

Our ref: CW 01052/08/10

4 March 2013

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By email

Dear Rickard

### **Ethernet disputes: costs**

I refer to your email of 20 September 2012 in which you requested that Ofcom, under section 190(6) of the Communications Act 2003 (“the Act”), should require BT to pay TalkTalk’s costs incurred in connection with the dispute between BT and TalkTalk about BT’s charges for Ethernet services (CW 01052/08/10) (“the dispute”). There were related disputes brought by four other CPs. We refer to the dispute and those other disputes collectively as “the disputes”. I also refer to your letter of 25 January 2013 in which you set out your further comments in relation to that request. We refer to these letters collectively below as “your costs submission”.

As we noted in our letter of 11 January 2013, we would in general expect that disputing parties bear their own costs for the majority of the disputes that we resolve and we therefore do not intend to routinely require costs payments between the parties to disputes.

Having considered the evidence and submissions put forward in your costs submission, we have decided that the circumstances of the dispute and BT’s conduct are on balance not such that we should exercise our discretion to direct BT to pay your costs in this case, for the reasons set out below.

### **Our approach**

Section 190(6) of the Act confers on us the power to require a party to a dispute to pay another party’s costs and expenses incurred in consequence of the reference of the dispute to Ofcom or in connection with it.

In accordance with section 190(6A) of the Act, Ofcom may not require a party to a dispute to make payments to another party unless Ofcom has considered: (a) the conduct of the party before and after the reference to Ofcom (including, in particular, whether any attempt has been made to resolve the dispute); and (b) whether Ofcom has made a decision in the party's favour in respect of the whole or part of the dispute.

In October 2012 we published for consultation draft guidance on the payment of costs and expenses in regulatory disputes<sup>1</sup>. The draft guidance sets out our proposals as to how in the future we expect to deal with applications for costs made by parties to disputes. As noted at paragraph 3.3 of the draft guidance, we decide whether to award costs in a dispute by exercising our discretion on a case-by-case basis. However, in line with the draft guidance, in light of our section 190 (6A) obligations, we are likely to have regard to the following factors in exercising our discretion:

- commitment to negotiations or ADR;
- behaviour that increases costs and expenses, such as providing incomplete or inaccurate information and/or failure to comply with deadlines;
- the nature and value of the issues in dispute; and
- the outcome of the dispute resolution process.

As noted in the draft guidance, we would not normally expect to require a party to a dispute to pay another party's costs unless a number of these factors are present which would suggest that payment of costs should be required.

In considering your request for costs we have had regard, in particular, to the following documents:

- TalkTalk's email of 20 September 2012;
- TalkTalk's letter of 25 January 2013 and the letters annexed to that letter;
- BT's letters of 25 January ("BT's first costs response") and 4 February 2013 ("BT's second costs response") commenting on TalkTalk's request for costs;

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<sup>1</sup> Draft guidance *Payments of costs and expenses in regulatory disputes* dated 29 October 2012 ("the draft guidance")  
<http://stakeholders.ofcom.org.uk/binaries/consultations/payment-costs/summary/main.pdf>

- Disputes between each of Sky, TalkTalk, Virgin Media, Cable & Wireless and Verizon and BT regarding BT's charges for Ethernet services, Determinations and Explanatory Statement dated 20 December 2012, ("the final determinations");
- correspondence between BT and TalkTalk regarding negotiations in connection with the dispute appended to TalkTalk and Sky's joint dispute submission dated 27 July 2010;
- TalkTalk and Sky's joint submission dated 27 July 2010 requesting that Ofcom resolve a dispute between BSkyB, TalkTalk and BT about BT's charges for Ethernet services ("your dispute submission");
- BT's letter dated 10 August 2010 providing comments on whether Ofcom should open a dispute; and
- TalkTalk's letter dated 31 August 2010 which provided further details of negotiations between TalkTalk and BT.

### **TalkTalk's submissions**

In support of your request for costs, you made the following submissions which we comment on in turn below:

- BT failed to engage in good faith negotiations with TalkTalk;
- BT's behaviour increased the costs and expenses of TalkTalk;
- the dispute is commercial in nature with minimal impact on citizens, consumers or the promotion of competition in the way envisaged by Ofcom's draft guidance; and
- the dispute has been determined in TalkTalk's favour.

### **BT's conduct before the reference to Ofcom – your claim that BT failed to engage in good faith negotiations**

With respect to BT's conduct before the reference of the dispute to Ofcom, you suggest in your costs submission that:

- *"BT's showed no real commitment to the negotiations that TalkTalk desired to pursue."*

- *“The position of Openreach throughout these negotiations can only be characterised as dismissive whereby it consistently failed to address the substantive issues and concerns raised by TalkTalk.”*
- *“Openreach refused to engage with TalkTalk’s argument in any greater detail and failed to produce any evidence to back up its own position that its charges were fully compliant with its cost-orientation and other regulatory obligations. Instead it merely repeated vague and unevidenced assertions.”*
- *“Despite obvious parallels between the PPC investigation (particularly the fact that it was clearly held that BT’s charges would in practice always have to be below DSAC), Openreach’s negotiation stance never changed with regard to TalkTalk’s claim... Openreach immediately sought to position BES services as being very different to PPC services...once Ofcom had issued its final determination in October 2009.”*
- *“Openreach’s stance during the negotiations showed a blatant disregard for its regulatory obligations and its customers in the face of overwhelming evidence that its charges for BES services were clearly not cost-orientated.”*

In its second costs response, BT disagrees that it refused to negotiate and explains that negotiations took place although they did not result in a settlement. BT states that it carefully considered TalkTalk’s submissions both before and after opening of the dispute, and *“adopted a position in the negotiations that were consistent with its position in the PPC disputes and the PPC 2Mbit/s trunk charges appeals (PPC1).”* BT further claims with respect to this argument that *“there were significant factual differences, and therefore resulting legal, regulatory policy and economic differences, between the AISBO market services the subject of this dispute and the trunk market service the subject of the PPC1 appeals.”*

#### Ofcom’s views

In assessing TalkTalk’s submissions on this issue, we have reviewed the correspondence between TalkTalk and BT included with your dispute submission regarding the negotiations that took place between TalkTalk and BT in relation to the dispute, and the documents

appended to your costs submission. We have also noted BT's comments in its 10 August 2010 letter<sup>2</sup>, in which BT stated that it did not consider commercial negotiations with TalkTalk on the issue had reached an impasse by that stage but that the PPC appeal<sup>3</sup> had had the effect of stalling negotiations, and that it was therefore not appropriate for Ofcom to accept the dispute for resolution.

From the evidence we have reviewed, it is our understanding that TalkTalk and Sky initiated negotiations with BT in connection with the dispute in January 2008 and that these were ongoing until late December 2009. We received TalkTalk's dispute submission at the end of July 2010, by which point the PPC appeal was ongoing. Prior to the submission of the dispute to Ofcom, there was a chain of correspondence and records of meetings that show attempts by the parties to discuss the substantive issues ultimately raised in the dispute. It is clear that BT and TalkTalk fundamentally disagreed on a central issue in the dispute, namely whether BT's prices had been cost-orientated and how to assess this. There is evidence that attempts were made by the parties to negotiate on this issue, but they were not successful. We note that BT maintained its position that its charges were cost- orientated. We do not consider that BT's adherence to its position should, in itself, be considered a lack of a genuine commitment to negotiations.

On balance, on the basis of the available evidence, we are not satisfied that there is sufficient evidence of a lack of a genuine commitment to negotiations by BT to justify, in itself, a direction that BT should be required to pay TalkTalk's costs in relation to the dispute.

### **BT's conduct after the reference to Ofcom – your claim that BT's behaviour increased the costs and expenses of TalkTalk**

TalkTalk claims that BT's behaviour increased the costs and expenses of TalkTalk for the following reasons:

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<sup>2</sup> We note this letter is referred to in the CAT's judgment on BT's appeal against Ofcom's decision to accept the Ethernet disputes for resolution, *BT v Ofcom* [2011] CAT 15, see paragraph 24.

<sup>3</sup> BT's appeal of Ofcom's final determinations in disputes concerning BT's charges for partial private circuits ("PPCs"), which was filed on 14 December 2009. As you are aware, the PPC disputes concerned a similarly worded cost orientation condition and the PPC appeal raised issues which were relevant to the consideration of the cost orientation condition that was the subject of the Ethernet disputes.

(1) BT's preliminary issues appeal

TalkTalk alleges that BT's appeal to the Competition Appeal Tribunal ("CAT") against Ofcom's decision to accept the dispute for resolution (the "preliminary issues appeal"), which was dismissed in a "short 25 –page judgment" was "the second strand of its delaying tactic". It also claims that "...BT's appeal in this case again quite clearly shows that BT ultimate aim was to delay any resolution of the substantive matter for as long as possible." We note that TalkTalk has included amongst the costs it seeks to recover the cost of the barrister to represent TalkTalk at that appeal.

BT argues in its second costs response that if TalkTalk incurred costs in respect of BT's preliminary issues appeal "the correct tribune of the question of whether BT should pay TalkTalk's cost of that appeal is the Tribunal and not Ofcom".

*Ofcom's views*

BT had the right to appeal Ofcom's decision to open the dispute to the CAT, and exercised that right.

Under the Competition Appeal Tribunal Rules<sup>4</sup>, the CAT has power to order the payment of costs by one party to another in respect of the whole or part of proceedings before the Tribunal. We note that the CAT's usual rule is that interveners do not recover their costs except in exceptional circumstances. TalkTalk had the right to apply to the CAT to seek its costs incurred in intervening in the appeal, however we understand that it did not do so. In the circumstances, we do not consider that it is appropriate for TalkTalk to seek to reclaim these costs under section 190 of the Act as part of its costs it has incurred in consequence of the reference of the dispute to Ofcom or in connection with it.

(2) Regulatory Financial Statement data

In your costs submission, you argue that:

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<sup>4</sup> (SI 2003 No.1372), as amended by The Competition Appeal Tribunal (Amendment and Communications Act Appeals) Rules 2004 (SI 2004 No.2068)

*“... the arguments put forward by BT to make changes to RFS cost data have shown that it has in the past provided incorrect and/or unreliable cost data to Ofcom” , and “...BT’s attempts to correct the data has frustrated, unduly delayed and even hindered Ofcom’s effective and timely resolution of the dispute which has been to the detriment of TalkTalk.”*

TalkTalk considers that this is no different to a situation in which BT had submitted incorrect information in response to a specific information request during the dispute.

In its second costs response, BT states that *“during the dispute process it was unclear to BT how Ofcom was going to approach its compliance and repayment assessment functions; against this backdrop, in providing the information BT did, it sought to be helpful as possible. It was not BT’s intention to cause detriment to TalkTalk, if any detriment was suffered. Indeed a number of the adjustments proposed by BT were beneficial to the disputing CPs.”*

#### *Ofcom’s views*

As noted in our final determinations, in May 2011 BT wrote to Ofcom informing us of possible anomalies in the Distributed Stand Alone Cost (“DSAC”) figures published in its RFS and argued that we should therefore not use the published DSAC figures for 2006/07 to 2009/10 for the purposes of resolving the disputes and instead use new DSAC figures that BT had calculated using a revised methodology.<sup>5</sup>

We note that both BT and several of the Disputing CPs<sup>6</sup>, including TalkTalk, made submissions arguing that certain adjustments needed to be made to BT’s published financial data in order to correct for volume errors and to ensure that revenues and costs were appropriately matched.<sup>7</sup> We also identified, in the course of examining data provided by BT, that certain other corrections to BT’s published financial data were required (mostly related to volume errors).

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<sup>5</sup> This issue is discussed in Section 12 of the final determinations.

<sup>6</sup> Being TalkTalk, British Sky Broadcasting Limited (“Sky”), Virgin Media Limited, Cable & Wireless Worldwide plc group and Verizon UK Limited

<sup>7</sup> This is discussed in Section 13 of the final determinations.

As we explain in the final determinations, we would normally expect to be able to rely on the data published in BT's RFS for the purposes of assessing compliance with BT's regulatory obligations.<sup>8</sup> In light of both BT's and the Disputing CPs' arguments as to the potential issues with and errors in its published data, Ofcom had to consider the question of what data to use for resolving the dispute in some detail. We consider that this may have led to some delay in resolving the disputes. In our view it is appropriate to give some weight to this factor in our consideration of whether BT should be required to pay costs of other parties, as where we are unable to rely on the data published in the RFS it can have a significant impact on our ability to resolve disputes efficiently.

However, we do not consider that TalkTalk has demonstrated that these issues have led to an increase in its costs in relation to the dispute. In particular, when considered in the round given the nature and complexity of the disputes, we do not consider that the delay that may have arisen as a result of this issue is in itself likely to have led to a material increase in TalkTalk's costs.

We therefore consider that on balance this factor is not sufficient to justify an award of costs in this instance.

### **The nature and value of the dispute**

In your costs submission, you express the view that:

*"The dispute is primarily commercial in nature as between TalkTalk and BT... The issues raised by the dispute do not materially affect citizens in relation to the communication markets; consumers in relevant markets; or the promotion of competition."*

TalkTalk also emphasises the significant financial value of the issues in dispute.

In its second costs response, BT argues:

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<sup>8</sup> See, for example, paragraphs 11.22 to 11.24.



*“The basis of the dispute was that BT had failed to comply with a regulatory condition, the basis of charges condition. That allegation required a careful analysis of complex factual, economic, regulatory policy and legal factors, factors concerning, amongst other things, the extent and use of Ofcom’s dispute resolution powers, the correct test(s) to be applied for the assessment of cost orientation, including what adjustments it is appropriate to make to BT’s published RFS, and the level of repayment, all of which factors will impact on the way that BT prices its products, both now and in the future, and which in turn will have an impact on citizens, consumers and competition.”*

### Ofcom’s views

In considering TalkTalk’s request for its costs, Ofcom has had regard to the nature of the disputes. The disputes related to BT’s compliance with its regulatory obligations in a market in which we have deemed it to have SMP. Resolution of the disputes is therefore relevant to our core duty to protect consumers, in this case by promoting competition in the markets for AISBO services. We also note that the dispute were complex, multi-party disputes which involved the consideration by Ofcom of a large number of detailed submissions on various regulatory, economic and financial issues. Ofcom does not consider that the disputes raised “purely commercial” issues (as understood in the draft guidance) such that we would be more likely to require a payment of costs on the part of BT in this instance.

### **The outcome of the dispute**

TalkTalk submits that we have *“made the determination entirely in TalkTalk’s favour”*.

### Ofcom’s views

As we note in our draft guidance, when deciding whether to require a party to pay another party’s costs, we consider whether a party has “succeeded” in its claims, in the sense that Ofcom has substantially accepted submissions made by a party and accordingly made a determination in its favour.

In this case, the dispute was not resolved in BT’s favour. Ofcom determined that BT had overcharged TalkTalk (and the other Disputing CPs) for a number of Ethernet services over a

number of years and required BT to repay TalkTalk the full amount of the overcharge which involved a repayment of a large sum of money. We therefore consider that TalkTalk substantially succeeded in its claims. We take this factor into account in our consideration of whether, in the round, it is appropriate to require BT to pay TalkTalk's costs in this case. Overall, we would be more likely to require a party to repay the costs of another party that has overall been successful in its claims. However, we do not consider that it is appropriate to require BT to pay TalkTalk's costs on the basis of this factor alone.

## **Conclusion**

In conclusion, we consider that overall Ofcom made a decision in TalkTalk's favour in respect of the dispute. We also consider that the issues relating to the accuracy or reliability of its RFS data is a factor that may support an award of costs against BT for TalkTalk. We do not, however, consider that there is sufficient evidence to suggest that there was a lack of genuine commitment by BT to negotiations with TalkTalk prior to the submission of the dispute, nor that the circumstances surrounding BT's preliminary issues appeal were such that these factors would justify requiring BT to pay TalkTalk's costs. Having considered the evidence and submissions put forward in your costs submission, and the considerations set out in s190(6A), and weighed up all the various factors, we have decided that the circumstances of the dispute and BT's conduct are on balance not such that we should exercise our discretion to direct BT to pay your costs in this case.

Yours sincerely



Neil Buckley

cc. Stuart Murray, BT Legal