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Ofcom Consultation; Wholesale Charges for Number Translation Services and Premium Rate Services NTS Retail Uplift Charge Control and PRS Bad Debt Surcharge

Submission for 4D Interactive Limited ("4D")

Dear Catherine

Background of 4D

4D has been interconnected with BT since 2001 and has been trading within the phone paid sector since 1993. As one of the fastest growing companies in the UK, 4D has a strong presence in both premium rate and national rate telephony both in its own capacity and on behalf of its 100 customers. In its response to this consultation, 4D is doing so primarily in its role as a terminating communication partner ("TCP") but will also be drawing on its experience and market knowledge as both a service provider and information provider as well. According to research released recently by PhonePayPlus, 4D and its customer base represent some 12% of the 0871 market in the UK. It is also a member of AIME and the PRA and is represented on the UKTCA.

General

4D does not believe it is appropriate at this stage, nor for this consultation to attempt to change the OCCN processes already agreed to and in place. 4D agrees with the general principles of the Bad Debt Surcharge, however, it has concerns as to how it has been defined, what the policies of recognition of bad debt are and how it has been calculated including what other assumptions have been made to derive a value. None of these have been disclosed. We also note that inherently all calculations will be based on BT's own, historic and current data when it is apparent this will be distorted by the current economic recession and historic problems with scams on PRS. All recent current data from PPP suggests that problems with PRS on voice have substantially reduced and represent only a small percentage of PRS complaints and recent financial data suggests that the economic outlook is improving. Therefore in our view there are very strong reasons to believe that

the levels going forward will be much lower than those looking back and this should be the basis in setting the surcharge.

Our other principal concern is to the relationship between the Bad Debt surcharge and BT's current obligations around artificially Inflated traffic ("AIT"). Again we feel it would be inappropriate for BT to attempt to recover through the bad debt surcharge "missed" or "overlooked" AIT. In these instances, where the issue is down to a small number of very active TCP's, separate recovery mechanisms should be applied. Instances of bad debt as a result of deliberate fraud or misleading promotions etc. should be recovered through the appropriate source which includes referral to PhonePayPlus for investigation, fine and compensation.

Whilst we agree in principle with a setting of the charge for a four year period before further review it would be wholly inappropriate to set an astonishingly high level of surcharge now, at what most commentators would agree is the bottom of the economic cycle and have this penalty hanging over the industry for the next four years before further review.

Whilst there is no definition of bad debt it is difficult to comment on a proposed level. From our experience a bad debt level of almost 10% of PRS is on the face of it staggering. This is at odds with the commercial data we have where we see bad debt levels albeit through different payment mechanisms in the region of 1.5-2.0%. Talking to colleagues in the industry this is the common view and there appears surprise at how this can have been calculated. A bad debt level of almost 10% calls into question the reliability and reasonableness of the methodology used to calculate it as well as the in-house processes to manage, mitigate and record it.

To give more clarity as to how the data has been calculated we would be interested to understand more about:

- How has VAT been treated? Our expectation is that this should not form part of the bad debt calculation.
- Have BT sought to mitigate any bad debt by making such provisions through its accounts on a specific basis so as to achieve a degree of corporation tax relief?
- To what extent has BT's actions on AIT also flexed over the same review period – have they improved or lessened their efforts in this regard?
- Where an invoice has been part paid how have payments on account been allocated?
- What analysis has been done on the reasons for the bad debt; hardship, dispute, dissatisfaction, opportunity, poor credit control? Does the bad debt distinguish between these and have assumptions been made in respect of these to determine apportionment between

- calls costs, the fixed line element of the bill in dispute and allocation between NTS, PRS and geographic calls?
- What analysis has been done in reviewing the concentration of bad debt to each price tariff, Service Providers or type of service? There is no attempt to target the surcharge towards those that have caused it. We would welcome greater analysis so that the surcharge can be applied more equitably. Our expectation is that the PRS bad debts will have certain core characteristics and trends that require specific action rather than a levy across all TCPs and by definition at SPs and IPs as a result.
 - How has BT sought to mitigate this problem that has evidently been sustained over a number of years? How proactive have they been to get to the root of the causes? From our own experience we have never been contacted by BT to highlight customers that have not paid their debts and if they had we would have immediately barred them from using our service.
 - As BT will also look to amend their commercial relationships across all TCPs for “off net” (that is non BT originated traffic) along the same lines as they are looking to have agreed for BT originated traffic through OFCOM’s agreement what further action can be taken to prevent over recovery or additional penalties being borne by TCPs as a result of this?

Questions:-

Question 1: Do you agree that RPI is the best inflation index for the proposed charge control? **Agree**

Question 2: Do you agree that an RPI-X control is the appropriate form of charge control for NTS Retail Uplift? **Agree**

Question 3: Do you agree that a four year duration for the proposed NTS Retail Uplift charge controls is appropriate? Given the volatility shown to date and without further detailed information from BT **we would like to see this tested and reviewed annually until such time as confidence can be given that BT are both correctly treating bad debt as bad debt and applying reasonable endeavours to limit it in an appropriate manner.**

Question 4: Do you agree that there should be a single price control basket for all NTS calls including freephone calls? **No comment**

Question 5: Do you agree that a glide path, rather than a one-off adjustment at the outset of the control, is appropriate? **No comment**

Question 6: Do you agree that CCA FAC for NTS calls drawn from BT’s regulatory accounting system is the appropriate cost basis for setting the proposed charge controls? **No comment**

Question 7: Do you agree with how we have proposed to adapt the cost recovery principles we established in our 2005 Statement to current circumstances? **No comment**

Question 8: Do you agree with the way in which we convert BT's mean capital employed into an annualised cost? **No comment**

Question 9: Do you agree with the way we propose to handle retail costs to freephone calls? **No comment**

Question 10: Do you agree that we should use NTS call volumes to forecast costs and our forecast for these traffic volumes? **No comment**

Question 11: Do you agree with our proposed approach to efficiency? **No comment**

Question 12: Do you agree that we should assume a Cost Volume Elasticity of 0.25? **No comment**

Question 13: Do you agree with the way in which we have forecast 'normal' bad debt, in particular that it is reasonable to apply a CRR of 1 and no efficiency adjustment? **Bad debt has not been defined and nor is there any clarity on how it is recognised therefore we believe it is wholly inappropriate to be asked to form any opinion on this until the full information is available. We feel a separate consultation exercise should be performed once accurate data and a full agreement on the definition of bad debt has been made with industry.**

Question 14: Do you agree that we should retain the PRS Bad Debt Surcharge in its current form to recover bad debt specific to PRS calls? **We agreed with the general principles of the surcharge however there is not enough information on its definition. Following this there must be a robust test by Ofcom as to its 'reasonableness' and challenge where appropriate any assumptions made. As things stand the proposed levels are completely at odds with all other data provided by PPP and the industry and this apparent contradiction needs to be understood and explained and Ofcom need to effectively adjudicate based on all information an acceptable level of surcharge. We feel a separate consultation exercise should be performed once accurate data and a full agreement on the definition of bad debt has been made with industry.**

There is an inherent conflict as BT are producing the information on which the surcharge is based and will benefit from a high surcharge and therefore the need to have a strong and focussed review of this is clear. BT should be made more accountable for any levels above industry averages.

Question 15: Do you agree that a four year duration for the PRS Bad Debt Surcharge is appropriate? **No, we believe with proper definitions and transparent information this should be tested annually and against other economic and industry data to ensure it is consistent for the time being.**

Question 16: Do you agree with approach for the PRS Bad Debt Surcharge and in particular use BT's own bad debt and retail revenue information to inform our proposal? **Agree, but as 14 above because of the conflict it is important that the data be independently and objectively reviewed.**

Question 17: Can you supply any evidence or other insight about the incidence of bad debt on PRS calls and in particular whether the incidence of PRS bad debt has risen substantially in recent years? **PPP data clearly highlights the substantial reduction in voice complaints and our own data using different payment mechanisms suggests a level of less than 2%. We would also note that it is our policy to offer a refund to dissatisfied customers and therefore we are effectively being asked to subsidise other providers in the industry. Through the PPP compensation scheme customer have at present the ability to "double recover" but receiving compensation direct from PPP where complaints have been made through official channels and also through non payment (and non argument over this) by BT. An obligation must be placed on BT to ensure that where there is suspected misleading services, promotions or fraudulent behaviour the proper recovery process is followed. At present, whereby BT can pass on all bad debt to TCPs through to SPs and IPs BT is not incentivised to chase or recovery debts relating to PRS rigorously enough.**

Question 18: Do you agree that in these circumstances that a one-off adjustment to the PRS Bad Debt Surcharge at the outset of the control, rather than phasing it in over time is appropriate? **We would like to see the surcharge set at the correct level whatever that may be. The principle of the surcharge is right, but we have little confidence in the data as it stands partly because there is no definition to it but also because it contradicts all the information in the market.**

Conclusion

If the surcharge is introduced at the level proposed this would have a significant detrimental impact on 4D and our clients. At a time of economic crisis and declining PRS revenues across the whole industry this would undoubtedly lead to further contraction of the market with further job losses and economic hardship on individuals as a result. Where a small number of TCPs are causing damage to the industry as a whole and to consumers alike through unscrupulous business practices we feel strongly that BT should report, censure and penalise those TCPs in the first instance before looking to impose the bad debt surcharge "safety net" across the industry as a whole

Whilst it is unfair for BT to pick up a disproportionate element of this cost as a result of its open access given its market SMP, its is equally inappropriate to release BT of this burden at the expense of all TCPs for the torts of a small minority. This is neither fair, reasonable or proportionate and fails all tests of good regulation.

We remain highly sceptical and surprised that the level of PRS bad debt is as high as stated. Whilst we accept the general principles of the surcharge we would like to see greater transparency around its calculation and greater accountability placed on BT to justify the levels. We would also welcome the levels being stress tested against other non BT information provided by industry and PPP. Then and only then do we feel it is appropriate to ask industry to opine on some of the issues raised through a further consultative process. Looking forward we would also ask that Ofcom look at ways that the surcharge could be more targeted towards those responsible as this is evidently in everyone's best interests.

In the meantime we would like to see the current level being fixed until such time as the surcharge be satisfactorily agreed.

Yours sincerely,

A handwritten signature in black ink that reads 'Simon Newton'.

Simon Newton
Financial Director