



BT's response to Ofcom's consultation document

“Financial reporting for standalone landline telephone services”

23 May 2017

Comments on this response should be sent to:

Tom James, Head of Competition Finance via email at Tom.James@bt.com

Contents

1	Introduction and executive summary	3
2	BT's comments on Ofcom's proposals for regulatory financial reporting	4
	Financial information to be provided privately	4
	Financial information to be published	5
3	BT's comments on the draft legal instruments	10
4	Response to specific consultation question	11

1 Introduction and executive summary

- 1.1 On 28 February 2017, Ofcom published a consultation on the review of the retail market for standalone landline telephone services (RMSLTS Consultation). British Telecommunications plc (BT) responded to the RMSLTS Consultation on 19 May 2017.
- 1.2 On 25 April 2017, Ofcom published a consultation on proposals for financial reporting for standalone landline telephone services (FRSLTS Consultation). This is BT's response to the FRSLTS Consultation. It should be read in conjunction with BT's response to the RMSLTS Consultation, and is without prejudice to our submissions relating to Ofcom's proposals for market definition, finding of SMP and proposed SMP remedies, set out in our response of 19 May 2017.
- 1.3 BT agrees with Ofcom's proposals in relation to financial information to be provided privately, subject to BT's response to the RMSLTS Consultation of 19 May 2017.
- 1.4 BT agrees with the proposed requirement to publish a statement confirming its compliance with the requirements under Conditions 3.1-3.3.
- 1.5 Ofcom's proposals requiring BT to publish volume information on standalone fixed voice (SFV) services and the compliance statements set out on p.29-31 of the FRSLTS Consultation, are disproportionate, not objectively justifiable nor necessary, in the context of the retail market for standalone landline telephone services, and would involve disclosing BT's commercially sensitive information to the detriment of effective competition.
- 1.6 Ofcom's powers to impose SMP remedies in relation to the provision of retail services are limited by section 91(6) of the 2003 Communications Act (the Act), as well as by sections 3(3) and 47(2) of the Act. BT considers that Ofcom's proposals in relation to financial information to be published, do not satisfy the above provisions for the reasons set out in our response below.
- 1.7 The information set out in the Annex to Condition 3 (p.21 of the FRSLTS Consultation) and in the Annexes to the Direction relating to the publication of Compliance Statements (p.29-31 of the FRSLTS Consultation) should only be provided to Ofcom privately.
- 1.8 Providing the requested information privately to Ofcom would ensure Ofcom has the *"information necessary to make informed regulatory decisions, monitor compliance with SMP conditions, ensure that those SMP conditions continue to address the underlying competition issues, and investigate potential breaches of SMP conditions and anti-competitive practices."*¹

¹ Ofcom, Regulatory Financial Reporting Statement, 20 May 2014 (2014 Regulatory Reporting Statement), paragraph 2.28.

2 BT's comments Ofcom's proposals for regulatory financial reporting

Financial information to be provided privately

- 2.1 Draft “Condition 3 – Regulatory Reporting” set out Ofcom’s proposals in relation to financial information to be provided privately by BT, as follows:
- 2.1.1 Information set out in a template at the Annex to Condition 3, within 4 months of the end of each Financial Year (Condition 3.1 and template on p.21, FRS LTS Consultation):

	Column A BT Consumer	Column B All fixed voice services	Column C SFV services
1) Revenue excluding VAT (£m)			
Total revenue	X.X	X.X	X.X
Line rental	X.X	X.X	X.X
Call plans not included with line rental	X.X	X.X	X.X
Out-of-plan calls	X.X	X.X	X.X
Other fixed voice revenue	X.X	X.X	X.X
Other revenue	X.X	X.X	X.X
2) Wholesale costs (£m)			
Total wholesale costs	X.X	X.X	X.X
Wholesale fixed voice line rental costs	X.X	X.X	X.X
Wholesale fixed voice call costs	X.X	X.X	X.X
Other wholesale fixed voice costs (if any)	X.X	X.X	X.X
Other wholesale costs	X.X	X.X	X.X
3) Gross margin (£m)			
Gross margin	X.X	X.X	X.X
4) Retail costs (£m)			
Total retail costs	X.X	X.X	X.X
Total SG&A	X.X	X.X	X.X
- SG&A internal	X.X	X.X	X.X
- Cost type 1	X.X	X.X	X.X
- Cost type 2	X.X	X.X	X.X
- etc	X.X	X.X	X.X
- SG&A external	X.X	X.X	X.X
- Cost type 1	X.X	X.X	X.X
- Cost type 2	X.X	X.X	X.X
- etc	X.X	X.X	X.X
Total cost of sales	X.X	X.X	X.X
- Internal cost of sales	X.X	X.X	X.X
- Cost type 1	X.X	X.X	X.X
- Cost type 2	X.X	X.X	X.X
- etc	X.X	X.X	X.X
- External cost of sales	X.X	X.X	X.X
- Cost type 1	X.X	X.X	X.X
- Cost type 2	X.X	X.X	X.X
- etc	X.X	X.X	X.X
Total other retail costs	X.X	X.X	X.X
- Cost type 1	X.X	X.X	X.X
- Cost type 2	X.X	X.X	X.X
- etc	X.X	X.X	X.X
5) Net margin (£m)			
Net margin	X.X	X.X	X.X
6) Volumes of lines and calls			
Number of fixed voice lines (thousands)	X,XXX	X,XXX	X,XXX
- Number of gross additions for SFV lines	X,XXX	X,XXX	X,XXX
- Number of gross losses for SFV lines	X,XXX	X,XXX	X,XXX
- Due to ceased lines	X,XXX	X,XXX	X,XXX
- Switched to BT broadband bundle	X,XXX	X,XXX	X,XXX
- Migrated to BT Basic	X,XXX	X,XXX	X,XXX
- Switched to another CP	X,XXX	X,XXX	X,XXX
Total volume of fixed voice calls (thousands of minutes)	X,XXX	X,XXX	X,XXX
- Included with line rental	X,XXX	X,XXX	X,XXX
- Call plans not included with line rental	X,XXX	X,XXX	X,XXX
- Out-of-plan calls	X,XXX	X,XXX	X,XXX

- 2.1.2 In relation to the template provided to Ofcom, the provision of (Condition 3.2):
- (a) an explanation of source data used in calculating the data inputted in each row of the template;
 - (b) the Regulatory Accounting Methodology for the purposes of preparing the data inputted in columns B and C of the template;
 - (c) for each Subsequent Financial Year, a description of any changes to the Regulatory Accounting Methodology in comparison to that of the previous Financial Year, including reason and impact of each of the changes on the figures, by setting out the figures that would have been presented in the previous Financial Year in accordance with the revised Regulatory Accounting Methodology; and
 - (d) a reconciliation statement of the data in Column A with information published for BT Consumer in BT Annual Report.
- 2.1.3 The provision of an assurance statement by the Regulatory Auditor in relation to the template, in accordance with Conditions 3.3 and Conditions 3.3A-3.3D.

BT's comments

- 2.2 BT agrees with Ofcom's proposals in relation to financial information to be provided privately, subject to BT's response to the RMSLTS Consultation of 19 May 2017.

Financial information to be published

- 2.3 Ofcom's proposals in relation to financial information to be published by BT, include:
- 2.3.1 Information supplied under heading 6 of Column C of the template at the Annex to Condition 3, within 4 months of the end of each Financial Year (Condition 3.4);
 - 2.3.2 A statement confirming that BT has provided to Ofcom the information required under Conditions 3.1-3.3 (Condition 3.5); and
 - 2.3.3 Compliance Statements set out in "Draft Direction under sections 49 and 49A of the Communications Act 2003 and Condition 2.7A relating to the publication of Compliance Statements", as per the three templates on pages 29-31 of the FRSLTS Consultation (reproduced for ease of reference below).

1. Compliance summary

		Period	20XX/20XX+1	Notes
Basket total	Condition X.xx	CPI	X.XX%	
		X	X.XX%	
		Controlling percentage (CPI-X)	X.XX%	
		Prior year Revenue	£x,xxx	
		Weighted revenue change made	£x,xxx	
		Weighted % price change made	X.XX%	
		Complies	True/False	
Single charge category 1	Condition X.xx	CPI	X.XX%	
		X	X.XX%	
		Controlling percentage (CPI-X)	X.XX%	
		Price ceiling	X.XX%	
		Complies	True/False	
Single charge category 2	Condition X.xx	CPI	X.XX%	
		X	X.XX%	
		Controlling percentage (CPI-X)	X.XX%	
		Price ceiling	X.XX%	
		Complies	True/False	

2. Compliance detail

Redacted

Period: 20XX/20XX+1

Basket 1

CPI	X.XX%
X	X.XX%
Controlling percentage (CPI-X)	X.XX%

Basket	Revenue weight			Prior period average price				Current period average price				Average price change x Revenue weight	
	Average price	Volume	Revenue	Initial price	Price change 1	Price change 2	etc	Average price	Initial price	Price change 1	Price change 2	etc	Average price
Days in year				x	x	x	x		x	x	x	x	
Service 1	x,xx	x,xxx	£x,xxx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx
Service 2	x,xx	x,xxx	£x,xxx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx
etc	x,xx	x,xxx	£x,xxx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx	x,xx
Total			(A)£x,xxx										(B)£x,xxx
Percentage change			X.XX% (B/A)										

Single change – service X

	Period 1	Period 2	Period 3
CPI	X.XX%	X.XX%	X.XX%
X	X.XX%	X.XX%	X.XX%
Controlling percentage (CPI-X)	X.XX%	X.XX%	X.XX%
Price ceiling	X.XX	X.XX	X.XX
Prices charged during period:			
- start of period	X.XX	X.XX	X.XX
- price change 1 (date)	X.XX	X.XX	X.XX
- price change 2 (date)	X.XX	X.XX	X.XX
- etc	X.XX	X.XX	X.XX

BT's comments

2.4 In summary:

- 2.4.1 BT does not agree with the proposed requirement to publish the information supplied to Ofcom privately under heading 6 of Column C of the template to Condition 3.
 - 2.4.2 BT agrees with the proposed requirement to publish a statement confirming its compliance with the requirements under Conditions 3.1-3.3.
 - 2.4.3 BT does not agree with the proposed requirement to publish the compliance statements as per the three templates annexed to the Draft Direction (p.29-31 of the FRS LTS Consultation). Instead, BT proposes to provide a non-redacted version of those templates privately to Ofcom.
- 2.5 Ofcom's powers to impose SMP remedies in relation to the provision of retail services are limited by section 91(6) of the Act, as well as by sections 3 and 47 of the Act. BT considers that Ofcom's proposals in relation to financial information to be published, do not satisfy the above provisions for the reasons set out in our response below.
- 2.6 Section 91 of the Act confers on Ofcom the power to impose SMP conditions about regulation of services to end users. Sub-section 5 provides:
- "The SMP conditions authorised by this section are conditions imposing on the dominant provider such regulatory controls as OFCOM may from time to time direct in relation to the provision by that provider of any public electronic communications service to the end-users of that service."*
- 2.7 Sub-section (6) provides:
- "Where OFCOM set a condition which is authorised by this section and imposes regulatory control on tariffs or other matters to which costs are relevant, they shall also set, and apply to the dominant provider, an SMP condition which requires him, to the extent that they consider it appropriate—*
- (a) *to use such cost accounting systems as may be determined by them;*
 - (b) *to have the use of those systems audited annually by a qualified auditor; and*
 - (c) *to publish an annual statement about compliance by the dominant provider with the obligations imposed by virtue of paragraph (a)."*
- 2.8 Ofcom recognises this limitation,² however it presents its proposal as the imposition of "retail cost accounting obligation" within its power.³ The information Ofcom proposes to require BT to publish under draft Condition 3.4 and the "Draft Direction under sections 49 and 49A of the Communications Act 2003 and Condition 2.7A relating to the publication of Compliance Statements", goes beyond what it is authorised to impose by virtue of section 91 of the Act, when regulating retail markets.
 - 2.9 Ofcom's proposals relating to publication of financial information do not meet the limitations set out in sections 3 and 47 of the Act. In particular, Ofcom's proposals requiring BT to publish volume information on SFV services and the compliance statements set out on p.29-31 of the FRS LTS Consultation, are disproportionate, not objectively justifiable and unnecessary, in the

² Paragraph 2.29 of the FRS LTS Consultation.

³ Paragraph 2.30 of the FRS LTS Consultation.

context of the retail market for standalone landline telephone services, and would involve disclosing BT's commercially sensitive information to the detriment of effective competition

- 2.10 Section 3(3) of the Act provides:

*"In performing their duties under subsection (1), OFCOM must have regard, in all cases, to—
(a) the principles under which regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed; ..."*

- 2.11 Section 47(2) of the Act provides:

*"That test is that the condition or modification is—
(a) objectively justifiable in relation to the networks, services, facilities, apparatus or directories to which it relates;
(b) not such as to discriminate unduly against particular persons or against a particular description of persons;
(c) proportionate to what the condition or modification is intended to achieve; and
(d) in relation to what it is intended to achieve, transparent."*

The requirement under draft Condition 3.4

- 2.12 The proposed requirement to publish the information supplied to Ofcom privately under heading 6 of Column C of the template to Condition 3 is disproportionate, not objectively justifiable nor needed, in that it would require BT to publish commercially sensitive information about volumes of lines and calls of SVF services to the detriment of effective competition, without any apparent benefit to the interest of citizens, consumers and competition. This particularly so as the target audience is not sophisticated communication provider customers and other stakeholders, with well-resourced financial reporting expertise, but rather customers who Ofcom considers are often elderly⁴ and stakeholders who support such customers, and who rely on Ofcom to ensure compliance and would therefore derive little or no benefit from publication.
- 2.13 Ofcom's rationale for requiring BT to publish the said information is "*that sufficient information should be published to enable stakeholders to: contribute to the development of robust regulatory decisions; review and challenge data on which those decisions are made; assist us in monitoring compliance and to intervene in a timely fashion when required; and have reasonable confidence that BT has complied with its SMP conditions.*"⁵
- 2.14 Ofcom's rationale for requiring publication (on top of the information being supplied to it privately), does not hold in the specific circumstances, of *ex ante* regulation at retail level, which must be robustly justified, in light of insufficiency of wholesale regulation and competition law.⁶
- 2.15 As far as stakeholders' "contribution to the development of regulatory decisions" and the "review and challenge of data on which those decisions are made", to the extent information is required to be published to inform future market reviews, Ofcom can if appropriate publish the information in the context of such market reviews, including via calls for input. As far as

⁴ Paragraph 1.7 of the RMSLTS.

⁵ Paragraph 2.1 of the FRSLTS Consultation, and paragraphs 2.29-2.41 of the 2014 Regulatory Reporting Statement.

⁶ Commission Recommendation of 9.10.2014 on relevant product and service markets, C (2014) 7174 (at para.18).

“assisting Ofcom in monitoring compliance and intervening in a timely fashion” and “having reasonable confidence in BT’s compliance”, the stakeholders here are primarily consumer advocate bodies and retail residential customers, which are generally less able and/or less likely to assist Ofcom in monitoring compliance.

- 2.16 The lack of justification for requiring publication is particularly evident in relation to the volumes information supplied to Ofcom privately as part of the Annex to Condition 3. Information at the proposed level of granularity is not published for any other regulated markets (other than in total). The proposed disclosure is not required to demonstrate compliance and would be detrimental to its legitimate business interests and effective competition.

The requirement under the draft Direction on Compliance Statements

- 2.17 In addition to the above, the information required in the Compliance Statements templates on pages 29-31 of the FRSLTS Consultation, is both disproportionate and not objectively justifiable nor needed, as it comprises information that is either:
- (i) in the public domain (or can be easily calculated from information in the public domain); or
 - (ii) commercially sensitive information, confidential to BT, the disclosure of which would harm BT’s legitimate business interests, and be detrimental to effective competition. In particular, information related to revenue (which Ofcom proposes to redact in the template on p.30, but does not propose to redact in the template on p.29). For the avoidance of doubt if BT’s proposal is rejected, the revenue information on the template on p.29 should also be redacted.

Proposal

- 2.18 All the information set out in the Annex to Condition 3 (p.21 of the FRSLTS Consultation) and in the Annexes to the Direction relating to the publication of Compliance Statements (p.29-31 of the RFSLTS Consultation) shall only be provided to Ofcom (in a non-redacted format) privately.
- 2.19 Providing the requested information privately to Ofcom would ensure Ofcom has the *“information necessary to make informed regulatory decisions, monitor compliance with SMP conditions, ensure that those SMP conditions continue to address the underlying competition issues, and investigate potential breaches of SMP conditions and anti-competitive practices.”*⁷

⁷ 2014 Regulatory Reporting Statement, paragraph 2.28.

3 BT's comments on the Draft legal instruments

- 3.1 BT's comments below on the Draft legal instruments, reflect our concerns above, and are without prejudice to BT's comments made in response to the RMSLTS Consultation of 19 May 2017.

Draft Condition 3 – Regulatory reporting

- 3.2 BT has no comments on draft Conditions 3.1-3.3D of the legal instruments, on p.18-19 of the FRSLTS Consultation, and the Annex to Condition 3.1, on p.21 of the FRSLTS Consultation.
- 3.3 BT does not agree with the proposed requirement to also publish the information supplied to Ofcom privately under heading 6 of Column C of the template provided in accordance with Condition 3.1. We therefore propose that draft Condition 3.4 is deleted from the final legal instrument.
- 3.4 BT has no comments on the requirement in draft Condition 3.5 to publish a statement confirming it has provided to Ofcom the information required under Conditions 3.1-3.3.
- 3.5 BT has no comments on the requirements stipulated in draft Conditions 3.6 (in relation to deficient information) and 3.7 (in relation to future directions).

Draft Direction under sections 49 and 49A of the Communications Act 2003 and Condition 2.7A relating to the publication of Compliance Statements

- 3.6 BT does not agree with the proposed direction set out in paragraph 10 of the Draft Direction requiring BT to publish for each of (a) the Residential Standalone Fixed Voice access services and (b) the Residential Standalone Fixed Voice call services markets, the Compliance Statements set out in the Annex to the Direction (pages 29-31), completed with the required information. BT instead will provide (un-redacted) versions of those templates privately to Ofcom for the reasons specified in our response above.

4 Response to specific Consultation question

- 4.1 Ofcom's consultation question:

"Do you agree with our proposals for BT's regulatory financial reporting? Please provide reasons and evidence in support of your views."

- 4.2 Subject to BT's response to Ofcom's RMSLTS Consultation, BT agrees with Ofcom's proposals for BT's regulatory financial reporting for information to be provided privately, as set out in draft Conditions 3.1-3.3D and the Annex on p.21 of the draft legal instruments.
- 4.3 For the reasons set out in our response above, BT does not agree with Ofcom's proposals for BT's regulatory financial reporting relating to information to be published, as set out in draft Condition 3.4, and the Draft Direction under sections 49 and 49A of the Communications Act 2003 and Condition 2.7A relating to the publication of Compliance Statements (Direction 10 and templates attached on p.29-31). BT will provide un-redacted templates privately to Ofcom instead.