Vodafone

August 2015

Response to Ofcom's Consultation:

Review of BT's cost attribution methodologies

1. Preface

1.1 We commend Ofcom for the work it has undertaken in taking forward this consultation. We appreciate the range and complexity of the investigative work involved and the scale of the challenge. We believe this is a very worthwhile project at the core of Ofcom's objectives, delivering for citizens and consumers. It is a class leading regulatory initiative that deserves credit, proving that even the most complex issues can be addressed when the correct skills are deployed and there is a sound framework in place to make the necessary improvements.

1.2 In an industry that has enduring access bottlenecks which are the cause of market failure the regulatory accounts are a crucial part of the process of creating a regulatory environment that seeks to emulate competitive market outcomes. Ofcom has developed an approach of encouraging retail competition reliant upon a range of regulated wholesale products. This gives consumers a choice of supplier, enabling them to experience first-hand the benefits that competition can deliver. However the foundations of that retail competition are predicated entirely on the fair supply of regulated wholesale products, which are priced at an efficient level.

1.3 We cannot overstate the importance to our industry and the wider consumer interest of reliable, unbiased regulatory accounting information. The detail within these accounts is used to set prices within charge controls, resolve disputes before Ofcom and even settle subsequent litigation before appeal bodies and the courts. What is in the accounts matters to consumers who are many stages removed from the detail. They need to have confidence in the regulatory system and the regulatory accounts are at the heart of that system. The accounts must be right first time all the time, they shouldn't be subject to either restatement or, as has now become all too common, revelations after the fact that cast doubt on the validity of previously published numbers.

1.4 Since 2008 we've seen confidence in BT's published regulatory accounting output evaporate, firstly through hasty restatements apparently motivated by BT's desire to reduce overcharging claims before Ofcom, then through the reallocation of costs in one year to the next, moving costs from regulated markets where charge controls have already been set into other regulated markets where baseline costs have yet to be established for future price setting. It was against this backdrop that Ofcom undertook its fundamental review of the regulatory accounting framework as it sought to reform the regime to restore trust.

1.5 We appreciate just how complicated and time consuming this project has been and we are acutely aware of the information asymmetries that are faced when dealing with an organisation as complex and large as BT, even with the benefit of Ofcom's information gathering powers. The complexity of BT's business, exacerbated by the fact that many regulated and unregulated services share a large pool of common costs means it is always a challenge to reach fairly derived, robust numbers. Ofcom's reforms to the regulatory accounting regime whereby the accounts must reflect past regulatory decisions and the introduction of a provision for Ofcom to have the ultimate right of veto on attribution changes have

started to, and will continue to make a big difference, improving confidence in the accounts and ensuring better regulatory decision making going forward.

1.6 With new rules in place around what changes can be made in the future, this latest consultation focuses on cleaning up the existing attribution decisions and calculations currently loaded within the accounts, to ensure that the new change control measures aren't compromised by the presence of significant errors and inappropriate attribution decisions already imbedded within the system. Without this crucial work we risk prolonging the adverse impact that past poor regulatory accounting decisions can have on our industry and consumers. Ofcom's reforms thus far can be likened to removing the source of pollution from a water course; the proposals set out within this consultation now begin to tackle the pollution that has previously flowed. It is not an easy task, but it is something we whole heartedly support as we strive for quality, reliable and most importantly unbiased regulatory accounting output to support our industry and bring benefits to end consumers.

1.7 As a significant purchaser of regulated services and a key stakeholder in the regulatory accounting debate we have seen many examples over the last few years that demonstrate the lengths BT will go to preserve its commercial interests. However the scale of the inappropriate attribution has taken even us aback. We applaud the work undertaken by Cartesian, however we cannot share their view that BT's 'cost attribution system is free from bias'. With proposals to remove a staggering £262M from the regulated cost base in one year and with material cost movements all in one direction (remedying misallocated costs that shouldn't have been charged against regulated services, but instead should have been allocated to non-regulated services) and with many more questionable areas identified for future review, we believe the numbers speak for themselves.

1.8 We fully support all of Ofcom's proposals to remove costs from the regulatory cost base. Some of the issues to be remedied are straightforward errors, others relate to current attribution decisions that are clearly indefensible on any objective basis. We believe Ofcom should and can go further. This consultation should represent just the start of this type of exercise, and it should continue until such time as confidence has been fully restored and we are certain that all incidences of inappropriate attribution have been eliminated. Things would look very different now if this work had been carried out a decade ago, as many of the issues identified extend back well beyond 2013/14, contributing to the regulated cost base and of course resulting in higher pricing being paid by UK consumers and businesses in the years since Ofcom's creation.

1.9 What is clear is that not only do Ofcom have to issue a subsequent consultation on the range of other attribution decisions identified that need to be changed, but it shouldn't stop there. Irrespective of the outcome of the BT/EE review currently with the CMA, the industry and Ofcom needs a Cartesian type review carried out on an annual or at the very least a bi-annual basis to preserve the integrity of any newly produced accounts. The current audit approach hasn't worked, having been present throughout the last decade but failing to stop both mistakes in arithmetic and spreadsheet management and permitting clearly inappropriate attribution decisions to stand, without question or discussion.

1.10 Ofcom must not forget the critical eye of stakeholders who have been vital thus far in holding BT to account. Given Ofcom's resource constraints, stakeholders provide oversight and insight, with the publication of regulatory accounting numbers and associated consultations on the subject remaining an important tool in ensuring regulatory accounts are useful. For the sake of end consumers this must not be a time limited project for Ofcom. Oversight of regulatory accounting output needs to be resourced properly and we believe Ofcom should commission Cartesian or another suitably qualified independent consultancy to deliver an annual report on BT's accounts to the Ofcom board and stakeholders. A more hands on Ofcom on regulatory accounting must be matched by an increase in specialist resources and relevant expertise if this role is to be completed with rigor. The continued participation of consultants reporting directly to Ofcom on these matters is invaluable and is money well spent; bringing wider public benefit for a comparatively modest sum.

1. Introduction

We warmly welcome this review, believing it to be critically important to the integrity of regime and resultant consumer outcomes. We congratulate Ofcom on the work undertaken thus far, however this can't be left as a standalone exercise.

We want Ofcom to consult further on a range of current attribution decisions to ensure that the regime has the confidence of stakeholders and is delivering for all consumers.

All errors and 'obliviously inappropriate' attribution decisions should be corrected as soon as possible and Ofcom should ensure that as many of those changes as possible are reflected in the baseline numbers for the Leased Lines Charge Control.

The existence of so many material errors raises questions about the assurance wrap around the accounts and Ofcom need to consider reforming the scope of the audit to ensure it is fit for purpose, including considering the prospect of using a deep dive review (like the one conducted by Cartesian) on a more regular basis and focused on areas where charge controls are due to be set.

It is clear that a number of attribution areas require far more regulatory scrutiny and we would like to see future consultations focusing on a number of key issues that have been highlighted in this consultation, including:

- BT's approach to copper depreciation, as it currently stands BT fails to recognise the residual value in the copper estate.
- The treatment of Transfers between BT Group businesses to better understand how these charges impact regulated charges.
- The Duct Valuation Methodology and how it is applied to specific regulated and unregulated products.

In the remainder of this response we consider the following key topics in detail:

The correction of errors [Section 2];
Proposed reforms to attribution [Section 3];
Attribution decisions identified by Ofcom for future consideration [Section 4];
Attribution decisions that we believe should be reconsidered [Section 5]; and
A review of supporting evidence [Section 6].

In the final section [7] we answer the specific questions posed by Ofcom.

2. Correction of Errors

2.1 Vodafone strongly supports the correction of all the identified errors at the earliest opportunity, including in relation to:

a) Fibre bandwidth and length (core and backhaul fibre attribution);

b) number of fibres used (access fibre attribution);

c) duct valuation (access: backhaul duct ratio);

d) usage factors - ISDN;

e) NGA duct depreciation;

f) facilities management costs;

g) IP network allocation to Ethernet switches;

h) usage factor for MSAN TDM cards;

i) call usage factors for part services; and

j) usage factor for i-Node component.

For the errors disclosed there is no justification for them to remain and even BT appears to recognise that they should be corrected immediately.

2.2 Whilst we do not want to spend much time discussing the detailed mathematics behind these errors, we do however believe their disclosure reinforces a number of key learning points that shouldn't be overlooked. The impact of the errors identified largely appears to be in one direction, favouring BT's commercial products over its regulated ones. It underlines the importance of what actually goes into the regulatory accounting numbers. Several errors in the preparation of calculations can easily add tens of millions to a regulated cost base that results in consumers paying more. Likewise if these costs are displaced from competitive markets, then BT may well be understating its cost base in these markets when competing with other communication providers for unregulated business, giving rise to competition concerns.

2.3 Firstly, in view of the number of errors identified and their impact on regulated markets, Vodafone urges Ofcom to ensure that a similar level of scrutiny is applied to all of the models and calculations upon which the Regulatory Financial Statements rely. If not already done, this could be achieved by developing a comprehensive listing of all such models and calculations, and checking that every one of them is scrutinised.

2.4 Secondly, the existence of these errors, in some case repeated year after year highlights just how significant the information asymmetry is between BT and Ofcom, let alone other industry stakeholders. Even with Ofcom's information gathering powers and the additional regulatory reporting it receives from BT (including flat-file access), not to mention the tri-partite obligations to Ofcom placed on the auditor of regulatory accounts, material mistakes can be repeated year after year. Even when these mistakes appear obvious as they are described in the consultation document, the brief, untransparent descriptions within BT's reference material mean they are passed by. Costs for voice services like Featurenet caught within the traditional leased lines market and unregulated

BT Wholesale service costs added to regulated Ethernet are just two obvious, unsubtle examples that should never have occurred. It is clear that all stakeholders, including Ofcom need to be able to better navigate their way around the accounts, increasing the scrutiny so that we avoid future mistakes of this magnitude.

2.5 Thirdly it underlines the poor performance of the current audit function, which has thus far been unable to deter multiple re-statements; cost re-allocation from one regulated market to the next; commercially motivated network re-valuations; the use of 'clearly inappropriate' cost allocations and now material calculation errors. A debate on what is realistic for the audit to achieve is all very well, but given the range of problems encountered thus far it is clear that the current arrangements on their own aren't satisfying the audit standard. The audit is often used as a seal of approval on the accounts that is assumed by the courts and appeal bodies to add a stamp of legitimacy to the accounts. The reality is very different and despite the audit costing BT a considerable sum to deliver, it hasn't provided stakeholders or Ofcom with the assurance needed. The audit on its own isn't the answer and Ofcom should give thought to how it can reform the audit to better target its focus, using it in conjunction with other in-depth evaluations of the accounts to ensure accuracy and above all integrity in the published output. Perhaps a revised audit, with a tighter focus would achieve more when combined with an Ofcom commissioned independent consultancy review (funded by BT) on an annual basis would achieve the correct balance. This could help identify the type of the errors highlighted by Cartesian and historically missed by the audit, making sure they were eliminated as part of a future assurance wrap. This could be coordinated with Ofcom's charge control cycle to ensure the most robust numbers were available to set charge control baselines for each market.

2.5 Despite the significant resources BT deploys in preparing its regulatory financial statements it is clear that mistakes are made and repeated year after year. CFO sign off may ensure that more focus is placed on the preparation of account, with a strive for accuracy. However we remain of the view that the accounts are treated within BT as a necessary inconvenience. We accept that the accounts are complicated as they reflect the complex nature of BT's business, both regulated and unregulated. We appreciate that mistakes will happen from time to time and we know that BT have recently invested in a new system to prepare the accounts. However in spite of all this, even when the new system was loaded up with data, glaring errors present for years were repeated. These errors are not harmless; they result in over-charging and poorer regulatory decision making. We need Ofcom to ensure BT puts the correct resourcing and management focus into account preparation. The cost of doing this is insignificant in comparison to the harm caused when over-charging occurs.

2.6 For the sake of clarity Ofcom should seek to identify in each case how long each error has been present within the accounts. It would appear that many of these errors have existed for several years and it is important that Ofcom takes action to help inform stakeholders and purchasers of these services the duration of the errors.

3. Proposed reforms to attribution

3.1 Vodafone welcomes Ofcom's proposals to reform inappropriate attribution decisions within the accounts. In this section we step through an evaluation of Ofcom's key proposals.

Duct valuation (access: backhaul duct ratio)

3.2 Ofcom highlights Cartesian's finding that in calculating the split of duct costs between Access and Core, based on the 1997 Absolute Duct Survey (ADS) plus a roll forward of capital expenditure since 1997, CCA indexation has not been applied as it should have been[1]. Vodafone notes that a similar approach is applied to the split of Access duct costs between fibre and copper[2], and would welcome assurance that CCA indexation is already being applied, or will also be applied, in that case.

Allocation errors

3.3 Vodafone strongly supports the correction of all allocation errors (i.e. allocations of costs to services not delivered using those costs, or failures to allocate costs to services delivered using those costs) at the earliest opportunity, including in relation to:

a) direct allocation (core/backhaul duct attribution to 21CN)[3];
b) transfer charges (BT Wholesale overheads)[4];
c) property cost apportionment[5];
d) power consumption for TSO (TSO electricity model)[6]; and
e) BT consumer costs allocated to Ethernet switches[7]; and
f) cost of phonebooks[8].

Attribution by pay and return on assets

Corporate costs

3.4 Vodafone agrees with Ofcom's overall conclusions on the current "pay and return on assets" allocation methodology applied to corporate costs[9]. In Vodafone's view, that methodology is obviously inappropriate:

a) a single allocation methodology should not be applied to a very large cost category such as this, when it can practicably be disaggregated into smaller cost categories with different cost drivers, and therefore different appropriate methodologies; and
b) BT's "combination" allocation methodology based on factorised pay plus return on assets does not appear objective or causal.

Vodafone believes that the allocation bases proposed by Ofcom for the disaggregated smaller cost categories it has identified are generally reasonable.

[1] Section 6.2.2, Cartesian report
[2] Section 6.3.2, Cartesian report
[3] Paragraphs 7.20 to 7.32, Cost Attribution Review consultation document
[4] Paragraphs 7.33 to 7.37, Cost Attribution Review consultation document
[5] Paragraphs 7.43 to 7.52, Cost Attribution Review consultation document
[6] Paragraphs 7.54 to 7.64, Cost Attribution Review consultation document
[7] Paragraphs 7.77 to 7.84, Cost Attribution Review consultation document
[8] Paragraphs 7.111 to 7.115, Cost Attribution Review consultation document
[9] Paragraphs 8.24 to 8.98, Cost Attribution Review consultation document

However, Vodafone does not believe it is reasonable to include any costs associated with BT's free staff Broadband Offer as part of its cost base. This is not a contractual benefit for staff but a discretionary one. It should not be funded in full or in part through regulatory charges, paid for by BT's commercial rivals. No other CP has the opportunity to charge the cost of discretionary staff benefits to their competitors and it is wrong that BT should retain this opportunity, which should be funded by BT alone.

If, contrary to this view, Ofcom does include such costs in the cost base, Vodafone submits that it would be completely erroneous to calculate the cost of providing the benefit by reference to the retail price[10]. Doing so results in regulated services contributing to the profits of BT's unregulated business. In particular, it seems inappropriate for CPs offering broadband products in competition to BT's retail broadband business, to be contributing to the profits of that business through the costs they pay for wholesale LLU or WBA. In Vodafone's view, the cost of providing this benefit should be removed entirely from the cost base of regulated products and appropriately reference to the underlying cost of provision.

TSO support function costs

3.5 Vodafone agrees with Ofcom's overall conclusions on the current "pay and return on assets" allocation methodology applied to TSO support function costs[11]. In Vodafone's view, that methodology is obviously inappropriate, for the same reasons given for corporate costs.

3.6 Vodafone believes that the allocation bases proposed by Ofcom for the disaggregated smaller cost categories it has identified are generally reasonable. However, Vodafone would welcome confirmation from Ofcom that these bases will be applied to TSO costs (i.e. excluding Openreach costs), not BT costs (i.e. including Openreach costs). TSO is responsible for running the non-Openreach segment of BT's network[12], and therefore the great majority of its activities will be unrelated to Openreach products. This should be reflected in the cost allocation methodology. For example, Ofcom states that it plans to allocate TSO Service, Strategy and Operations costs on the basis of "all previously allocated total costs"[13]. As these costs support TSO, rather than Openreach, activities, this should be "all costs previously allocated to TSO", rather than "all costs previously allocated to TSO and Openreach", but this is not clear from the document.

Openreach common costs

3.7 Openreach common costs are allocated using the same "pay and return on assets" allocation methodology used for corporate costs and TSO support function costs.

Ofcom:

a) expresses reservations similar to those expressed over the use of the same methodology for corporate costs and TSO support function costs, but has not yet reached a conclusion on whether it is appropriate for these costs;

[10] Paragraphs 8.51 to 8.53, Cost Attribution Review consultation document
[11] Paragraphs 8.99 to 8.139, Cost Attribution Review consultation document
[12] 5.10.11 (and also 5.4.6.1, 5.5.11 and 5.5.11.4) Cartesian report. See also Ofcom discussion of floor space utilisation at paragraphs 9.42 to 9.70, Cost Attribution Review consultation document
[13] Paragraphs 8.90 to 8.92, Cost Attribution Review consultation document

b) and observes that since the methodology only allocates costs incurred by Openreach, within Openreach, it will have less of an impact on the allocation of costs between regulated and unregulated services than in the case of corporate costs[14].

3.8 Vodafone submits that the same considerations that make the "pay and return on assets" allocation methodology obviously inappropriate in the case of corporate costs and TSO support function costs, make that methodology inappropriate in the case of Openreach common costs. No evidence has been advanced for the adoption of a different conclusion for the latter costs. On the contrary, many of the smaller cost categories described within Openreach common costs make it clear that the "pay and return on assets" allocation methodology would be obviously inappropriate for those cost categories:

a) training: this appears similar to "Learning Academy" costs within corporate costs, which Ofcom proposes allocating on the basis of employee pay, not pay and return on assets[15];
b) internal hospitality: these costs are driven by employees, not assets;
c) H&S services: this appears broadly similar to "employee healthcare" costs within corporate costs, which Ofcom proposes allocating on the basis of the number of employees, not pay and return on assets[16];
d) fleet ICU rental charges: these costs are driven by employees, not assets; and
e) stationery: these costs are driven by employees, not assets.

3.9 Vodafone also observes that even though this methodology only allocates costs incurred by Openreach, within Openreach, it is still capable of having a significant impact on the allocation of costs between regulated and unregulated services: 25% of Openreach revenue is from unregulated services[17]. Vodafone therefore urges Ofcom to apply the same level of scrutiny to these costs, that has been applied to other overheads.

Revenue from sale of copper and property cost apportionment

Sales of property

3.10 Vodafone agrees with Ofcom that it is obviously inappropriate for profits on disposals of properties to be allocated only to the Retail Residual business. Vodafone agrees that this benefits BT unfairly, because in many cases these properties were used in the past to provide regulated services, and regulated services will therefore have contributed to the cost of these properties. The alternative allocation basis proposed by Ofcom appears reasonable[18].

3.11 Vodafone also encourages Ofcom to ensure that BT data on profits on disposals of properties is consistent with reports of disposals of properties[19]. Vodafone would welcome confirmation that this allocation error will be corrected in the 2014/15 Regulatory Financial Statements, and so reflected in the Business Connectivity charge controls.

Sales of copper

Sales of copper from the Backhaul and Inner Core networks

[14] Paragraphs 8.140 to 8.146, Cost Attribution Review consultation document
[15] Paragraphs 8.86 to 8.89, Cost Attribution Review consultation document
[16] Paragraphs 8.48 to 8.50, Cost Attribution Review consultation document
[17] Section 12.2 of BT's 2013/14 Current Cost Financial Statements discloses total Openreach revenue of £5,193m, of which £1,333m is from markets and activities with no SMP reporting obligations.
[18] Paragraphs 9.12 to 9.41, Cost Attribution Review consultation document
[19] Paragraph 9.34, Cost Attribution Review consultation document

3.12 BT allocates revenue from disposals of copper only to the Network Residual business. Vodafone does not agree with Ofcom's conclusions on this allocation[20]. The current approach to disposals of copper is obviously inappropriate, for the same reasons that the current approach to disposals of property is inappropriate:

a) In the case of disposals of property, Ofcom concludes that allocation to the residual is inappropriate, because in many cases the properties disposed of were used in the past to provide regulated services, and regulated services will therefore have contributed to the cost of these properties.
b) The same considerations apply in the case of disposals of copper. In many cases, the copper cables disposed of were used in the past to provide regulated Backhaul and Inner Core services, and those regulated services will therefore have contributed to the cost of these cables.

3.13 Ofcom appears to partially recognise point (b), when it states that:

"*BT may have made windfall gains from these proceeds to the extent that this core and backhaul copper has been used to provide regulated services in prior periods*"[21].

However, precisely the same could be said of proceeds from sales of property.

Ofcom's acceptance of the allocation of proceeds exclusively to unregulated services is partly based on the observation that regulated services do not use copper in the Backhaul and Inner Core networks to any material extent:

"*It might be appropriate to allocate these proceeds to regulated services that still used copper in BT's core and backhaul networks but we are not aware of any that do so to any material extent.*" [22]

3.14 However, precisely the same statement could be made with regard to unregulated services, which also do not still use copper to any material extent. Applying the same logic would lead to the conclusion that proceeds should not be allocated to unregulated services.

3.15 Neither regulated nor unregulated services in the Inner Core and Backhaul networks still use copper to any material extent. In other words, copper is incremental to neither set of services, but is common to both sets of services. The common nature of Inner Core and Backhaul copper should be reflected in its allocation approach, and this will not entail exclusive allocation to only one of the two sets of services to which that copper is common.

3.16 In Vodafone's view, revenue from disposals of Inner Core and Backhaul copper should recognise the relevance of regulated services, and the common nature of that copper. For example, revenue could be allocated in line with the costs of existing Backhaul and Inner Core cables.

Sales of copper from the Access network

3.17 Ofcom observes that revenue from sales of copper from the Access network is likely to remain low for the foreseeable future, and so concludes that this is not relevant to current charge controls[23].

[20] Paragraphs 9.12 to 9.41, Cost Attribution Review consultation document
[21] Paragraph 9.23, Cost Attribution Review consultation document
[22] Paragraph 9.23, Cost Attribution Review consultation document
[23] Paragraph 9.23, Cost Attribution Review consultation document

3.18 Vodafone does not agree with this conclusion, and believes that revenue from sales of Access copper is of material relevance to current charge controls, including Business Connectivity. This is because future sales of copper are not an unforeseeable windfall gain. Rather, they are a predictable consequence of the ownership of copper cable assets, which should be reflected in current charges for the use of copper cable assets. Specifically:

a) copper depreciation is, Vodafone understands, currently calculated by writing off the original cost of the copper cable (C) over the expected life of that copper cable (L), i.e. C/L[24]; but
b) copper depreciation should, Vodafone submits, be calculated by writing off the difference between the original cost of the copper cable (C) and its expected future disposal or "residual" value, (R), over the expected life of that copper cable (L), i.e. (C-R)/L.

3.19 The importance of reflecting the residual value of an asset in the current depreciation charge for that asset is a very well established principle in accounting. The accounting policies set out in BT's own audited statutory financial statements make it clear that depreciation should be calculated net of expected residual value (emphasis added):

"*Depreciation is provided on property, plant and equipment on a straight line basis from the time the asset is available for use, to write off the asset's cost over the estimated useful life taking into account any expected residual value*." [25]

3.20 This is in line with the relevant accounting standards issued by the UK's independent regulator, the Financial Reporting Council, Financial Reporting Standard 15 (emphases added), and by the international regulator the International Accounting Standards Board, International Accounting Standard 16:

"*The fundamental objective of depreciation is to reflect in operating profit the cost of use of the tangible fixed assets (i.e. the amount of economic benefits consumed by the entity) in the period. Therefore, the depreciable amount (i.e. cost, or revalued amount, less residual value) of a tangible fixed asset should be recognised in the profit and loss account on a systematic basis that reflects as fairly as possible the pattern in which the asset's economic benefits are consumed by the entity, over its useful economic life.*" [26]

"*Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life...*

Depreciable amount is the cost of an asset, or other amount substituted for cost, less its residual value." [27]

3.21 Vodafone believes that the depreciation of copper assets in the Access network[28] should comply with these principles, in accordance with BT's own accounting policies and best practice[29]. Given the potential scale of copper residual value, compliance is likely to have a material effect on regulated charges for services using the Access network.

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[24] For simplicity this ignores the impact of current cost accounting adjustments.
[25] Page 131, BT 2013/14 Annual Report
[26] Summary, Financial Reporting Standard 15
[27] Definitions, International Accounting Standard 16
[28] And indeed all of BT's assets
[29] A 2014 report prepared for Sky and TalkTalk made similar arguments (*Regulated costs for BT's copper cable*, Frontier Economics, January 2014)

4. Attribution decisions for future consultation

In this section we highlight a number of areas that we believe Ofcom should review in the immediate future. The first part of the section discusses areas that Ofcom appear to recognise as needing further review as well as those issues where we believe there is merit in Ofcom reconsidering its initial stance.

Floor space utilisation (and the treatment of vacant space)

Non-chargeable vacant space

4.1 Vodafone agrees with Ofcom's conclusion that allocating vacant space within non-chargeable areas across all building types (i.e. both General Purpose Buildings and Operational Buildings) is neither causal nor objective and is therefore obviously inappropriate. Vodafone believes that the allocation basis proposed by Ofcom is broadly reasonable[30].

4.2 Vodafone would welcome confirmation that this allocation error will be corrected in the 2014/15 Regulatory Financial Statements, and so reflected in the Business Connectivity charge controls.

Operational buildings

4.3 We would request clarity around the impact that BT's long term property leasing decisions have had on their ability to flex building space. It may well be the case that BT's contractual commitments prevent it from utilising smaller units of space. There long term leases were entered into on a commercial basis to suit BT's corporate interests at time. It should not then be left to Openreach (and by default other CPs who purchase regulated services) to pick up additional costs that otherwise wouldn't be present absent of the long term lease commitments.

4.4 In any event Vodafone does not agree with the allocation of all vacant space in Operational Buildings with an MDF to Openreach rather than TSO, on the basis that Openreach is the "anchor tenant" in such buildings, i.e. on the basis that Openreach assets (MDF and cable chambers) are preventing a reduction in the size of the Operational Building portfolio due to the prohibitive cost of moving them to smaller buildings.

[30] Paragraphs 9.42 to 9.70, Cost Attribution Review consultation document

4.5 In the case of the revenues from surplus property space, Ofcom concludes that allocation should recognise the balance of past use of those properties[31]. It is not clear why that same principle should not also be applied to the costs of surplus property space (i.e. vacant space). From that perspective, the vacant space in local exchanges is primarily attributable to TSO, not Openreach: it is TSO assets (switches, etc.) whose space requirement has shrunk significantly since the local exchanges were constructed, not Openreach assets.

4.6 From the perspective of a forward-looking Long Run Incremental Cost analysis, the focus is typically on long run costs without regard to transition costs. From that perspective, vacant space is incremental to neither TSO activities nor Openreach activities; it is a common cost between TSO and Openreach, and should be treated accordingly, not allocated solely to one of the two.

4.7 Even if a forward-looking incremental cost analysis is adapted to include the impact of transition costs, it would be wrong to treat the entire cost of vacant space as attributable to Openreach. If the transition costs associated with Openreach assets are preventing movement to smaller buildings, it may be arguable that some vacant space costs that could otherwise be saved are attributable to Openreach. However, it would be wrong to assume that those costs are equal to current vacant space costs, because realisable vacant space costs are likely to be significantly smaller than current vacant space costs.

4.8 The last point can be illustrated by way of worked example. For simplicity, property costs are expressed as up front capital values so that they can be compared with transition costs on a like for like basis:

a) Suppose an Operational Building has a total cost of £100, with floor space split 15% Openreach, 60% TSO, and 25% vacant.

b) A smaller Operational Building of the right size is available for a total cost of £75, but transition costs would be £40 for Openreach assets and £15 for TSO assets.

c) Under the current approach, the vacant space cost of £25 (25% x £100) is allocated entirely to Openreach, on the grounds that transition costs for its assets of £40 make the move to the smaller building uneconomic.

d) However, absent these transition costs, the realisable vacant space cost is not £25, but £10, because TSO transition costs of £15 would reduce the gross £25 saving from the move.

e) So, while there may be an argument for allocating the realisable vacant space cost of £10 entirely to Openreach, the remaining £15 of unrealisable vacant space cost is incremental to neither the absence of Openreach nor the absence of TSO. In other words, the £15 is a common cost to both TSO and Openreach.

[31] Revenue from sale of copper and property cost apportionment, see above

f) It would not be appropriate to allocate that common cost entirely to Openreach or TSO. The common cost could instead be allocated in line with previously allocated costs of £85, in line with Ofcom's proposed treatment of other common costs. That would result in an allocation of £4.40 to Openreach £10.60 allocation to TSO[32].

g) The result of this approach would be that instead of allocating all the £25 vacant space cost to Openreach, only £14.40 would be allocated to Openreach, and the remainder of £10.60 would be allocated to TSO. Applied over the whole Operational Building estate, this could make a significant difference to allocated costs.

Transfer charges (Miscellaneous - Accuracy)

4.9 Vodafone shares Ofcom's concern that "balanced transfers" which make no net contribution to BT's total costs introduce complexity and reduce transparency for no obvious benefit, and would encourage their replacement with clearly articulated allocation methodologies[33].

4.10 Vodafone also shares Ofcom's concern that "unbalanced transfers", which by definition make a contribution to BT's total costs, might contain an element of mark-up. Vodafone is concerned that this may result in BT shareholders being remunerated twice over for the some activities and assets (once via a transfer mark-up, and again via a return in a charge control), merely as a result of those activities or assets being designated "non-core". This may give BT an inappropriate incentive to designate as many activities and assets as it can as "non-core", just to boost its total returns.

4.11 Further transparency is necessary in this area to help understand how these charges impact regulated charges and if they permit BT's retail divisions to utilise a range of ancillary services (such as Project Services, Special Fault Investigations and Broadband Boost) in far greater volumes than external CPs, who find these ancillary services expensive to provide to their end customers.

Duct Valuation Methodology

4.12 Vodafone would welcome greater clarity over the distinction between Backhaul duct and Inner Core duct, and the allocation of each type of duct to regulated and unregulated services.

4.13 BT's Regulatory Financial Statements provide the following definitions of the two types of duct:

a) "*Backhaul Duct is the national network of underground bores and ducting between exchange nodes that are considered part of the Openreach division's assets*";

b) "*Inner Core Duct is the national network of underground bores and ducting between exchange nodes (excluding Openreach assets)*"[34].

[32] Openreach: (£15 + £10) / £85 = 29%; 29% x £15 = £4.40. TSO: £60 / £85 = 71%; 71% x £15 = £10.60.
[33] Paragraphs 9.71 to 9.89, Cost Attribution Review consultation document

4.14 However, these definitions do little to clarify the distinction between these two types of duct, because they are based on what is "*considered part of Openreach*", without any apparent explanation of why a particular section of duct should be considered part of Openreach or not. The cost of Openreach products cannot be determined by what is considered to be part of Openreach; there must be an objective definition of the network services that Openreach provides, in order for the cost of those services to be determined.

4.15 Some clarity is provided by BT's Undertakings[35]. These define a "Backhaul Product" as a service which runs from a BT Local Access Node (i.e. a local exchange) to:

a) another BT Local Access Node; or

b) a BT Core Node; or

c) another CP's point of handover.

4.16 This appears to suggest that:

a) Backhaul duct is the duct that links local exchanges to other local exchanges or to a core node; and (by exclusion)

b) Inner Core duct is the duct that links one core node to another core node.

4.17 However, if these definitions are correct, it is difficult to understand the cost allocations that are applied. For example:

a) The services voice origination and termination, WBA, and Ethernet main link, are allocated part of the cost of Backhaul duct, but none of the cost of Inner Core duct[36]. It is not clear how these services can be delivered without linkages between core nodes.

b) The services PPC distribution and trunk are allocated part of the cost of Inner Core duct, but none of the cost of Backhaul duct[37]. It is not clear how these services can be delivered without linkages between local exchanges and core nodes.

<u>Fibre Gross Replacement Cost methodology</u>

4.18 Vodafone is concerned that the allocation of Access fibre costs between NGA fibre and non-NGA fibre[38] is not based on a coherent methodology, and does not produce plausible results.

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[34] P127, 2013/14 Detail Attribution Methods
[35] Undertaking given to Ofcom by BT pursuant to the Enterprise Act 2002
[36] Per Appendix E, 2012/13 Detailed Attribution Methods, Openreach Backhaul Fibre (PG170B) is allocated to a range of network components, including Remote - local transmission length (CO326) (allocated to call origination and termination per the Current Cost Financial Statements), Broadband backhaul circuits (CCO681) (allocated to WBA per the Current Cost Financial Statements), and Ethernet main links (CO484).
[37] Per Appendix E, 2012/13 Detailed Attribution Methods, Wholesale Inner Core Fibre (PG350N) is allocated to a range of network components, including PC rental 2Mbit link per km trunk (CO372) and PC rental 2Mbit link per km distribution (CR371).
[38] Paragraphs 9.135 to 9.149, Cost Attribution Review consultation document

4.19 In terms of results, the methodology leads to:

a) 13% of Access fibre costs allocated to NGA fibre; and

b) 87% of Access fibre costs allocated to non-NGA fibre[39].

4.20 Total fibre Mean Capital Employed (MCE) amounts to around £880m[40]. A 13% allocation of that figure to NGA suggests total NGA fibre costs of around £115m. It is hard to reconcile a figure as small as £115m with repeated announcements by BT management that NGA fibre investment is around £2,500M[41]. Clearly a lot of this investment will have been in equipment other than NGA fibre itself, including cabinets and electronics, but the scale of the difference still seems implausible.

4.21 Vodafone would urge Ofcom to seek a better understanding of the overall investment and how it is broken down into its constituent components, for a top down comparison with the results of the fibre gross replacement cost methodology.

4.22 In terms of methodology, Vodafone has serious concerns with the coherence and reliability of the approach adopted.

4.23 In particular, Ofcom explains the startling reduction in NGA Spine Fibre cable volumes from 48,000 in 2012/13 to 2,500 in 2013/14[42] primarily by reference to a reclassification of FTTC Fibre from NGA Spine Fibre to NGA Distribution Fibre[43]. It is very hard to understand how such a reclassification can be justified, given that:

a) FTTC Fibre is by definition (Fibre to the Cabinet) fibre that runs from the local exchange to the cabinet;

b) NGA Spine Fibre is by definition also fibre that runs from the local exchange to the cabinet[44]; and

c) NGA Distribution Fibre is by definition fibre that runs from the cabinet to customer premises, i.e. a physically separate part of the Access network[45].

4.24 In view of the questionable nature of this reallocation, Vodafone would also urge Ofcom to scrutinise the cause of the remainder of the reduction in NGA Spine Fibre cable volumes, the reclassification of NGA fibre to non-NGA fibre as a result of a revised allocation rule[46].

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[39] 6.2.8.4, Cartesian report
[40] Per Table 65, Cartesian report, total fibre MCE is £1,1,32m, of which £200m to £300m is Inner Core or Backhaul, leaving roughly £1,132m - £250m = £882m as Access.
[41] See, for example, page 12 of the transcript from BT's Q4 2009/10 analyst webcast.
[42] Section 6.2.8.4, Cartesian report
[43] Paragraph 9.145, Cost Attribution Review consultation document
[44] Paragraph 10.32, Cost Attribution Review consultation document; Sections 5.5.3 to 5.5.5, Cartesian report
[45] Paragraph 10.32, Cost Attribution Review consultation document; Sections 5.5.3 to 5.5.5, Cartesian report
[46] Paragraph 9.145, Cost Attribution Review consultation document

4.25 In addition, Vodafone notes that BT's methodology only estimates a split between NGA and non-NGA fibre for Distribution Fibre, and then assumes that same split for allocating Spine Fibre between NGA and non-NGA[47]. However, it is very hard to understand how this can be appropriate, given that FTTC is by definition a product that only uses Spine Fibre.

4.26 BT's records relating to recent network deployments completed over the past 5 years would be intact and Ofcom would not encounter the data gaps that cause issues when making use of historical network records.

[47] Section 6.2.8.4, Cartesian report

5. Issues identified as not clearly inappropriate

Duct Valuation and Cable Depreciation Methodology

Identification and allocation of common costs

5.1 The allocation of Access duct follows a two-step process:

a) First, Access duct is allocated between fibre cables and copper cables.

b) Then, fibre cables and copper cables are allocated between their component elements, i.e. E-side, D-side and LLU tie cables in the case of copper, and Spine and Distribution in the case of fibre[48].

5.2 In Vodafone's view, the order in which these steps are performed is obviously inappropriate.

5.3 Ignoring for the moment the relatively minor issues of LLU and FTTC tie cables, the Access duct network essentially consists of two separate physical elements:

a) duct which connects local exchanges to cabinets (or exchange side duct), which houses E-side copper cables and Spine Fibre; and

b) duct which connects local exchanges to end user premises, or distribution points close to end user premises from which aerial dropwires run (or distribution side duct), which houses D-side copper cable and Distribution Fibre.

5.4 Since fibre and copper share the same duct, and the incremental duct cost of either type of cable is very small compared with the total duct cost, duct is essentially a common cost between fibre and cable, and an allocation of that common cost is required.

5.5 In Vodafone's view, the first step in any common cost allocation exercise should be the accurate identification of the location and scale of the common cost, and the nature and volume of the services or assets to which that cost is common. However, since exchange side duct and distribution side duct are separate physical assets, and, crucially, share few if any common costs, there are in fact two separate common cost pools which require allocation:

a) the common costs of exchange side duct need allocating between E-side copper cables and Spine Fibre; and

[48] Paragraphs 9.105 to 9.118, Cost Attribution Review consultation document; Section 6.3.2, Cartesian report

b) the common costs of distribution side duct need allocating between D-side copper cables and Distribution Fibre.

5.6 This requires that that Access duct costs are:

a) first split between exchange side duct and distribution side duct; and then

b) the duct cost on each side is allocated to the cable which shares that side of the Access duct.

5.7 However, by allocating Access duct costs between fibre and copper first, and only then allocating duct costs between exchange side and distribution side, the current approach fails to achieve this. As a result, it fails to identify the location and scale of the common costs, and the nature and volume of services or assets to which those costs are common. In Vodafone's view, this makes the current approach obviously inappropriate.

5.8 Fortunately, all that appears to be required to correct this is for similar steps to be repeated, using BT's existing methodologies, but in a different order. Specifically:

a) Access duct costs can be split between exchange side duct and distribution side duct on the basis of the aggregate depreciation of fibre and copper cables on each side, as a proportion of aggregate depreciation of fibre and copper cables on both sides; and

b) duct costs on each side can separately be allocated between fibre and copper, either on the basis of depreciation, or on some other basis if the available data allows.

5.9 Vodafone estimates that this would have a material impact on the allocation of duct costs, with, for example, the duct cost allocated to D-side copper falling by over £100m a year.

Allocation basis for copper and fibre

5.10 The current allocation methodology uses the depreciation of cables (whether copper or fibre) to allocate Access duct costs between exchange side, distribution side, and, in the case of copper, LLU tie cables[49].

5.11 This might be appropriate if the cost of duct were driven by the cost of cable. However, there are several reasons to suspect that it is not: For example, in the case of copper:

a) much LLU tie cable does not use duct at all;

b) cable will often be fully depreciated before the duct it occupies, meaning that the duct associated with fully depreciated cable will be wrongly allocated; and

[49] Section 6.3.2, Cartesian report

c) one metre of exchange side duct, featuring relatively fat cables, is likely to have a much higher cable cost to duct cost ratio than one metre of distribution side duct, featuring relatively thin cables, meaning that allocation based on cable depreciation will over-allocate duct costs towards the exchange side.

5.12 As a result, Vodafone believes that cable depreciation does not form a causal basis for the allocation of Access duct costs. We would welcome a more comprehensive review of this issue within a future consultation.

6. Review of supporting evidence

6.1 Vodafone supports Ofcom's plans to explore opportunities to improve the reliability of the evidence base supporting cost allocations, but has no observations at this stage on any of the specific issues highlighted based on the information provided.

Review of documentation / Future developments

6.2 Vodafone believes that the documents currently produced in support of the Current Cost Financial Statements (CCFS) (i.e. the Primary Accounting Documents (PAD), Detailed Attribution Methods (DAM), Detailed Valuation Methodology (DVM) and Long Run Incremental Cost Model: Relationships and Parameters (DAM)) manage to combine an unhelpful set of attributes:

a) they are very long and detailed;
b) they are opaque, with vague and qualitative narrative descriptions of allocation assumptions and costing approaches;
c) they are lacking in specific and/or quantitative information; and
d) most importantly, they fail to show any clear qualitative or quantitative linkages between the detailed allocations they describe and the costs and allocations disclosed in the CCFS.

As a result, they are in practical terms of very limited use in understanding the information contained in the CCFS. In particular:

The CCFS show a relatively clear qualitative and quantitative linkage between reported product FACs of and the FACs of the underlying super-components making up those products.

However

The supporting documents, which should be an opportunity to continue that theme by showing the linkage between super-components and underlying components, between components and Plant Groups, etc, describes those linkages in the vaguest of terms, if at all.

6.3 Indeed, at times it appears as through the DAM has been deliberately designed so as to prevent readers from gaining an understanding of cost allocations. To take a specific example, whereas in previous years the "Key Destinations" table, which gives some mapping information between Plant Groups etc and components, was published as an ordinary Excel spreadsheet, allowing copying, searching, filtering, etc, in 2013/14 BT decided to publish it as a password-protected file, making copying, searching and filtering impossible, and so rendering a table with over 18,000 rows virtually unusable.

6.4 Clearly, there are some legitimate confidentiality concerns that place limits on the degree of disclosure. However, the transparency of published non-confidential information in the Cartesian report, which goes far beyond the quality of information contained in BT's supporting documents, demonstrates that BT's documents are currently very far from those limits.

6.5 Vodafone therefore strongly supports Ofcom's efforts to improve transparency, and hopes that the 2015 Documents will prove to be an important first step towards that aim.

6.6 In terms of future developments, Vodafone agrees with Ofcom's observation that a key element of transparency relates to understanding the make-up of costs for products CPs purchase[50]. In particular:

The linkage between the costs of super-components and components should be as quantitatively transparent as that between products and super-components. That can be achieved either by eliminating aggregation at the super-component level, or by providing additional tables showing these linkages.

6.7 Given the importance of each of the duct, copper, fibre and electronics cost types, it is important that there is a transparent quantitative linkage between each of these cost types and components/super-components. That can be achieved by defining each cost type as a different component, or by providing additional table showing clear linkages between Activity Groups, Plant Groups and components.

6.8 More generally, the number of attribution levels of less absolute importance than the transparency of the linkages between attribution levels. At present, since there are many levels, and that quantitative transparency is only provided for the final level (super-components to products), the overall result is an opaque system that is hard to follow.

[50] Paragraph 12.39, Cost Attribution Review consultation document

7. Answers to the consultation questions

Question 4.1: Do you have any comments on the scope and approach to this review? Specifically, do you agree with our decision to determine whether BT's attribution methodologies were clearly inappropriate by reference to the Regulatory Accounting Principles?

We warmly welcome this review, believing it to be long overdue. We congratulate Ofcom in pursuing this initiative as we appreciate it is not easy ask task to complete, but we cannot stress the importance of the Regulatory Accounts on all regulatory decision making. It has an impact on charge controls, dispute setting and even any subsequent appeals.

At a high level we concur with Ofcom's proposals, however we believe there is an urgent need for this work to go further and review the next tranche of attribution decisions.

Question 6.1: Are there any specific issues that we do not identify in Section 6 that you consider should be reviewed further? If so, please identify those methodologies and explain why you consider the current methodology might not be appropriate.

As external stakeholders we have limited insight into BT's attribution decisions and agree with Ofcom's own statements around the accessibility and digestibility of the DAM restricting our ability to comment on this.

Question 7.1: Do you have any comments on the errors we have identified in Section 7 and how we have addressed them?

The errors identified appear to be significant oversights on BT's part that would, on the face of it point to many years of over-recovery and are not in the main confined to the 2013/14 RFS. We commend Ofcom's in getting these remedied. We would welcome confirmation from on Ofcom on how long each of the errors is likely to have been present within the accounts.

Question 8.1: Do you agree with our assessment that BT's use of attribution methodologies based on pay and return on assets for general overheads is clearly inappropriate? Please provide your reasons.

Vodafone agrees with Ofcom's overall conclusions on the current "pay and return on assets" allocation methodology applied to corporate costs. In Vodafone's view, that methodology is obviously inappropriate. Vodafone submits that the same considerations that make the "pay and return on assets" allocation methodology obviously inappropriate in the case of corporate costs and TSO support function costs, make that methodology inappropriate in the case of Openreach common costs. No evidence has been advanced for the adoption of a different conclusion for the latter costs. On the contrary, many of the smaller cost categories described within Openreach common costs make it clear that the "pay and return on assets" allocation methodology would be obviously inappropriate for those cost categories. Vodafone also observes that even though this methodology only allocates costs incurred by Openreach, within Openreach, it is still capable of having a significant impact on the allocation of costs between regulated and unregulated services: 25% of Openreach revenue is from unregulated services

Question 8.2: Where we have proposed alternative methodologies to attribute general overheads in Section 8, do you agree that they provide an appropriate and practicable basis? Please provide reasons to support your answer.

Vodafone believes that the allocation bases proposed by Ofcom for the disaggregated smaller cost categories it has identified are generally reasonable. However, Vodafone does not believe it is reasonable to calculate the cost of providing the employee broadband offer benefit by reference to the retail price. Doing so results in regulated services contributing to the profits of BT's unregulated business. It would be more appropriate for this discretionary cost to be excluded entirely.

Question 9.1: Do you agree that the way BT attributes profits and losses on disposal of land and buildings is clearly inappropriate and, if so, do you agree that it should instead attribute them in the way we propose in Section 9?

Vodafone agrees with Ofcom that it is obviously inappropriate for profits on disposals of properties to be allocated only to the Retail Residual business. Vodafone agrees that this benefits BT unfairly, because in many cases these properties were used in the past to provide regulated services, and regulated services will therefore have contributed to the cost of these properties.

Question 9.2: Do you agree that the way BT attributes non-chargeable vacant space to be clearly inappropriate and, if so, do you agree that it should instead attribute them in the way we propose in Section 9?

Vodafone does not agree with the allocation of all vacant space in Operational Buildings with an MDF to Openreach rather than TSO, on the basis that Openreach is the "anchor tenant" in such buildings, i.e. on the basis that Openreach assets (MDF and cable chambers) are preventing a reduction in the size of the Operational Building portfolio due to the prohibitive cost of moving them to smaller buildings.

In the case of the revenues from surplus property space, Ofcom concludes that allocation should recognise the balance of past use of those properties. It is not clear why that same principle should not also be applied to the costs of surplus property space (i.e. vacant space). From that perspective, the vacant space in local exchanges is primarily attributable to TSO, not Openreach: it is TSO assets (switches, etc.) whose space requirement has shrunk significantly since the local exchanges were constructed, not Openreach assets.

Question 9.3: Do you have any comments on our assessment of the other attribution methodologies considered in Section 9? Specifically, do you have any information that you consider to be relevant to our assessment of whether the methodologies are appropriate and of any alternative attribution methodologies that might replace them?

BT allocates revenue from disposals of copper only to the Network Residual business. Vodafone does not agree with Ofcom's conclusions on this allocation. The current approach to disposals of copper is obviously inappropriate, for the same reasons that the current approach to disposals of property is inappropriate:

In the case of disposals of property, Ofcom concludes that allocation to the residual is inappropriate, because in many cases the properties disposed of were used in the past to provide regulated services, and regulated services will therefore have contributed to the cost of these properties.

The same considerations apply in the case of disposals of copper. In many cases, the copper cables disposed of were used in the past to provide regulated Backhaul and Inner Core services, and those regulated services will therefore have contributed to the cost of these cables.

Vodafone also has detailed concerns around BT's Fibre Gross Replacement Cost methodology and BT's approach to copper depreciation set against a backdrop of active used copper sales to realise ongoing residual values.

Question 10.1: Do you have any comments on our assessment of the supporting evidence used by BT to inform its cost attribution decisions, as described in Section 10? Specifically, do you have any suggestions for alternative data sources?

The transparency of published non-confidential information in the Cartesian report goes far beyond the quality of information contained in BT's supporting documents, demonstrates that BT's documents are currently falling short of what is required to ensure transparency and maintain quality. Vodafone therefore strongly supports Ofcom's efforts to improve transparency, and hopes that the 2015 Documents will prove to be an important first step towards that aim.

Question 11.1: Do you have any comments on our findings relating to BT's supporting documentation, as described in Section 11?

We support Ofcom's efforts to improve future documentation and would stress that our key requirement relates to understanding the make-up of costs for products we purchase.

Question 12.1: Do you consider it would be helpful to stakeholders if BT reduced the number of attribution levels in BT's cost attribution system? Please provide your reasons for or against such a change.

The linkage between the costs of super-components and components should be as quantitatively transparent as that between products and super-components. That can be achieved either by eliminating aggregation at the super-component level, or by providing additional tables showing these linkages.

Question 12.2: Do you think the current list of components or Plant Groups is appropriate? For example, do you agree that BT should report results for components, rather than super-components?

Given the importance of each of the duct, copper, fibre and electronics cost types, it is important that there is a transparent quantitative linkage between each of these cost types and components/super-components. That can be achieved by defining each cost type as a different component, or by providing additional table showing clear linkages between Activity Groups, Plant Groups and components.

Question 12.3: Does reporting of costs by network component provide a sufficiently transparent way of breaking down costs for services? For example, do you think that costs for different network elements of duct, fibre and copper should be reported separately?

We would support more granular reporting; however the number of attribution levels of less absolute importance than the transparency of the linkages between attribution levels. At present, since there are many levels, and that quantitative transparency is only provided for the final level (super-components to products), the overall result is an opaque system that is hard to follow.

In addition, we would highlight the need for greater cost transparency around the operation of BT's Payphone network. Other communications providers make a significant contribution towards running this network through the payphone access charged (currently set at 79ppm and levied on all free to caller minutes originated from payphone to CP free to caller numbers). BT makes revenue from cash calls from payphones, but also uses them as WIFI points, ATMs, internet access stations and of course sells space for street furniture advertising. We need far greater detail on the costs of the payphone network and the revenues from all sources to ensure payphone access charges are derived fairly.