

# APPENDIX 1: SPECIFICATION

## Background

Ofcom has recently been informed by BT that both the internal and external turnover for a range of services covered the Business Connectivity Market Review have previously been calculated using incorrect volume data. PwC (BT's auditor) is currently reviewing the corrected data as part of its annual audit of the 2008 regulatory financial statements (RFS's).

This data, both volumes and turnover, are key inputs to Ofcom's previous and current work developing leased line charge controls. There is also the potential for significant consequential effects on BT's cost attributions on other services and products. It is essential that the data used to model forward looking price controls is reliable and relevant and the disclosure of that information in the RFS's is robust.

We understand that BT will be restating its 2006/07 comparatives in the 2007/08 RFS's reflecting the updated calculations. The RFS's are the key source of information used by Ofcom and other stakeholders to assess BT's compliance with its cost orientation and non-discrimination obligations and these adjustments are expected to have a material impact in some markets.

## Objective

The purpose of this work is to prepare a report for Ofcom that, in summary, confirms that BT;

- has restated volume and revenue data for services provided from markets covered by the Business Connectivity Market Review in 2006/07 to a standard that can be confidently relied upon for use in the price control modelling work and by users of the RFS's and;
- that the volume data used is the most appropriate measure of relevant volumes and revenues in all cases.

## Outline of study

Given these significant corrections and implications on the leased line charge control work and other regulatory decisions, Ofcom wishes to commission a study that will provide:

- a) an assessment of the accuracy of the revised turnover calculations and supporting volume data (all relevant sources);
- b) an opinion on whether or not the recognition and measurement basis on which turnover is calculated for price control calculations and the RFS's is relevant, reliable and fit for purpose including a review of the options available;
- c) an appraisal of the capability of BT's source data systems and processes together (inc. checks and controls) to deliver reliable volume data and;
- d) if appropriate, recommendations for further quality improvements to the data used in setting leased line charge controls and changes to the regulatory financial reporting of the relevant markets.

## Scope

The study will cover the following markets and services:

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#	Market / technical area	Example services
<i>For RFSs and price control purposes:</i>		
1	Traditional interface symmetric broadband origination (up to and including 8Mbit/s)	Partial private circuits Radio Base Station Backhaul SiteConnect IPstream and Datastream symmetric products
2	Traditional interface symmetric broadband origination (above 8Mbit/s up to an including 155Mbit/s)	Partial private circuits SiteConnect
3	Wholesale trunk segments (all bandwidths)	Partial private circuits Radio Base Station Backhaul SiteConnect IPstream and Datastream symmetric products
4	Technical areas (Point of Handover)	Customer sited handover In span handover
5	Alternative interface symmetric broadband origination (all bandwidths)	Wholesale extension services Wholesale end to end extension service Backhaul extension services Backhaul network services Openreach backhaul network services
<i>For price control purposes:</i>		
	Volumes of point of handover links for PPCs by bandwidth (all bandwidths)	Currently not separately charged for

### Timing

It is important that this review should be completed as quickly as possible in order to minimise the delay to the introduction of leased line charge controls. Our expectation is that it should be possible to complete the work within a period of 4 weeks, although respondents should provide their own assessment of the time required.

A version of the final report will be made available to stakeholders and/or included in the leased line charge control consultation paper.

### Task descriptions

The following sets out in more detail our requirements from each of these tasks:

#### **Task A: An assessment of the accuracy of the revised turnover calculations and supporting volume data**

- To confirm that the restated 2006/07 turnover values and related volume data by wholesale service are free from material error, complete and faithfully represented.
- To confirm that the equivalent draft values for 2007/08 are equally reliable and comparable
- To review all the judgements, assessments and estimations carried out by BT in carrying out these calculations

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- To fully describe and explain any variances or differences found as part of this assessment

### *Outputs:*

- If appropriate, statements of turnover and volume data by service amended to reflect any findings of this study
- Commentary on methodology used to verify values
- Report on matters that should be brought to the attention of Ofcom
- Commentary on any material judgements, assessments and estimations including an assessment of options considered

### **Task B: An opinion on whether or not the recognition and measurement basis (inc. choice of volume definitions) on which turnover is calculated for price control calculations and the RFS's is relevant**

- To determine what the "definitions" of service revenues and volume measures, as used in preparing the RFS's, are and that these are applied consistently for external and internal sales.
- To compare and contrast, in consultation with Ofcom, the "definitions" above with the volume definitions required for price control monitoring purposes.
- To review alternatives and options considered by BT in determining the most appropriate recognition and measurement basis
- To verify that the RFS's and any supplemental information supplied to Ofcom for volumes and turnover are prepared using appropriate recognition and measurement basis
- To confirm that BT's interpretation and application of the relevant policies, principles and methodologies as set out in the RFS "Accounting Documents" is sound and reasonable.

### *Outputs*

- A statement comparing the definitions of services and volume measures supplied by BT with the appropriate measure for price control and RFS purposes
- An opinion on alternatives available and BT's selection process

### **Task C: An appraisal of the capability of BT's source data systems and processes to deliver reliable volume data**

- To provide a view on the adequacy of BT's systems and processes in generating reliable and relevant volume data for 2007/08 for the RFS's and price control modelling.
- To provide an assessment of the capabilities of BT's systems and processes in providing reliable data in the future and thoughts on possible improvements
- To describe and comment on BT's checks and controls used to ensure the volume data is reliable

### *Outputs*

- A report setting out the strengths and weaknesses of BT's data gathering and validation systems and processes to deliver reliable data

### **Task D: Consider ways for further quality improvements**

- Propose ways in which any identified deficiencies found during the course of this study can be addressed by BT
- Propose, if necessary, new reporting and information requirements that BT can prepare for Ofcom that would enhance the transparency and confidence in BT's internal transfer charge calculations.

### *Outputs*

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- A report setting out recommendations for improving any aspect of BT's systems, processes, methodologies and statements related to this topic.

It is expected that this study will have full access to all relevant BT staff, documentation and systems. BT is also preparing for Ofcom a report detailing the background to the issue, rationale and description of the new methodology and explanations of the calculation process. This report will be available to the successful Thought Partner.

Respondents should therefore demonstrate that they possess the necessary skills and expertise to deliver the study, or indicate where it may be necessary to bring in skills from third parties.

Respondents must recognise that their conclusions will come under close scrutiny from stakeholders and may be subject to appeal. It is essential that the conclusions from any review are robust and capable of withstanding challenge. The final report should be addressed to Ofcom and will be published as part of the leased line charge control consultation.

### Additional information:

As an indication of the scope of this work, the table below indicates the number of services covered by this study by product type. We do not have sufficient information at this time to indicate the number of site connect services although this is a relatively small group of services compared to PPC's.

	Total	Rentals			Un- defined	Conn- ections
		Main link		(Local) ends		
		Fixed	Variable			
<i>Traditional interface</i>						
PPCs	18	4	8	4		2
RBS	4				2	2
Site Connect	??				??	??
SDSL	2				1	1
POH	1					1
<i>Alternative interface</i>						
WES/WEES	13		1	6		6
BES	11		1	5		5
BNS					1	1
ONBS					1	1
<b>Grand total</b>	<b>49</b>	<b>4</b>	<b>10</b>	<b>15</b>	<b>5</b>	<b>19</b>