Wholesale Local Access Market Review

Further consultation on proposed charge control for wholesale standard and superfast broadband

and

Further consultation on proposed quality of service remedies

October 2017

NON-CONFIDENTIAL VERSION

1 Summary

1.1 This document is TalkTalk's response to the two WLA consultations Ofcom published on 14 Sept 2017 covering revised QoS targets and a range of changes to the MPF and GEA charge controls.

1.2 We agree with many of Ofcom's proposals and changes. However, we have some significant areas where we disagree with Ofcom's proposed approach or have other comments:

- We understand the logic underlying Ofcom's proposal to reduce the repair QoS standard to 85% within SLA. However, given the importance of quality to consumers we consider that the new standard should reasonably be set higher – for instance, because the standard for each region is based on the worse performing region in the worse year. Also, Ofcom must be wary of relying on Openreach's estimates for the additional cost of higher quality given BT's/Openreach's track record of provided Ofcom with biased, inaccurate and self-serving data.
- In proposing to not impose a starting charge adjustment to MPF prices to reflect the cost attribution review, Ofcom has lost sight of its ultimate objective to protect consumers' interests. As a result of its previous flawed cost attributions, BT has enjoyed inflated prices and excess profits at the expense of consumers (of over £1 billion across the last 5 years). The excess profits will continue unless the inflated prices are ended by applying a starting charge adjustment.
- We are pleased that Ofcom has changed its stance and agreed to set cost-based prices for Cablelink which will result in price reductions averaging around 80%. This data reveals how Openreach has strong incentives to set hugely inflated prices and why it is therefore essential that Ofcom limits Openreach's pricing flexibility.
- The revised costs for co-mingling and tie cables reveal that BT has provided inaccurate data to Ofcom, and that there has been extensive double recovery of costs. This is far from a one-off – BT has a consistent track-record of adopting inappropriate attributions and making errors the vast majority of which are in its favour. Ofcom must seriously consider whether BT has breached its regulatory obligations (and if so, enforce robustly). It should also ask why this error was not spotted earlier and whether Ofcom needs to revise its future approach to scrutinising costs.
- Ofcom's approach towards aborted visit charges (AVCs) as well as to various GEA service charges will bake in systematic over-recovery of costs leading to consumers paying excessive charges. Ofcom has proposed that charges are not based on attributed costs due to a lack of data. It is not acceptable that BT is permitted to over-recover its costs due to BT's inadequate cost information.

1.3 This second consultation includes a number of significant changes in forecast costs and prices. For example, a number of changes decreased the 2020/21 MPF rental costs by £30m per year or about £3.50 per line[1]. Co-mingling, Cablelink and tie cable prices reduced significantly decreasing wholesale revenue by about £30m[2]. These are large changes so late in the consultation process. Some were due to new information becoming available (such as on non-domestic rates). However, in other cases the changes correct mistakes and errors Ofcom in the March consultation e.g. removing double cost recovery, previous miscalculation of SLGs and no charge control on Cablelink. Whilst we naturally welcome Ofcom correcting errors, we are concerned about the number and magnitude of them – consumers rely on Ofcom to set prices based on reliable cost data albeit against the best efforts of BT to deceive Ofcom. It is essential that Ofcom ensures BT provides sound information and, where BT is breaching its obligations, Ofcom takes robust enforcement action.

1.4 This document is laid out as follows:

- Section 2 discusses aspects related to quality such as the revised repair QoS standard and the cost of increased quality;
- Section 3 provides our comments on assumptions that affect the MPF rental price such as pension, SLG and non-domestic rates; and,
- Section 4 describes our comments on ancillary services.
- Section 5 outlines our concerns in relation to poor practices in BT's regulatory accounting that this consultation made apparent.

2 Quality aspects

2.1 In this section we cover a number of aspects regarding quality that are raised in the two consultation documents:

- The revised QoS standards;
- The cost of higher quality (sometimes referred to as the resource uplift); and,
- Other aspects of cost forecasting relating to quality.

2.1 Revised QoS standards

2.2 Ofcom has revised the proposed fault repair QoS standard for 2020/21 from 93% within SLA to 88% within SLA (for repairs where MBORC does not apply). For all repairs, including those where MBORC does apply, Ofcom has revised the standard from 90% to 85%.

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[1] These cost decreases and increases offset each other to some degree. For MPF rental decreases totaled £3.50 and increases totaled £3.40 giving a net decrease of £0.10. For GEA rental decreases totaled £1.90 and increases totaled £3.80 giving a net increase of £1.90

[2] About £21m for co-mingling, £3m for tie cables and £8m for Cablelink. The latter is a rough estimate since Cablelink market volumes/revenue is not disclosed

2.3 As set out in our response to the March 2017 QoS consultation, we strongly support the use of quality standards to improve quality of service, and Ofcom's proposals to increase these standards following its Digital Communications Review to drive a step change in Openreach performance. In our previous response, we supported the higher standards Ofcom proposed and argued for their introduction on swifter glidepaths. We recognise that Ofcom has revised its proposals in light of new evidence about Openreach's operational capabilities, the resources required to meet the increased standards and the expected performance of the access network. However, while it is appropriate for Ofcom to take account of the new evidence when setting standards, it is vital for consumers that Ofcom does not reduce the targets too much and thoroughly scrutinises the Openreach evidence.

2.4 Whilst we think there is sound logic for setting the fault repair target below 93% we think that the 88% and 85% targets could reasonably be set higher. There are a number of reasons for this:

- The 88% has been chosen on the basis of the glass ceiling level in East Anglia which is the most difficult / has the highest level of the 10 GM regions[3]. This means that all the other 9 regions will find meeting this standard 'easy'. Whilst it may be appropriate to set the standard for each or any region at 88% there should be a standard for all regions in aggregate that is above 88% (about 89.5% based on Ofcom's data[4])
- the 3% MBORC allowance (i.e. the assumption used to reduce from 88% to 85%) is too high. It was based on 2011/12 which was a 'bad' year for MBORCs. Ofcom should consider updating this and base the MBORC adjustment on the average year
- The 88% is still substantially below the glass ceiling level of 90.8%
- Openreach can complete some of the more difficult repairs (that are above the glass ceiling) within the SLA period (particularly the CL1 SLA). For example, almost half of the 'glass ceiling' repairs are difficult due to the need for civil engineering (see QOSC Fig 3.3). Whilst civil engineering may on average take several days there must be some simpler cases where it can be completed within the SLA period.

2.5 The first and second points above mean that Ofcom is basing its target on the most difficult region in the worse year. That is not a stretching standard.

2.2 The cost of higher quality

2.6 Given that Ofcom is proposing to require Openreach to provide higher QoS than it currently provides, forecast costs need to reflect the additional costs of delivering higher quality of service – this is referred to as the 'resource uplift'.

[3] See QoSC §3.16, Fig 3.5

[4] Figure 3.5 shows that the national average glass ceiling is 1.5% higher than the glass ceiling for East Anglia

2.7 In the March consultation Ofcom based its estimate of resource uplift using the Analysys Mason (AM) Resource Performance Model (RPM). Openreach have proposed that instead Ofcom should use its model (referred to as the Allocation Model) – a model which, Openreach claims, estimates that the resource uplift is much higher. Ofcom has rejected using Openreach's model.

2.8 We have not had sight of Openreach's model and so cannot comment on the detail of the model. However, we think there are strong *a priori* reasons for not relying on it:

- BT and Openreach have a consistent track record of providing information to Ofcom that is biased and self-serving. For example:
  - Ofcom had to extensively modify Openreach's model to estimate resource uplift for the FAMR 2014 to reach an appropriate assumption[5]. Openreach's model was so poor that in this review Ofcom has had to invest in developing its own model
  - More recently in this consultation has revealed that the costs BT provided to Ofcom for co-mingling and tie-cable included extensive double cost recovery
- Openreach's model does not reflect reality – for instance, sharing of resources across adjacent areas
- As AM note the model produces counter-intuitive results (QoSC §1.10[6])

2.9 We are also concerned that AM's model and Openreach's model may not take into account that short term peaks can be met at lower cost by flexible working practices, for example through overtime or the use of contractors rather than recruiting additional full-time staff[7]. It appeared that the model used in 2014 did not take these factors into account and it is not clear if this is taken into account in the 2017 RPM model.

2.10 We note that the resource uplift is based on the 88% QoS standard i.e. 88% of repairs where MBORC does not apply must be repaired within SLA. It is not clear whether this is appropriate or whether the resource uplift should be based on the post-MBORC standard (i.e. 85%) i.e. 85% of all repairs (including repairs where MBORC applies) must be repaired within SLA. Given that MBORC is an arbitrary concept it would seem logical that resource requirements would not depend on whether MBORC applies to a repair or not.

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[5] See FAMR Statement May 2014 §A17.71*ff*

[6] CCC refers to the 'Further consultation on proposed charge control for wholesale standard and superfast broadband' and QoSC refers to 'Further consultation on proposed quality of service remedies'

[7] See Frontier Economics Report – FAMR: Review of Openreach's DES model, February 2014 https://www.ofcom.org.uk/__data/assets/pdf_file/0028/83971/sky_and_talktalk_-_frontier_economics_review_of_openreachs_des_model.pdf

2.3 Other quality aspects

2.11 We comment below on a number of other aspects of the charge control that relate to quality.

2.3.1 *Efficiency and fault reduction overlap*

2.12 We note that Openreach have argued that the efficiency assumption and fault reduction assumption double count the potential improvements (CCC §3.76). We do not agree with Openreach's suggestion since we consider that it is reasonable for Openreach to achieve both the fault reduction (of about 10%) and the efficiency gains (5.5% on opex and 3% on CAPEX).

2.13 Openreach's fault levels have remained broadly flat in recent years[8]. Therefore the 6.6% historic BT efficiency gains[9] that is a key benchmark Ofcom uses to set the future efficiency assumption was achieved without making any fault rate reductions. Thus 6.6% remains a relevant and reasonable benchmark for potential efficiency gains excluding fault reductions.

2.14 In any case, Ofcom must reflect that as an incumbent monopolist Openreach will experience in-built X-inefficiency that should be reflected in the efficiency improvement assumption.

2.3.2 *FVR expenditure capitalisation policy*

2.15 We note that 35% of the expenditure on the FVR programme is expensed (i.e. not capitalised) (CCC §3.83). We consider that 100% of the expenditure should be capitalised since the beneficiaries of the expenditure are the users of the network over many years into the future. It would only be appropriate to expense the expenditure (or some of it) if it was fully used or consumed within the year. This is not the case. The purpose of the FVR programme is to enhance network performance over many years.

2.3.3 *Retrospective uplift for previous FVR 'overspend'*

2.16 We note that Openreach have argued that the costs of the FVR occurred before March 2017 should be included in this upcoming charge control since the actual FVR CAPEX was above the FVR CAPEX forecast made in 2014 – see CCC §3.91. This is effectively a request for retrospection. Such a claim by Openreach is extraordinary. Openreach has over-recovered by several billion £s over the last 10 years and have also insisted that there should be no claw back of this excess profit. They have even argued that the excess should continue. Yet when there is one small cost category

[8] WLA March 2017 consultation A15.216 "*BT's fault rate has remained largely flat in recent years*"

[9] WLA March 2017 consultation Annex 15 Table 15.13

where they have notionally under-recovered they demand compensation even though their overall CAPEX was less than forecast. Openreach never cease to amaze!

3 MPF and GEA rental charges

3.1 In this section we comment on Ofcom proposals that predominantly affect MPF and GEA rental charges:

- non-domestic rates;
- SLGs;
- pension;
- LRIC:FAC ratios;
- impact of DPA proposals;
- MPF rental starting charge adjustment; and,
- Income from community fibre partnerships.

3.1 Non-domestic rates

3.2 Ofcom has proposed to update the BT's non-domestic rates (NDR) cost forecasts to reflect recent developments in light of stakeholder comments (including from TalkTalk) that the RV is highly likely to decrease as a result of BT's challenge/appeal of its valuation. We agree with the need to update the forecast as well as, for the most part, the proposed reductions.

3.3 It is essential that even though the outturn NDR cost reduction is currently uncertain that Ofcom makes a 'best estimate' of BT's expected NDR cost. It would be wrong in principle to not make a reduction or to err on the cautious side because of uncertainty. Such an approach would systematically bake in cost over-recovery. Instead, as Ofcom does (or should do) for the efficiency assumption, Ofcom should estimate the expected or average outcome with no bias up or down.

3.4 Ofcom has based its estimate of the reduction in BT's RV resulting from BT's challenge to its assessment on the level of RV reduction that Virgin achieved. Absent other better information this is the most reliable assumption for the reduction that BT will achieve. Therefore, this assumption should be used unless and until better information becomes available (e.g. the actual reduction achieved by BT).

3.5 The reasons for Virgin's reduction in RV are redacted. This makes it almost impossible for other stakeholders to comment on the applicability of this reduction to BT's case. We would encourage Ofcom to disclose at least a summary of the reasons. It is difficult to see that this information would be genuinely commercially confidential. If more transparency is not provided than Ofcom should give limited weight to any arguments from Virgin as to why Virgin's reduction is not relevant to BT.

3.6 We have the following comments on Ofcom's proposed approach:

- Ofcom compares the changes in RV for BT and Virgin across the 2010 list, draft 2017 list and latest list (for Virgin) (Table 3.3). One reason why Virgin's RV increased between 2010 and 2017 was an increase in the size of its network and business (e.g. Project Lightning). BT's network coverage has not expanded over this period.
- We think that Ofcom should set the assumption for RV reduction at the upper end of its 20% to 35% range. BT dedicates substantial resources to, and has a strong track record of, successfully reducing its NDR payments. There is no reason to suggest that they will not be successful this time

3.2 SLGs

3.7 Ofcom has significantly revised its estimate of the SLG costs that are included in charges: the total SLG costs in 2020/21 has increased by 63% (from £45.3m in March consultation to £73.9m in September consultation[10]) including a much larger 185% increase in repair SLG (£10.0m to £26.5m). We are also concerned by a lack of transparency.

3.8 This is a very substantial change in cost estimates which results in an increase in MPF charges by about £0.80[11]. In its summary of cost/price movements (in Tables 3.26 and 3.27) this large change is not transparent since it has been combined with several other factors some of which offset the SLG cost increase. Ofcom have not explained what led to previous mistake (except the small change in SLG days per event).

3.9 We ask that Ofcom provides a comprehensive, transparent and quantified outline of the assumptions it previously used and now uses to reach its SLG estimates. This will enable stakeholders to respond meaningfully to this consultation. For example, we have attempted to replicate Ofcom's estimate of a 185% increase in repair SLG but have been unable to come close to Ofcom's result.

3.10 In the table below we provide a breakdown for the percentage change in repair SLG payments (from £14.2m in 2018/19 to £26.5m in 2020/21[12]) based on the methodology Ofcom uses (e.g. event rate x SLG days x SLG per day x volume) and the data provided in the document.

Assumption	% change 18/19 to 20/21	Note

[10] CCC Table 3.12 and Table 3.20

[11] Increase of £28m is across MPF, WLR, SMPF and GEA lines. We estimate that the SLG per MPF line has changed by about £0.80 given there are c25m MPF and WLR lines

[12] CCC Table 3.20

Fault rate per line	-9%	Ofcom say *"less than 10%"*
% repairs outside SLA	-29%	From 17% to 12%[13]
= Event rate	-36%	Calculated
Average SLG days per event	+ 37%	3.10 to 4.24 (Table 3.14)
Daily SLG	+ 139%	£7.20 to £17.20
Volume (MPF+WLR+GEA)	+12%	MPF+WLR flat, SMPF decline, GEA increasing c8% pa
TOTAL	+ 135%	Calculated

3.11 Based on Ofcom's individual assumptions we derive that the increase in SLG is 135%[14] rather than the 185% Ofcom have used. Ofcom should explain clearly how it reached its result.

3.12 From what we can infer from the available information, we also believe that the individual assumptions proposed by Ofcom substantially overestimate the cost of SLG payments:

- The increase in average days payable appears too high. Assuming that the increase in repairs within SLA only reduces the non-glass ceiling repairs[15] – which have fewer SLG days per event – then using the data in Table 3.13 would suggest a 19% increase in average days payable (not 37%). The derivation of this is shown in the table below (for MPF). For WLR and GEA (which have different average SLG days per event) the increase is slightly higher – 22% and 21% respectively

		2018/19	**2020/21**	**increase**
fault repair QoS standard		83%	88%	
fail QoS standard		17%	12%	
of which:				
'glass ceiling' repairs		8%	8%	
non 'glass ceiling' repairs		9%	4%	
SLG days	MPF			
'glass ceiling' repairs	1.87			
non 'glass ceiling' repair	5.18			
average		3.43	4.08	19%

- The 37% assumption is anyway counter-intuitive since on Ofcom's assumptions the increased adherence to SLA will result in only a 3% decrease in the total

[13] derived as 1 – repair within SLA standard. 17% = 1 – 83% for 2018/19. 12% = 1 – 88% for 2020/21.

[14] This calculation is simplified since it does the calculation for all products together since Ofcom have not provided the SLGs for each product

[15] Openreach will tackle the low hanging fruit i.e. the repairs that it now completes within SLA (rather than outside SLA) will be those with shorter lead times which had lower SLGs paid per event

SLG days paid – a 29% reduction in repairs outside SLA and a 37% increase in average days payable.

- We understand that there is no guarantee that Openreach will increase the SLG by the amount of auto-compensation. Therefore we do not think that it is appropriate for Ofcom to assume that the SLG will increase by this amount unless it gets a firm commitment from Openreach or imposes an obligation on Openreach to increase the SLG in this way. In fact, the current assumption provides an additional incentive to Openreach not to do so and over-recover.
- The SLG costs should be adjusted to reflect that not all CPs will pay auto-compensation and therefore Openreach may not pay increased SLGs for all its CPs
- The prices SLG costs must be adjusted to reflect that there is little auto-compensation (and so additional SLG) will be paid in 2018/19[16]. Under the three year glidepath approach prices in 2018/19 will be increased to cover two thirds of increased SLG cost
- In any case, the daily SLG should be updated to reflect the final SLG amounts for auto-compensation (for example, the current proposal is £8 for repair not the £10 Ofcom has used).

3.13 Ofcom should similarly review its calculation of provisioning SLGs and also provide a clear and transparent description of its assumptions and calculation.

3.14 We note that Openreach claims (CCC §3.106) that SLG payments should rise as the QoS standard improves since in the past when performance has improved SLGs have risen (from 2011/12 to 2015/16). This is an absurd claim. Firstly, *a priori* it is illogical since as performance improves there will be fewer instances of SLGs being paid. Secondly, the historic rise in the SLG paid was a result of Openreach's strategy of avoiding SLG payments up to 2012 being checked by industry and regulatory action around 2013/2014.

3.3 Pension

3.15 Ofcom have noted that the on-going service pension cost for the BT defined benefits pension scheme (BTPS) may change as an impact of:

- changing market conditions (which alter actuarial assumptions); and,

[16] We understand that the current proposal is that there will be a 15 month maximum implementation window following Ofcom publishing its statement which is likely in November or December 2017

- BT's review to reduce its pension cost and deficit through, for instance, ending new accruals for current members of the BTPS[17] and moving to CPI indexing rather than RPI[18].

3.16 We agree that Ofcom should wait until the outcome of that review is clearer before finalising its assumption. However, we would note that if the actuarial assumptions worsen then it becomes increasingly likely that BT will take stronger steps to reduce costs as the need for mitigation will increase. Thus, it is highly unlikely that the combined effect of changed actuarial assumptions and the review of the scheme will be an increase in ongoing service cost – rather it will either stay the same or reduce.

3.4 Impact of duct/pole access

3.17 Ofcom have reduced the estimated cost of DPA productisation (from £28m to £7m). We agree with this change.

3.18 TalkTalk suggested[19] in its submission to the March consultation that the attribution of duct/pole asset costs to MPF/WLR should reduce as a consequence of the forecast use of DPA. Ofcom discusses this at CCC §3.123 – however, the text is not clear as to whether this occurs. We would appreciate if Ofcom could clarify its approach.

3.5 LRIC:FAC ratios

3.19 Given the brief description of the change to an already highly complex approach and the lack of explanation as to why the revised approach is appropriate it is not possible for TalkTalk to engage or comment on this issue.

3.6 Starting charge adjustment for MPF rental

3.20 We have three broad areas of comment on Ofcom's section regarding starting charge adjustments (SCA) for MPF rental.

- Lack of reasoning in March consultation
- The new reasoning provided in this consultation
- The use of DSAC as a test for distortion

[17] https://www.theguardian.com/business/2017/may/30/bt-considering-closing-defined-benefit-pensions-scheme-for-existing-staff

[18] http://www.telegraph.co.uk/pensions-retirement/news/bts-move-cut-workers-pensions-has-implications-millions/

[19] TalkTalk WLA Consultation response Jun 2017 §8.29

3.6.1 *Lack of reasoning in March consultation*

3.21 Ofcom portrays its description of the reasons for not imposing an SCA on MPF rental as a 'clarification' of its March consultation (CCC §3.161).

3.22 In the March consultation Ofcom provided a cursory two paragraph description to justify its approach. The September consultation includes many new reasons and far more detail. Thus the reasoning laid out in this September consultation does not feel like a clarification. Rather it feels like this thinking had not been completed prior to proposals in March[20] and instead the thinking was developed subsequently.

3.23 The lack of developed reasoning prior to the proposal in March is both surprising and disappointing. Whether to impose an SCA as a result of the cost attribution review (CAR) would have a significant impact on prices (over £140m over the review period[21]). It was an issue that demanded much more attention than the scant level of analysis than Ofcom gave it.

3.24 In contrast, by way of example Ofcom dedicated extensive resource and expense – including commissioning a complex model from Analysys Mason – to estimate the resource uplift for higher QoS – the impact of which is about £20m per year[22]. We recognise that Ofcom does not have the resources to be able to work through every assumption in detail but it must prioritise its effort on the most important issues in light of its duties. The SCA is an important issue that warrants much more attention.

3.6.2 *The new reasoning provided in this consultation*

3.25 We do not agree with Ofcom proposals to not impose an SCA for MPF rental to reflect the changes in attributions in the CAR and particularly the reattribution of cost from WLA to non-regulated markets.

3.26 We consider that there are two core flaws in Ofcom's reasoning to not impose an SCA:

- first, and most critically, Ofcom seems to have lost sight of Ofcom's ultimate objective to protect consumer interests
- second, Ofcom equates a BCMR to WLA reattribution with the CAR reattribution from WLA to non-regulated market – this ignores the fundamentally different nature of these reattributions which, as Ofcom itself states, affects whether an SCA is appropriate

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[20] For example, in the March consultation there was no mention of the BCMR at all, the cost attribution review or the subsequent reattribution from BCMR to WLA which now form fundamental elements of Ofcom's new reasoning. Indeed, in meetings with the team it did not appear to TalkTalk that these had been considered.

[21] This is the total amount over the charge control period. (TalkTalk Submission to March consultation §8.13)

[22] About £0.60 per MPF line (WLA March 2017 A11.132) across about 35m MPF, WLR and GEA lines

3.27 In developing its reasons to not impose an SCA Ofcom appear to have lost sight of the context of what the CAR was doing to meet consumer interests. Concerns over BT's cost attribution approach were first raised with Ofcom in 2009. By 2015 Ofcom had rightly concluded that BT had adopted an attribution approach that resulted in about £260m too much cost being attributed each year to regulated products[23]. As a result of this prices were higher than they should have been and BT was making excess profits at the expense of consumers.

3.28 It is axiomatic that consumers should benefit from price reductions to more competitive levels (and stop paying inflated charges) as soon as possible. We cannot see any sound reason to perpetuate consumers funding BT's excess profits. Yet Ofcom in its proposals effectively conclude that consumers' interests are best served by wholesale prices continuing to be inflated until April 2019. This cannot be right. Ofcom should be doing everything within its powers to end this damaging situation as quickly as possible.

3.29 Regarding the particular reasons given, there is a further and significant flaw in the way Ofcom analyses different reattributions.

3.30 Ofcom's basis for arguing that there is no need for an SCA is that the CAR adjustments are offset by the reattribution of costs from BCMR to WLA[24] in 2012/13. This is not correct.

3.31 The BCMR consultation and the BCMR statement rightly distinguished between two different types of reattribution:

- reattributions between regulated and non-regulated markets (we refer to these as type 1 reattributions)
- reattributions between different regulated markets (type 2 reattributions) e.g. BCMR to WLA

3.32 Ofcom concluded type 1 reattributions warrant an SCA but type 2 do not. This was clearly Ofcom's position in the BCMR consultation and the BCMR statement.

- In the BCMR consultation Ofcom said:

> *"we believe it is important to make a distinction between two types of cost reattribution: one that reattributes costs between regulated markets and one that reattributes costs between regulated and unregulated markets."* [25]
>
> *"changes in cost allocations (and accounting errors) between regulated and unregulated markets – we propose to impose a starting charge adjustment; and […]"*[26]

[23] The £260m included some basic errors as well as inappropriate attributions

[24] see CCC §3.155-§3.159

[25] BCMR: Leased lines charge controls and dark fibre pricing consultation June 2015 §4.107

[26] BCMR: Leased lines charge controls and dark fibre pricing consultation June 2015 §4.116

- In the BCMR statement Ofcom said "… *allowing BT the opportunity to recover its efficiently incurred costs. We note that part of the returns in excess of WACC is due to BT's cost re-attributions to other charge controlled markets which will not be reflected in those markets' regulated charges for at least the first year of our control. <u>We consider that such reallocations should be excluded from a potential SCA</u>*" [27] [emphasis added]

3.33 The reason for Ofcom treating them differently is sound: type 1 changes alter cost-recovery and distort competition whereas type 2 do not. Therefore, it is key to make type 1 corrections quickly to avoid unjustified cost over-recovery (or under-recovery).

3.34 Therefore, Ofcom is wrong to equate the CAR reattributions (type 1) and the BCMR to WLA cost reattribution (type 2). The latter cannot offset the need for an SCA. In deciding whether to apply an SCA to MPF rental the BCMR to WLA reattribution is irrelevant.

3.35 More generally, Ofcom attempts to suggest that the BCMR statement took a different position to the consultation (CCC §3.149). This is not the case. Whilst the BCMR statement backed away from having a formulaic approach to calculating the size of the SCA, it did not retract from the key underlying principles of where an SCA should apply (type 1 reattributions) and where it should not (type 2). Regulatory consistency dictates that Ofcom should follow the same underlying principles as in the BCMR, or clearly explain why it has changed its principles and/or why the principles apply differently in the two situations.

3.36 There are several other parts of Ofcom's reasoning that are also flawed.

3.37 First, Ofcom has ignored the allocative efficiency benefit of an SCA – applying an SCA will move prices closer to marginal costs[28] so improving allocative efficiency.

3.38 Second, Ofcom appear to believe that an SCA is only appropriate if price and costs are 'significantly' misaligned[29]. This is not correct for two reasons.

- Firstly, this is an arbitrary test – there is no sound economic rationale for Ofcom to use it to 'gate' where it will use an SCA and where it will not.
- Secondly, it is important to understand the reason for the lack of misalignment. Even though current MPF rental prices set in FAMR 2014 were based on pre-CAR attributions the current price is not currently misaligned from the current costs (which are based on post-CAR attributions). This is because BT's costs are higher than forecast in FAMR 2014 due, for instance, to BT underperforming the forecast efficiency gains. If Ofcom does not apply an

[27] BCMR Statement Vol II April 2016 §7.80

[28] Given the large fixed and common costs involved in providing MPF the marginal costs are much lower than FAC costs and prices

[29] see QoSC §3.150. The 'distorted price signals' test requires prices to be more misaligned from costs than the 'significant price/cost misalignment' test. Thus the relevant/binding test is the 'significant price/cost misalignment'

SCA for the CAR reattribution then effectively Ofcom is allowing MPF prices to immediately rise to reflect BT's underperformance (i.e. a starting charge adjustment for BT's inefficiency). This is not consistent with Ofcom approach's to not apply an SCA when there is an outperformance[30].

3.39 Lastly, applying SCAs will discourage BT manipulating its regulatory accounts. BT has a consistent track-record of adopting inappropriate attributions and making 'errors' which in the vast majority of cases work in its favour. This cannot be explained by chance – rather there must be something systematic and endemic in the way BT prepares, reviews and corrects its regulatory accounts that means that inappropriate attributions and errors work in BT's favour. For instance: when there are several possible attribution methods do they choose those which are most favourable; do they only invest effort in seeking and correcting errors that are not favourable; or, do they intentionally manipulate the accounts hoping that they will not be caught.

3.40 If BT are able to keep the gains from this manipulation for years after the errors are identified then BT's incentive to game the accounts will increase. Applying SCAs will reduce the incentive[31].

3.6.3 *Use of DSAC as test for distortive prices*

3.41 Ofcom highlights that it uses DSAC to test whether prices distort price signals and risk economic inefficiency (CCC §3.150). We think that the use of DSAC is unsound. Ofcom indicate that it uses DSAC since it reflects the prices that would be charged in a contestable market[32]– in other words the price a hypothetical competitor offering a sub-set of the products BT provides would charge. However, the use of DSAC is neither sound on the basis of economic theory nor in practice. We explain our reasoning below.

3.42 First, by way of context it is worth recognising that DSAC is only used in telecoms regulation. Despite being an approach developed by Oftel in the 1990s it has not, as far as we are aware, been adopted in any other country or any other sector (despite the EC adopting many of the approaches that Oftel/Ofcom have developed). This alone should raise questions as to whether DSAC is as useful as Ofcom appears to think.

3.43 Second, the DSAC cost is derived based on BT's cost structures and BT's cost levels. However, a competitor – particularly one that offers a subset of the services offered by BT – may well adopt a different cost structure/business model (e.g. different network architecture, fewer network nodes, different technology as do Virgin and

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[30] See BCMR Statement March 2016 §7.45

[31] although unless Ofcom removes the historic profits BT gets from its manipulation as well as imposing punitive sanctions the incentive to manipulate will remain strong

[32] See BCMR Statement March 2016 Vol II §4.99 "*The economic rationale for using DLRIC and DSAC stems from the theory of contestable markets. In a contestable market, we would expect a charge to be within the range of LRIC78 and SAC …*"

COLT) and will have different (almost certainly lower) unit cost levels since they are not hampered by legacy.

3.44 Third, the DSAC cost relies on an arbitrary assumption that BT makes for the scope of the hypothetical competitor – this assumption has a significant impact on the level of DSAC. For instance, if BT assumed an operator with limited scope then DSAC would be very high (and close to SAC) whereas if the competitor had a similar scope to BT DSAC would be much lower (and close to FAC/LRIC+). BT has chosen to use a certain scope for the hypothetical competitor – Ofcom has not assessed whether this scope assumption is appropriate (either in general or for a particular purpose).

3.45 Fourth, DSAC is unreliable (since it is not audited) and not transparent (since many of the DSAC costs are not calculated or published).

3.46 We think Ofcom should reject using DSAC and instead use a measure of cost such as FAC +X% (say FAC +30%). Whilst the choice of X will be somewhat arbitrary this is no worse than the arbitrary scope assumption that BT make to derive DSAC figures, particularly given the lack of theoretic or practical support for DSAC as a concept. Using a FAC+X% approach would have several clear advantages over DSAC:

- Ofcom rather than BT would set the key assumption driving the allowable price level
- Transparency will be increased since FAC data are available for more products than DSAC
- The data will be more reliable since FAC is audited whereas DSAC is not

3.7 Income from community fibre partnerships

3.47 Openreach operates a scheme (called community fibre partnerships[33]) whereby communities can pay Openreach in order to get FTTC rolled out in their community. Once the network is in place wholesale services are provided as in other areas.

3.48 This income will effectively reduce costs. Ofcom should take this into account both in assessing the cash flows and returns used to judge whether the fair bet has been honoured and also in assessing the costs of GEA and so wholesale prices.

4 Ancillary charges

4.1 In this section we comment on Ofcom's proposals for various ancillary charges:

- cablelink;
- co-mingling;
- tie-cables;

[33] https://www.homeandbusiness.openreach.co.uk/fibre-broadband/community-fibre-partnership

- AVCs; and,
- GEA service change charges.

4.1 GEA cablelink

4.2 In its March consultation Ofcom proposed that the Cablelink charges for 1G (£2,000 per connection) and 10G (£10,000) should be capped at CPI-CPI for the review period (i.e. flat in nominal terms). Ofcom claimed it did not have the cost information to set a cost-based charge control. TalkTalk in its response highlighted that Ofcom's approach allowed BT to substantially over-recover its costs since the likely costs were substantially lower than the prices – about [✂ - CONFIDENTIAL - ✂] (1G) and [✂ - CONFIDENTIAL - ✂] (10G). The fact that the 10G circuit price was £8,000 more than the 1G circuit even though the additional cost was only about [✂ - CONFIDENTIAL - ✂] was further clear evidence of excessive prices.

4.3 On 7 September, Openreach announced very large price reductions for Cablelinks: new prices of £790 for 1G (60% reduction); £1,800 for 10G (82%). Openreach trumpeted these as its initiative. A week later Ofcom published its consultation which reflected the new Openreach prices.

4.4 It appears that Openreach did not initiate the change – rather they decided to jump before they were pushed to try and garner unmerited credit and attempt to discourage Ofcom from setting genuinely cost-based charges. Ofcom must resist this since not only would it not serve consumers interests but it would also encourage more gaming by Openreach to set excessively high prices and not retain cost data.

4.5 We also note that Openreach suggested that the price reduction was a result of a different cost attribution to Cablelink[34]. This is inconsistent with our understanding that there is no specific attribution to Cablelink in the regulatory accounting data (since Openreach was unable to provide any cost information to Ofcom[35]).

4.6 Ofcom is proposing to set a cost based charge for Cablelink based on FAC costs. In particular Ofcom proposes to set initial charges in 2018/19 at its cost estimate and then cap charges going forward on a CPI–X% basis (setting X at 0%).

4.7 We agree with this overall approach but disagree with a number of elements.

4.8 Ofcom has proposed setting the initial charge at £500 to £790 (for 1G) and £1,000 to £1,800 (10G). The upper bound is based on Openreach's new prices. Ofcom do not describe how it has determined the lower bound. We do not agree with Ofcom's

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[34] Email of 7 September from Katie Milligan to TalkTalk: "*Following our discussion in the exec board to board this week, I wanted to share that we are announcing our new GEA cablelink prices today, which as promised are significant reductions, as we have revised our cost allocation approach on this product going forward*"

[35] See March Consultation Vol II §3.114 and footnote 120

approach. Ofcom should set the initial charge based on its best estimate of costs for two reasons.

- First, it is unsound to use Openreach's price as an estimate of Openreach's FAC costs since Openreach has very strong incentives to set prices above FAC costs. It is almost inconceivable that Openreach would set prices as low as FAC unless compelled to do so by price regulation.
- Second, though the provenance of the lower bound is unclear the figures (£500 and £1,000) look unreliable – for example:
  - there is no explanation of why the costs are so much higher than the costs TalkTalk provided [✂ - CONFIDENTIAL - ✂] and [✂ - CONFIDENTIAL - ✂])
  - Ofcom have not explained how the figures relate to the cost data Openreach provided
  - the £500 additional cost for 10G versus 1G is inconsistent with TalkTalk's evidence that the difference is about [✂ - CONFIDENTIAL - ✂].

4.9 Ofcom must review the data from Openreach and TalkTalk (and if necessary other sources) and come to its own reasoned and transparent judgement as to the likely cost including (if appropriate) an assumption for how a new supplier is likely to reduce costs[36]. In particular, and in any event, the difference in price of 1G and 10G should equal the incremental cost difference between 1G and 10G in order to ensure efficient choice between these potentially substitutable products.

4.10 In order that TalkTalk and other stakeholders can properly contribute to determining the costs Ofcom should provide more transparency particularly around what costs are recovered from the Cablelink charge and which form GEA rental charges e.g. are layer 2 switch (L2S) costs recovered from GEA rental or GEA Cablelink? Otherwise there is a risk of yet more double recovery.

4.11 Regarding the X we disagree with the proposal to set the X at 0% (i.e. a flat real price cap). Efficiency improvements and unit price reductions are likely to result in costs reducing over time. A suitable proxy for the X could be the underlying cost decrease for tie cables (which similarly connect between Openreach equipment and CP equipment within an exchange, albeit using copper rather than fibre). The underlying cost decrease for tie cables are –3.8% (which can be seen from the X applied in 2020/21[37]). Arguably the X could be greater than 3.8% since (unlike for tie cables) the growth in Cablelink volumes will lead to scale economies and lower unit costs.

4.12 We consider that CPs who have purchased circuits in the past are granted a refund. The normal commercial model for purchasing a circuit is to pay a rental charge

[36] Openreach have claimed they are changing suppliers (see Openreach Response to Vol 2 §131). It is likely that a change in supplier will lead to reduced costs (or higher quality)

[37] the X in other years reflects other changes aside of underlying cost changes (e.g. alignment of prices with costs)

possibly alongside a connection charge so that all or most of the circuit cost is recovered through rental. In fact almost every major circuit charge recovers costs through rental charge e.g. MPF, WLR, GEA, Ethernet leased lines, tie cables, voice interconnection circuits. If Cablelink circuits were charged on a similar basis then the introduction of cost-based prices would result in the costs of existing circuits reducing. However, because Openreach do not have a Cablelink rental charge the costs of existing circuits will be unaffected. This could be addressed by requiring a refund on existing circuits[38]. Openreach's approach of only charging a (very high) connection charge is effectively a means of circumventing and diminishing the effect of regulation.

4.13 We note that in its submission Openreach claims that Cablelink costs are "*very uncertain*"[39] due to the use of a new supplier, the use of more 10G and unclear port utilisation and consequently there should be no charge control. This is nonsense. The use of more 10G will not create any uncertainty since both the 1G and 10G prices will be separately charge controlled at cost. Whilst the other two factors may result in some cost uncertainty it will be small since it only relates to a portion of the overall cost and it is no more than is experienced for other products Openreach provides.

4.2 Co-mingling

4.14 Ofcom have revised their estimates of co-mingling costs downwards by about 45%[40]. This is an exceptionally large change both in relative terms (the initial 2019/20 cost estimate that Ofcom made in March was 80% above the revised cost) and absolute terms (a £40m cost over-estimation[41]).

4.15 The reason for the over-estimation was that[42]: BT has double recovered some costs by recovering them once in up-front charges and again in on-going rentals; certain volumes were significantly understated resulting in over-estimation of unit costs and so prices; APCA costs were over-attributed to co-mingling (from FTTC).

4.16 This raises a number of issues that Ofcom should consider:

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[38] This could be derived as follows. For a 1G circuit with a previous connection charge of £2,000. Say the new connection charge is £400. For a circuit that was installed in 2015/16 and assuming a 10 year life then there were 3 years at the higher price (2015/16 – 2017/18) and 7 years at the lower price (2018/19 – 2024/25). The adjusted connection charge should be 3 / 10 x £2,000 + 7 / 10 x £400 = £880. The refund would be £2,000 less £880 = £1,120

[39] see Openreach Response to Vol 2 §131

[40] In the March 2017 consultation prices rose by about 90% to align with forecast costs in 2019/20. In this Sept 2017 consultation the prices rose by 5%.

[41] In the 2015/16 RFS the total revenue was £46m and FAC £71m. However the presented FAC figure may not be a reliable estimate of the genuine cost. If the cost was £50m then the cost over-estimate would be £40m

[42] Of the total error the double recovery was about 30% of the total; volume mistake 40% and APCA attribution 30%

- Why were these errors not spotted earlier? A 90% increase[43] in the unit price of a mature and stable product should have raised a red flag for Ofcom (and to be fair should have raised a red flag within TalkTalk)
- Have the costs used to set prices in previous WLA reviews been similarly exaggerated ? If so, how should this be addressed ?
- Is this double recovery occurring for other products? It has happened for tie cables as Ofcom describe in this consultation. It also happened previously for excess construction costs for leased lines whereby the cost was recovered up front (in excess construction charges) and was capitalised and recovered again in rental charges[44]
- Was the data BT provided reliable and has BT complied with its regulatory accounting obligations? For instance, BT double recovered certain costs (e.g. survey and provision) in up-front charges and again in rental charges. Was BT aware of this obvious error, and was it intentional? If Ofcom wants BT to comply with these key obligations then, when BT breaches, there must be robust enforcement.
- What changes should Ofcom adopt to ensure this does not recur? Are the regulatory accounts fit for purpose? Do the regulatory accounting principles (RAP) need to be amended? Is the audit reliable?

4.17 Regarding the corrections that Ofcom has proposed, we in general agree with them since they implement obviously correct underlying principles e.g. costs should only be recovered once. However, it is very difficult for TalkTalk (and we imagine other CPs) to engage in the detail since the description is limited and it relies to a large degree on terminology to which only BT and (possibly) Ofcom understand.

4.18 Lastly, we note that as a result of this correction more APCA costs are attributed (in the first instance) to GEA. Ofcom then explains that it considers that these costs are common and so recovers them from both GEA and MPF charges. It is not clear why APCA costs are common to MPF. According to BT's 2016 AMD APCA costs are relevant to co-mingling and GEA DSLAM and cabinets only.

> *The base apportions capital work in BT TSO (CoW ACPA) relating to racks, power and ventilation.*
>
> *The base apportions to PG132B (LLU Co-mingling Recurring Costs (OR)), PG136A (LLU Co-mingling Surveys) and PG953C (GEA DSLAM and Cabinets).*

4.19 Thus, none of the APCA cost that is not attributed to co-mingling is common to MPF – MPF does not require racks, power and ventilation. Accordingly, all the non-co-mingling APCA cost should be recovered from GEA.

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[43] from 2017/18 to 2020/21

[44] Business Connectivity Market Review Statement March 2013 §19.131. Also occurred for Ethernet circuits (§20.232)

4.3 Tie cables

4.20 Ofcom have revised their estimates of tie cable costs downwards by about 10%. This comprised two changes that decreased costs by about 20% (adjust component volume uplift and base year adjustment) and two changes that increased costs by about 10% (remove cost reduction and adjusted disposal value).

4.21 The largest change was a 17% cost reduction for base year adjustment to reflect that BT was double recovering certain costs by recovering them in up-front charges and again in rental charges. This is the same basic error of double recovery as for co-mingling. As we describe above, as well as correcting this error Ofcom should consider how to address past failure (e.g. through enforcement) and also what action it should take to ensure this does not happen again.

4.22 We also note that it appears that Ofcom is proposing to make an allowance for stranded assets through its approach to disposals (CCC §4.36). We do not consider that this is appropriate.

4.4 Aborted visit charge (AVC)

4.23 In its consultation, Ofcom refers to TalkTalk's comments regarding the AVC price and in particular that the AVC price should be reduced to the FAC AVC cost (around £25) or the excess profit on AVCs should be deducted from the cost of other products (CCC §4.93).

4.24 In response, Ofcom reiterated that they do not consider that a charge control should be applied. Ofcom repeats the point it made in the March consultation that a price above cost will discourage missed appointments and raises a number of new points:

- it would be difficult to observe the opportunity cost of a missed appointment
- consumers are protected by other general SMP remedies
- CPs can raise a dispute if they wish to challenge the charge

4.25 We think these new points do little or nothing to justify not imposing a charge control:

- The cost (or opportunity cost) of a missed appointment is no more difficult to assess than the cost of a repair or provision job of a certain length. An AVC is simply another use of engineering resource (albeit a rather inefficient one)
- The other SMP remedies do not effectively protect consumers from excess charges since they do not prevent BT from over-recovering
- It is disappointing that Ofcom even raises the possibility of addressing this problem via a dispute. Raising a dispute is a waste of Ofcom's, CPs' and Openreach's resources when this matter can be resolved more quickly, effectively and with more certainty by setting a charge control. CPs should not have submit such disputes to demonstrate that the dispute approach is plainly inefficient

4.26 Also, Ofcom has not responded to TalkTalk's suggestion that if the charge is not set at cost then the excess profit (i.e. revenue less FAC costs of AVC including WACC) should be deducted from the cost of other products by reducing those products' common cost allocations. Such a change would be unequivocally good for consumers by reducing prices closer to cost and not threatening BT's overall cost recovery. If Ofcom wishes not to adopt such an approach then they should engage with this option and clearly justify their position.

4.27 Lastly, we note that the FAC cost of AVC is capitalised whilst the charge is a one-off. We agree with Ofcom that this cost should not be capitalised. Given BT's errors elsewhere where BT has capitalised costs that were recovered upfront and recovered these costs again against rental charges we would ask Ofcom to confirm that this capitalised AVC cost is not recovered against another rental charge.

4.5 Charges for GEA service changes

4.28 Ofcom has proposed that certain GEA service change charges (in particular, GEA bandwidth modification, GEA Cancel/Amend/Modify and VLAN modification that apply to 40/10) are priced at FAC and that the estimated FAC is the same as GEA CP-CP migration (which is estimated to reduce to about £6 in 2020/21[45]) since they all involve only software changes. We have a number of concerns about this.

4.29 The charges for these services are not based on the FAC costs attributed in the RFS. This will lead to over-recovery[46].

4.30 Ofcom say that these services are attributed costs but that the costs (and presumably revenues) are aggregated with "*other smaller Wholesale Local Access ancillary services (aside from the CP to CP migration service).*" Ofcom must require BT to identify the FAC attributed to the GEA service changes. It must then either:

- Base the GEA service change charge on the attributed cost; or,
- Deduct the excess margin between charge and cost (i.e. revenue less FAC costs) from the cost of other products by reducing those products' common cost allocations

4.31 If BT is unable to identify the cost then Ofcom should assume that it is zero.

4.32 Ofcom should also ensure that the cost attributed to these GEA service changes (within other WLA ancillaries) are not recovered from other WLA ancillary services.

[45] This is based on the clarification Ofcom provided in October. In the September consultation Ofcom said it would align GEA amend charges with GEA bandwidth modify charges (which is currently priced at currently £11, £8.02 in 2018/19 and then CPI-18.0% and CPI-2.8% results in about £6 in 2020/21). Ofcom have clarified that the GEA bandwidth modify charge is based on the GEA CP-CP migration FAC

[46] If attributed cost is greater than charge then will lead to under-recovery. However, this is unlikely for two reasons. First, Openreach will point this out to Ofcom and insist the charge is increased to reflect attributed cost. Second, BT seems in the past to have under-attributed costs to low volume, nascent services

4.33 More generally, Ofcom must develop and implement a robust test to ensure that its pricing proposals do not lead to cost-over recovery. It should transparently explain this test in its documentation. Furthermore, Ofcom must be aware that if it allows over-recovery where costs are not disaggregated then it creates a harmful incentive that discourages Openreach from providing sufficiently granular and accurate cost data.

4.34 We also consider that the FAC estimate for CP-CP migration (used to set GEA service change charges) is too high. Since this is a software-only activity there are large economies of scale. The FAC in the RFS has reduced from £10.34 in 2015 to £5.74 in 2017[47] as volumes grew rapidly. Given the strong forecast growth in GEA volumes the FAC might be £3 to £4 in 2020/21 not the £6 that Ofcom has proposed.

4.35 Ofcom should review whether the common cost allocation to GEA CP-CP migration is reasonable. It is currently about 2.4 times LRIC[48] which appears excessive.

4.36 Lastly, Ofcom should clearly specify which services are capped at £6. We believe that it should be the 40/10 versions of the following products:

- Cancel/Amend/Modify – CRD (changes to order)
- Cancel/Amend/Modify – regrade (changes to DLM either pre-install or in-life)
- Bandwidth modify – change from (e.g. 40/10 to 80/20)
- Change in DLM profile[49]
- VLAN modification ("*VLAN moves applied to GEA Cablelink Modify transactions*")

4.37 The bulk versions of each of the above services (i.e. rather than singletons) should be charged at a discount to the singleton price.

4.38 It seems that the prices for these services are currently significantly above cost. Given this we think it is important that these margins are included in Ofcom's assessment of Openreach's overall cash flows and returns on its FTTC investment and whether the fair bet has been 'honoured'. Without including these margins (and those on other GEA services such as Cablelink) the returns Openreach will earn on its investment will be underestimated.

4.39 In a similar vein we are concerned about the charges and cost recovery for Visit Assure and Fibre Broadband Boost. Ofcom must ensure that the cost recovered

[47] 2015 – 54k, £10.34 [2016RFS p43]; 2016 – 165k, £7.57 [2017RFS p36]; 2017 – 398k, £5.74 [2017RFS p33]

[48] For GEA CP-CP migration FAC is £6 and LRIC is about £2.50 (derived from March consultation Table 4.6). Common cost allocation is FAC less LRIC

[49] TalkTalk is currently incurring significant charges from Openreach to change the DLM profile of GEA customers to improve the stability and speed of their connections. It is not clear what the name of this charge is.

from these services is set to equal the charge. If not then it will lead to systematic over-recovery. There are two approaches Ofcom could adopt:

- Ideally derive a FAC-based charge
- If no cost is attributed to these services then adjust downwards the costs attributed to other products by the revenue for these services

5 Regulatory accounting review

5.1 The significant errors in the cost data BT provided to Ofcom on co-mingling and tie cables reveal in our view a significant problem that warrants a more fundamental look at whether the current regulatory accounting arrangements are fit for purpose.

5.2 We think Ofcom should consider:

- Why it is that the vast majority of inappropriate attributions and errors in the regulatory accounts are in BT's favour ?
- Have the costs used to set prices in previous WLA reviews been similarly exaggerated ? If so, how should this be addressed ?
- Whether further audits are required to look for further examples of the errors we have seen – in particular whether any costs are double recovered and whether the cost recovery approach matches the charging approach (e.g. if an activity is recovered in up front charges the cost should be capitalised and visa-versa)
- Whether BT has complied with its regulatory accounting obligations?
- Whether the regulatory accounts are fit for purpose ? Do the regulatory accounting principles (RAP) need to be amended ? Is the existing audit reliable?
- How it can develop and implement a robust test to prevent over-recovery of costs as it was proposing to allow on AVC and GEA service changes. This is particularly important where it sets prices that are not based on known attributed costs.