes are unilaterally decided by BT without industry agreement	Why is industry agreement relevant - cost causation looks at who causes costs to be incurred? It seems odd for other CPs to pick up more costs as a result of co-operating
11.18	e) the extent to which new investment of assets which cannot be re-employed is reasonably and justifiably made by a Communications Provider after it has been made aware of forthcoming changes	This is not clear-cut. If change is somewhat off, but CP needs more capacity to deal with current customer demand why should it be forced to either not meet customer demand or not be able to recover investment
11.20	This section 11 contains all BT's specific obligations by virtue of these Undertakings in relation to the development and deployment of its NGN. Subject to the provisions of this	This provides very large doorway through ASD separation and Chinese walls. Shouldn't this be subject to other undertakings e.g. 3.7 on migrations?

	section 11, nothing in these Undertakings shall impede the flow of information reasonably required to enable BT to design, build and operate its NGN or the decision-making process relating thereto.	
12.1	<i>[BT shall treat any request for information from Ofcom in connection with these Undertakings as if such request were a request made under section 135 of the Communications Act 2003, provided that Ofcom makes such request as if it were made under Section 135 of the Communications Act 2003.]</i>	Which could be a protracted process. Why does Ofcom have to consult? Why not “extend” power of Ofcom under s135 Comms Act to gather info (which has safeguards) to gathering information in respect of these undertakings?
14	Directions	Must not delay real enforcement action
Annex 1		Must be amended to make it clear that EoI applies to ALL downstream products for EoI inputs (e.g. VPNs etc)
Annex 2		There should be specific restrictions on the uses to which these people can put data which would otherwise be of restricted circulation

VI

Contact details:

For further information, please contact:

Markus Reinisch

Regulatory Affairs
COLT Telecommunications
Beaufort House
15 St Botolph Street
London
EC3A 4QN

Tel: 020 7947 1036

Email: markus.reinisch@colt.net

Alternative contact:

Florence Duffield

Regulatory Affairs
COLT Telecommunications
Tel: 020 7390 3676
Email: Florence.duffield@colt.net