



# Changes to BT and KCOM's regulatory and financial reporting 2011/12 update

Statement

Publication date:

17 April 2012



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## Section 1

# Executive Summary

## Background

- 1.1 Relevant, reliable and timely regulatory financial information informs many of our decisions. We require this information in order to monitor and enforce various obligations that are placed on dominant providers in markets where they are found to have significant market power ("SMP").
- 1.2 In this statement we set out the minor modifications we have decided to make to enhance the presentation and improve the quality of BT's regulatory financial statements ("RFS"). As set out in the February Consultation<sup>1</sup>, these modifications reflect developments over the last 12 months in the regulatory, technological and competitive environment, our ongoing analysis and use of the RFS, comments from users of the RFS and discussions with BT.
- 1.3 There are no significant modifications to the RFS in the current year. The Cost Orientation and Regulatory Reporting (CORR) project is running at the same time with the remit of addressing fundamental issues and proposing modifications to financial reporting. As set out in the February Consultation, in order not to duplicate the work, we consider that the CORR project is better placed to consider concerns in depth this year.
- 1.4 In the February Consultation we consulted on two minor modifications to BT's 2011/12 RFS. Both were modifications to reporting of services in the Alternative Interface Symmetric Broadband Origination ("AISBO") market. We proposed to disclose Ethernet Access Direct services for rentals and connections separately by bandwidth. These modifications are aimed at improved disclosure of services in the RFS. We also proposed to amalgamate Wholesale Extension Service connections due to the forecasted low revenue of these services.
- 1.5 The regulatory financial reporting regime is also applicable to KCOM. This year, however, we have identified no reporting modifications relating to KCOM which require consultation.
- 1.6 This statement sets out our final decisions in respect of the proposals in the February Consultation.
- 1.7 We have decided to implement the two modifications to AISBO market reporting that were proposed in the February consultation. These modifications are:
  - to require BT to disclose Ethernet Access Direct services for rentals and connections separately by bandwidth; and
  - to amalgamate Wholesale Extension Service connections.

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<sup>1</sup><http://stakeholders.ofcom.org.uk/consultations/bt-kcom-financial-reporting/>

## Section 2

# Introduction

## Background

- 2.1 Relevant, reliable and timely regulatory financial information is required to inform many of our decisions. It is essential therefore that the regulatory reporting framework is kept up to date and fit for purpose.
- 2.2 Under sections 87 to 91<sup>2</sup> of the Act there are a range of remedies that can be implemented by Ofcom once it has been determined that an undertaking has SMP in an identified services market. These include obligations:
- to offer cost-oriented charges;
  - not to discriminate unduly; and
  - to cap charges, i.e. charge controls.
- 2.3 When setting SMP conditions, Ofcom is exercising its duties under sections 3 and 4 and 4A of the Act. These include the duty to further the interests of consumers in relevant markets by promoting competition and to act in accordance with the six Community requirements, the first of which is to promote competition. Where these obligations have been imposed it is essential that they are monitored and enforced effectively through, in part, an effective regulatory financial reporting framework.
- 2.4 Regulatory financial information is normally prepared either on a regular (e.g. annual) basis for ongoing monitoring purposes or on request, for example in connection with investigations.
- 2.5 BT's RFS, like any form of business information, evolve over time to reflect a range of internally and externally driven factors. These include changes to accounting policies and standards, improved understanding or knowledge of cost drivers, changes in technologies and business processes and changes in the regulatory environment.

## The February Consultation

- 2.6 The February Consultation included proposals for two minor modifications that Ofcom considered were justified in order to maintain a fit for purpose reporting framework.
- 2.7 Responses to the February Consultation were received from BT, Cable & Wireless Worldwide, Everything Everywhere and Verizon Business. Collectively Cable & Wireless Worldwide, Everything Everywhere and Verizon Business will be referred to as the other communications providers (OCPs) in the rest of this document.
- 2.8 We have taken these responses fully into account in making our decisions on the modifications to the RFS, as set out in this statement.

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<sup>2</sup> As amended by the Electronic Communications and Wireless Telegraphy Regulations 2011/1210.

## Structure of the Document

- 2.9 In the February Consultation we invited comments on our proposals by way of responses to the questions we posed. This statement sets out these questions as they appeared in the February Consultation, considers the responses received and sets out our final decision.
- 2.10 In Section 3 we set out our decisions on the proposals raised in the February Consultation for BT to make improvements to the RFS.
- 2.11 The reporting modifications that we present in this document impact solely on BT. There are no reporting modifications which impact KCOM.

## Legal Tests

- 2.12 All legal tests relating to Ofcom's considerations and conclusions are set out in Annex 1. This annex should be read in the light of relevant considerations and Ofcom's conclusions as set out in this statement.

## Section 3

# Updated reporting requirements

## Introduction

- 3.1 In the February consultation we proposed two reporting modifications. The modifications relate to BT only. We present our conclusions below, having fully taken into account respondents' views on these proposals.

## Disclosure of AISBO Services

**Question 1: Do you agree with Ofcom's proposal to disclose EAD service information for connections and rentals by bandwidth?**

### Proposed Change

- 3.2 We proposed to report separately:
- EAD connections across 10Mb, 100Mb and 1000 Mb bandwidths;
  - EAD rentals across 10Mb, 100Mb and 1000Mb bandwidths.
- 3.3 The purpose of this proposal was to ensure improved disclosure of these services in the RFS.

### OCP responses

- 3.4 OCP respondents agreed with the proposed separate reporting of EAD connection and rental services by bandwidth.
- 3.5 OCP respondents also made two other comments in relation to reporting in this market. Although these comments are outside the scope of the specific consultation question we believe it is appropriate to consider these.
- 3.6 Firstly, OCPs would like to see separate reporting on internal Ethernet Backhaul Direct product volumes on the grounds that this is a strategic product that is covered by Equivalence of Input undertakings.
- 3.7 Secondly, OCPs would like to see BT provide a split between EAD Local Access circuits and standard circuits in order to be able to see migration patterns to these services. OCPs would also like have more clarity on where volumes, revenues and costs of connections from BT price lists are reported in the RFS.

### BT response

- 3.8 BT agreed with our proposal to report EAD services by bandwidth. However, BT considered that it is not necessary or appropriate to disaggregate these services into connections and rentals.
- 3.9 We have also engaged in further discussions with BT. In respect of EBD internal services, BT has stated that these are only used as an input to Wholesale products and are therefore reported as part of their costs. BT also said reporting of EBD services in the RFS is consistent with reporting for other products that are consumed

internally by BT but not sold internally, such as SMPF and BES. Therefore, publishing internal EBD volumes would be a fundamental change to the way the accounts are presented.

### **Decision**

- 3.10 We have decided to adopt the proposal to report EAD connections and rentals separately by bandwidth. This is to provide greater disclosure of services in the RFS and is consistent with the principle of transparency.
- 3.11 We have referred the question on internal EBD reporting to the Equality of Access Office.
- 3.12 The issues of reporting of Local Access connections separately and more clarity around what is included in the reported connections, will be considered following the conclusions of the Business Connectivity Market Review and of the Cost Orientation and Regulatory Reporting projects.

### **Question 2: Do you agree with the proposed change to amalgamate reporting for WES connections in the AISBO market?**

#### **Proposed change**

- 3.13 We proposed to amalgamate reporting for WES connections into one line in the RFS due to the fact that the WES connections revenues are expected to be below £5m in 11/12.

#### **OCP responses**

- 3.14 One OCP disagreed with the proposal on the grounds that the CORR project will be assessing materiality for amalgamation of services and it is inappropriate to make the change ahead of the CORR results. They also cited transparency of costs as important due to migration between WES and EAD.
- 3.15 Other OCPs agreed with our proposal.

#### **BT response**

- 3.16 BT agreed with our proposal to amalgamate reporting for WES connections. However, BT considered that it is not necessary or appropriate to disaggregate WES services into connections and rentals.

### **Decision**

- 3.17 We have decided to adopt the proposal to amalgamate WES connections reporting into one line in the RFS.
- 3.18 WES connections are withdrawn from new supply and the revenue is expected to be below £5m in 11/12. In our view it is reasonable to amalgamate reporting for WES connections. This is to ensure the RFS focuses on the main regulated services produced by BT and these are not obscured by the reporting of many small services.
- 3.19 The table below shows the required reporting in the regulatory financial statements.





## Annex 11

## AISBO Market summary

Purpose of statement: to provide more detail on financial performance and first order tests of compliance with cost orientation and non-discrimination obligations

Alternative interface symmetric broadband origination (up to and including 1Gbit)

## Summary

|      | Internal Sales<br>£m | External Sales<br>£m | Turnover (see<br>note 1)<br>£m | Operating<br>costs<br>£m | HCA<br>Depreciation<br>£m | Holding<br>(gain)/loss<br>£m | Supplementar<br>y depreciation<br>£m | Other<br>adjustments<br>£m | Roundings<br>£m | Total CCA<br>operating costs<br>£m | Return<br>£m | Mean capital<br>employed<br>£m | Return on<br>mean capital<br>employed |
|------|----------------------|----------------------|--------------------------------|--------------------------|---------------------------|------------------------------|--------------------------------------|----------------------------|-----------------|------------------------------------|--------------|--------------------------------|---------------------------------------|
| 200x | £                    | £                    | £                              | £                        | £                         | £                            | £                                    | £                          | £               | £                                  | £            | £                              | %                                     |
| 200y | £                    | £                    | £                              | £                        | £                         | £                            | £                                    | £                          | £               | £                                  | £            | £                              | %                                     |

Note 1: Comparison of Average internal and external charges with each other and with FAC

| for the year ended 31 March 200x          | Non- discrimination |        |          |                    | Cost orientation                  |                              |                                |                      |
|---|---------------------|--------|----------|--------------------|-----------------------------------|------------------------------|--------------------------------|----------------------|
|   | Turnover<br>£m      | Volume | Unit     | Average price<br>£ | FAC<br>(see<br>Section<br>5)<br>£ | Unaudited<br>LRIC Floor<br>£ | Unaudited<br>LRIC Ceiling<br>£ | Average<br>price/FAC |
| <b>Service</b>                            |                     |        |          |                    |                                   |                              |                                |                      |
| <u>Wholesale Extension Services (WES)</u> |                     |        |          |                    |                                   |                              |                                |                      |
| <u>Rental</u>                             |                     |        |          |                    |                                   |                              |                                |                      |
| Internal WES 10 Mbits                     | £                   |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES 10 Mbits                     | £                   |        | y x<br>y | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| Internal WES 100 Mbits                    | £                   |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES 100 Mbits                    | £                   |        | y x<br>y | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| Internal WES 1000 Mbits                   | £                   |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES 1000 Mbits                   | £                   |        | y x<br>y | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| Internal WES other bandwidth              | £                   |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES other bandwidth              | £                   |        | y x<br>y | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| <u>Connection</u>                         |                     |        |          |                    |                                   |                              |                                |                      |
| Internal WES                              | £                   |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES                              | £                   |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| Internal WES 10 Mbits                     | £                   | y      | x        | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES 10 Mbits                     | £                   | y      | x<br>y   | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| Internal WES 100 Mbits                    | £                   | y      | x        | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES 100 Mbits                    | £                   | y      | x<br>y   | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| Internal WES 1000 Mbits                   | £                   | y      | x        | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES 1000 Mbits                   | £                   | y      | x<br>y   | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| Internal WES other bandwidth              | £                   | y      | x        | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES other bandwidth              | £                   | y      | x<br>y   | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| <u>Backhaul Extension Services (BES)</u>  |                     |        |          |                    |                                   |                              |                                |                      |
| <u>Rental</u>                             |                     |        |          |                    |                                   |                              |                                |                      |
| External BES 1000 Mbit/s                  | £                   |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External BES other bandwidth              | £                   |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| <u>Connection</u>                         |                     |        |          |                    |                                   |                              |                                |                      |
| External BES                              | £                   |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |

**Ethernet Access Direct (EAD)**Rental

|                     |   |     |   |   |      |      |      |
|---------------------|---|-----|---|---|------|------|------|
| Internal EAD 10Mb   | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| External EAD 10Mb   | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| Internal EAD 100Mb  | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| External EAD 100Mb  | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| Internal EAD 1000Mb | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| External EAD 1000Mb | £ | y x | £ | £ | x.xx | x.xx | x.xx |

Connection

|                     |   |     |   |   |      |      |      |
|---------------------|---|-----|---|---|------|------|------|
| Internal EAD 10Mb   | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| External EAD 10Mb   | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| Internal EAD 100Mb  | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| External EAD 100Mb  | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| Internal EAD 1000Mb | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| External EAD 1000Mb | £ | y x | £ | £ | x.xx | x.xx | x.xx |

**Main Link**Rental

|                            |   |     |   |   |      |      |      |
|----------------------------|---|-----|---|---|------|------|------|
| Internal Main Link charges | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| External Main Link charges | £ | y x | £ | £ | x.xx | x.xx | x.xx |

**Other Ethernet**Rental

|                                       |   |      |      |   |      |      |      |
|---------------------------------------|---|------|------|---|------|------|------|
| Internal other ethernet all bandwidth | £ | (ux) | (sx) | £ | x.xx | x.xx | x.xx |
| External other ethernet all bandwidth | £ | (ux) | (sx) | £ | x.xx | x.xx | x.xx |

Connection

|                                       |   |      |      |   |      |      |      |
|---------------------------------------|---|------|------|---|------|------|------|
| Internal other ethernet all bandwidth | £ | (ux) | (sx) | £ | x.xx | x.xx | x.xx |
| External other ethernet all bandwidth | £ | (ux) | (sx) | £ | x.xx | x.xx | x.xx |

**Excess Construction Charges**

|                                      |   |      |      |   |      |      |      |
|--------------------------------------|---|------|------|---|------|------|------|
| Internal Excess Construction Charges | £ | (ux) | (sx) | £ | x.xx | x.xx | x.xx |
| External Excess Construction Charges | £ | (ux) | (sx) | £ | x.xx | x.xx | x.xx |

**Other Services**

|                    |   |     |   |   |      |      |      |
|--------------------|---|-----|---|---|------|------|------|
| Service 1 Internal | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| Service 1 External | £ | y x | £ | £ | x.xx | x.xx | x.xx |
|                    |   | y   |   |   |      |      |      |
| Service 2 Internal | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| Service 2 External | £ | y x | £ | £ | x.xx | x.xx | x.xx |
|                    |   | y   |   |   |      |      |      |

£

(sx) This service comprises a number of individual prices as indicated by the value of x  
 (ux) This service comprises a number of individual volumetrics as indicated by the value of x

**Key**

Service which has amalgamated other services  
 Service which has been amalgamated into other services  
 New services reported in the year



## **Legal Tests**

- 3.20 In order to implement the modifications we have decided to make, Ofcom needs to modify Direction 4 under SMP condition OA2. We have set out how we have satisfied the relevant legal tests under the Act in order to implement these changes at Annex 1.

## Annex 1

# Legal Tests

## Introduction

- A1.1 This annex sets out how Ofcom has satisfied the legal tests<sup>3</sup> required in order to modify the regulatory financial accounting obligations applying to BT.
- A1.2 As set out in Section 3 above, in order to implement our decision, Ofcom needs to modify Direction 4 under SMP condition OA2. For this purpose we show how our duties have been met under sections 3, 4, 4A and 49(2) of the Act.

### **Sections 3, 4 and 4A – general duties, the six Community requirements and the duty to take account of European Commission recommendations for harmonisation**

- A1.3 Section 3 of the Act sets out Ofcom's duties in carrying out its functions, in particular that it furthers the interests of citizens in relation to communications and furthers the interests of consumers in relevant markets.
- A1.4 Section 4 of the Act requires that Ofcom acts in accordance with the six Community requirements concerning: the promotion of competition; the development of the European internal market; the promotion of the interests of all EU citizens; non-discrimination; promoting efficiency and sustainable competition and the maximum benefit for consumers; and facilitating service interoperability and securing freedom of choice for consumers.
- A1.5 Section 4A of the Act requires Ofcom to take into account all applicable recommendations issued by the European Commission under Article 19(1) of the Framework Directive<sup>4</sup>.

### **Section 49(2) tests**

- A1.6 Ofcom has the ability to modify a direction that gives effect to an SMP obligation under section 49<sup>5</sup> of the Act but only where it is satisfied that the tests under section 49(2) have been met. The tests are that the modification of the direction is:
- a) objectively justifiable in relation to the networks, services, facilities, apparatus or directories to which it relates;
  - b) not unduly discriminatory against particular persons or against a particular description of persons;
  - c) proportionate to what it is intended to achieve; and
  - d) transparent in relation to what it is intended to achieve.

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<sup>3</sup> Including changes to the relevant sections of the Act that took effect on 26 May 2011.

<sup>4</sup> Directive 2002/21/EC of the European Parliament and of the Council of 7 March 2002 on a common framework for electronic communications and services (OJ L 108 24.04.2002, p33), as amended,

<sup>5</sup> As amended by the Electronic Communications and Wireless Telegraphy Regulations 2011/1210.

## Sections 49A and 49B

- A1.7 Sections 49A and 49B set out the relevant procedures that must be followed for domestic and EU consultations respectively on proposals to modify directions. Section 49A applies where the proposals are for the purposes of:
- a) an SMP apparatus condition; or
  - b) any other condition set under section 45 where what is proposed would, in Ofcom's opinion, have a significant impact on a market for any of the services, facilities, apparatus or directories in relation to which Ofcom has functions under Chapter 1 of Part 2 of the Act.
- A1.8 Section 49B applies where the proposals are of "EU significance". Section 150A(2) sets out the cumulative criteria that must be satisfied in order for a proposal to be of EU significance.

## Disclosure of AISBO Services

### Section 3, 4 and 4A

- A1.9 As part of the relevant EU market review process Ofcom has imposed wholesale cost accounting and accounting separation obligations (conditions and directions) on BT in specific identified markets as appropriate remedies to its SMP in these markets. The relevant individual market reviews determined that these regulatory accounting obligations met the tests outlined in Sections 3 and 4 of the Act. The modifications to Direction 4 under SMP condition OA2 are designed to enable BT to fulfil the purpose for which these particular obligations were imposed (i.e. demonstrate cost orientation and non-discrimination) more effectively and efficiently, by disclosing AISBO services in a way that aligns with the charges levied by BT on the other communication providers. In consequence Ofcom considers the modifications to Direction 4 under SMP condition meet the tests in Sections 3 and 4 of the Act.
- A1.10 In proposing the modifications to Direction 4 under SMP condition OA2, Ofcom has also taken into account all applicable recommendations issued by the European Commission under Article 19(1) of the Framework Directive, in particular Commission Recommendation of 19 September 2005 on accounting separation and cost accounting systems under the regulatory framework for electronic communications<sup>6</sup>. In consequence Ofcom considers it has fulfilled its duty under section 4A of the Act.

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<sup>6</sup> OJ L 266 11.10.2005, p64. This recommends, amongst other things, that "a national regulatory authority, when assessing the features and specifications of the cost accounting system, reviews the capability of the notified operator's cost accounting system to analyse and present cost data in a way that supports regulatory objectives", and that "national regulatory authorities make relevant accounting information from notified operators available to interested parties at a sufficient level of detail" (see paragraphs 3 and 5 respectively).

## Section 49(2) tests

### Objectively justifiable in relation to the networks, services, facilities, apparatus or directions to which it relates

- A1.11 Ofcom considers that modifying Direction 4 under SMP condition OA2 in the manner described in paragraphs 3.2 to 3.19 is objectively justifiable. The modifications we have decided to make provide for the reporting of certain services at a greater degree of granularity, and amalgamate the reporting of certain low revenue services. This is consistent with forecasted growth of revenues for these services. The modification will therefore allow us to monitor more accurately that BT is complying with its non-discrimination and/or cost orientation obligations in the relevant market, and is necessary for that purpose.

### Not unduly discriminatory against particular persons or against a particular description of services

- A1.12 Ofcom considers that modifying Direction 4 under SMP condition OA2 in the manner described in paragraphs 3.2 to 3.19 is not unduly discriminatory. BT is the only communications provider with SMP in the AISBO market which provides the relevant (or similar) services externally.

### Proportionate to what it is intended to achieve

- A1.13 Ofcom considers that modifying Direction 4 under SMP condition OA2 in the manner described in paragraph 3.2 to 3.19 is proportionate. By amalgamating the reporting of WES connection services, we are modifying BT's regulatory obligations so that the reporting of many small revenue services does not obscure the focus on the main reported services. EAD revenues have grown and therefore greater granularity of reporting will allow us to monitor more effectively BT's compliance with obligations regarding those services. The extent of BT's obligations should therefore correspond more closely with the purpose and effect of the RFS: to allow us to monitor that BT is complying with its non-discrimination and/or cost orientation obligations in the relevant market. The modification is, accordingly, no more than necessary for BT to demonstrate compliance with its obligations in the AISBO market.

### Transparent in relation to what it is intended to achieve

- A1.14 Ofcom considers that modifying Direction 4 under SMP condition OA2 in the manner described in paragraph 3.2 to 3.19 is transparent. In this statement Ofcom have explained clearly and succinctly what the modifications are intended to achieve.

## Section 49A

- A1.15 Section 49A(1)(a) has not been applicable because we are not modifying Direction 4 for the purposes of an SMP apparatus condition. Section 49A(1)(b) has not been applicable because, in our view, and for the reasons set out in Section 3 and in this annex, given their nature and consequently their limited impact our modifications will not have a significant impact on a market for any of the services, facilities, apparatus or directories in relation to which we have functions under Chapter 1 of Part 2 of the Act.

## Section 49B

- A1.16 Section 49B does not apply because our modifications are not of EU significance, as defined under section 150A(2), in particular because in our view, and for the reasons set out in Section 3 and in this annex, given their nature and consequently their limited impact, the modifications will not affect trade between Member States<sup>7</sup>.

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<sup>7</sup> The cumulative criteria that must be satisfied in order for a proposal to be of EU significance include the criterion that the proposal would, in Ofcom's opinion, affect trade between Member States (see section 150A(2)(d)).



## **Annex 2**

# **Notification of Modifications to Direction 4 (BT)**

## **Notification under section 49 of the Communications Act 2003**

### **Direction modifying Directions under section 49 of the Communications Act 2003 and SMP services condition OA2 specifying requirements for the form and content of Regulatory Financial Statements in respect of wholesale cost accounting, accounting separation and retail cost accounting**

#### **WHEREAS:**

(A) as a result of a market analysis carried out by the Director General of Telecommunications (the 'Director') and OFCOM in accordance with section 79 of the Act, BT has been designated as having SMP in respect of certain identified markets in accordance with section 79 of the Act;

(B) as a result of such SMP designations, BT has been subject to various SMP services conditions in accordance with sections 45 and 86 to 91 of the Act, including conditions OA1 to OA34 and FA10 imposing obligations on BT in respect of wholesale cost accounting, accounting separation and retail cost accounting in relation to BT's activities in those markets where BT has been designated as having SMP;

(C) the FA10 SMP services conditions have now been revoked in accordance with section 48 of the Act, but BT remains subject to the OA SMP services conditions;

(D) in complying with the OA SMP services conditions referred to in paragraphs B and C above, and in particular condition OA5, BT is required to prepare such Regulatory Financial Statements as directed by OFCOM from time to time;

(E) by virtue of the Transitional Provisions, references to the Director in any of those SMP services conditions should be read as references to OFCOM;

(F) condition OA2 includes, and FA10.2 included, in accordance with section 45(10) of the Act, the ability for OFCOM to make such directions as they consider appropriate from time to time in relation to BT's obligations under conditions OA1 to OA34 and FA10;

(G) Ofcom has made such directions under conditions OA2 and FA10.2 in relation to BT's obligations under conditions OA1 – OA 34 and FA10, although those made under condition FA10.2 now have force as if made under condition OA2 and are to be read accordingly;

(H) this modified Direction modifies Direction 4 which relates to BT's obligations under SMP services conditions OA1 to OA34, in that it sets out the form and content to be applied by BT in preparing certain Regulatory Financial Statements required by virtue of condition OA5 and Direction 3;

(I) BT is entitled to depart from the form and content set out in this Direction in certain circumstances in accordance with conditions OA7 and OA21;

(J) for the reasons set out in the explanatory statement accompanying this modified Direction, OFCOM are satisfied that, in accordance with section 49(2) of the Act, this Direction is:

- i. objectively justifiable in relation to the networks, services, facilities, apparatus or directories to which it relates;
- ii. not such as to discriminate unduly against particular persons or against a particular description of persons;
- iii. proportionate to what it is intended to achieve; and
- iv. in relation to what it is intended to achieve, transparent;

(K) for the reasons set out in the explanatory statement accompanying this modified Direction, OFCOM have considered and acted in accordance with the six Community requirements set out in section 4 of the Act, and (to the extent applicable) with their duty in section 4A of the Act, and with their duties in section 3 of the Act;

(L) for the reasons set out in the explanatory statement accompanying this modified Direction, OFCOM have considered that sections 49A and 49B of the Act do not apply;

(M) in accordance with section 49C of the Act, a copy of this modified Direction will be sent to:

- the Secretary of State; and
- the European Commission;

**NOW, therefore, pursuant to section 49 of the Act and condition OA2, OFCOM hereby gives the following modification to Direction 4:**

1. The form and content of the Regulatory Financial Statements set out in Direction 4 shall be amended as follows in Annex A to this modified Direction.
2. For the purpose of interpreting this modified Direction, the following definitions shall apply:
  - a) "Act" means the Communications Act 2003 (c. 21);
  - b) "BT" means British Telecommunications plc, whose registered company number is 1800000, and any of its subsidiaries or holding companies, or any subsidiary of such holding companies, all as defined by section 1159 of the Companies Act 2006;
  - c) "Direction 3" means the Original Direction 3 and the following modifying Directions: at Annex 2 of the *Changes to BT's regulatory financial reporting framework*, dated 31 August 2005; at Annex 3 of the *Changes to BT's regulatory financial reporting and audit requirements*, dated 16 August 2006; at Annex 4 of *BT's regulatory financial reporting requirements*, dated 30 May 2007; at Annex 4 of *Changes to BT's 2007/08 Regulatory Financial Statement*, dated 26 June 2008; at Annex 4 of *Changes to BT and KCOM's regulatory financial reporting – 2008/09 update*, dated 15 June 2009; at Annex 3 of *Changes to BT and KCOM's regulatory financial reporting – 2009/10 update*, dated 4 June 2010; and at Annex 4 of *Changes to BT and KCOM's regulatory and financial reporting – 2010/11 update*, dated 2 June 2011, which relates to BT's obligations under SMP services conditions OA1 to OA34, in that it sets out requirements for the preparation, audit and delivery of Regulatory Financial Statements in respect of wholesale cost accounting, accounting separation and retail cost accounting;
  - d) "Direction 4" means the Original Direction 4 and the following modifying Directions: at Annex 3 of the *Changes to BT's regulatory financial reporting framework*, dated 31 August 2005; at Annex 4 of the *Changes to BT's regulatory financial reporting and audit requirements*, dated 16 August 2006; at Annex 5 of *BT's regulatory financial reporting requirements*, dated 30 May 2007; at Annex 5 of *Changes to BT's 2007/08 Regulatory Financial Statement*, dated 26 June 2008; at Annex 5 of *Changes to BT and KCOM's regulatory financial reporting – 2008/09 update*, dated 15 June 2009; at Annex 4 of *Changes to BT and KCOM's regulatory financial reporting – 2009/10 update*, dated 4 June 2010; and at Annex 5 of *Changes to BT and KCOM's regulatory and financial reporting – 2010/11 update*, dated 2 June 2011, which relates to BT's obligations in that it sets out the form and content to be applied by BT in preparing certain Regulatory Financial Statements required by virtue of condition OA5 and Direction 3;
  - e) "Director" means the Director General of Telecommunications as appointed under section 1 of the Telecommunications Act 1984;
  - f) "Notification" means the notifications which set in place the obligations on BT referred to in recital (B) of this modified Direction above;
  - g) "Original Direction 3" means the Direction given under SMP services condition OA2 at Annex 4 of *The Regulatory Financial Reporting obligations on BT and Kingston Communications statement*, dated 22 July 2004;

- h) "Original Direction 4" means Direction 4 given under SMP services condition OA2 at Annex 4 of *The Regulatory Financial Reporting obligations on BT and Kingston Communications statement*, dated 22 July 2004;
- i) "OFCOM" means the Office of Communications;
- j) "Transitional Provisions" means sections 408 and 411 of the Act, the Communications Act 2003 (Commencement No.1) Order 2003, and the Office of Communications Act 2002 (Commencement No. 3) and Communications Act 2003 (Commencement No. 2) Order 2003.

4. Except insofar as the context otherwise requires, words or expressions shall have the meaning assigned to them in this notification and otherwise any word or expression shall have the same meaning as it has in the Notification and otherwise any word or expression shall have the same meaning as it has in the Act.

5. For the purpose of interpreting this modified Direction:

- a) headings and titles shall be disregarded; and
- b) the Interpretation Act 1978 (c. 30) shall apply as if this Direction were an Act of Parliament.

6. This Direction shall take effect on the day it is published.

7. The Annex to this modified Direction shall form part of this modified Direction.

**David Brown**

**Director of Competition Finance, Ofcom**

**A person authorised by Ofcom under paragraph 18 of the Schedule to the Office of Communications Act 2002**

**17 April 2012**

## **Annex A**

The form and content of the Regulatory Financial Statements set out in Direction 4 shall be amended as shown below in that the words in blue are inserted, the words struck through are deleted and the services highlighted purple and green shall be amalgamated as indicated.

## Annex 11

## AISBO Market summary

Purpose of statement: to provide more detail on financial performance and first order tests of compliance with cost orientation and non-discrimination obligations

Alternative interface symmetric broadband origination (up to and including 1Gbit)

## Summary

|      | Internal Sales<br>£m | External Sales<br>£m | Turnover (see<br>note 1)<br>£m | Operating<br>costs<br>£m | HCA<br>Depreciation<br>£m | Holding<br>(gain)/loss<br>£m | Supplementar<br>y depreciation<br>£m | Other<br>adjustments<br>£m | Roundings<br>£m | Total CCA<br>operating costs<br>£m | Return<br>£m | Mean capital<br>employed<br>£m | Return on<br>mean capital<br>employed |
|------|----------------------|----------------------|--------------------------------|--------------------------|---------------------------|------------------------------|--------------------------------------|----------------------------|-----------------|------------------------------------|--------------|--------------------------------|---------------------------------------|
| 200x | £                    | £                    | £                              | £                        | £                         | £                            | £                                    | £                          | £               | £                                  | £            | £                              | %                                     |
| 200y | £                    | £                    | £                              | £                        | £                         | £                            | £                                    | £                          | £               | £                                  | £            | £                              | %                                     |

Note 1: Comparison of Average internal and external charges with each other and with FAC

Non- discrimination

Cost orientation

| for the year ended 31 March 200x          | Turnover<br>£m | Volume | Unit     | Average price<br>£ | FAC<br>(see<br>Section<br>5)<br>£ | Unaudited<br>LRIC Floor<br>£ | Unaudited<br>LRIC Ceiling<br>£ | Average<br>price/FAC |
|---|----------------|--------|----------|--------------------|-----------------------------------|------------------------------|--------------------------------|----------------------|
| Service                                   |                |        |          |                    |                                   |                              |                                |                      |
| <b>Wholesale Extension Services (WES)</b> |                |        |          |                    |                                   |                              |                                |                      |
| <u>Rental</u>                             |                |        |          |                    |                                   |                              |                                |                      |
| Internal WES 10 Mbits                     | £              |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES 10 Mbits                     | £              |        | y x<br>y | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| Internal WES 100 Mbits                    | £              |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES 100 Mbits                    | £              |        | y x<br>y | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| Internal WES 1000 Mbits                   | £              |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES 1000 Mbits                   | £              |        | y x<br>y | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| Internal WES other bandwidth              | £              |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES other bandwidth              | £              |        | y x<br>y | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| <u>Connection</u>                         |                |        |          |                    |                                   |                              |                                |                      |
| Internal WES                              | £              |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES                              | £              |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| Internal WES 10-Mbits                     | £              | y      | x        | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES 10-Mbits                     | £              | y      | x<br>y   | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| Internal WES 100-Mbits                    | £              | y      | x        | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES 100-Mbits                    | £              | y      | x<br>y   | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| Internal WES 1000-Mbits                   | £              | y      | x        | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES 1000-Mbits                   | £              | y      | x<br>y   | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| Internal WES other bandwidth              | £              | y      | x        | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External WES other bandwidth              | £              | y      | x<br>y   | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| <b>Backhaul Extension Services (BES)</b>  |                |        |          |                    |                                   |                              |                                |                      |
| <u>Rental</u>                             |                |        |          |                    |                                   |                              |                                |                      |
| External BES 1000 Mbit/s                  | £              |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| External BES other bandwidth              | £              |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |
| <u>Connection</u>                         |                |        |          |                    |                                   |                              |                                |                      |
| External BES                              | £              |        | y x      | £                  | £                                 | x.xx                         | x.xx                           | x.xx                 |

## BT and KCOM's regulatory financial reporting

### Ethernet Access Direct (EAD)

#### Rental

|                     |   |     |   |   |      |      |      |
|---------------------|---|-----|---|---|------|------|------|
| Internal EAD 10Mb   | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| External EAD 10Mb   | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| Internal EAD 100Mb  | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| External EAD 100Mb  | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| Internal EAD 1000Mb | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| External EAD 1000Mb | £ | y x | £ | £ | x.xx | x.xx | x.xx |

#### Connection

|                     |   |     |   |   |      |      |      |
|---------------------|---|-----|---|---|------|------|------|
| Internal EAD 10Mb   | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| External EAD 10Mb   | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| Internal EAD 100Mb  | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| External EAD 100Mb  | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| Internal EAD 1000Mb | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| External EAD 1000Mb | £ | y x | £ | £ | x.xx | x.xx | x.xx |

### Main Link

#### Rental

|                            |   |     |   |   |      |      |      |
|----------------------------|---|-----|---|---|------|------|------|
| Internal Main Link charges | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| External Main Link charges | £ | y x | £ | £ | x.xx | x.xx | x.xx |
|                            |   | y   |   |   |      |      |      |

### Other Ethernet

#### Rental

|                                       |   |      |      |   |      |      |      |
|---------------------------------------|---|------|------|---|------|------|------|
| Internal other ethernet all bandwidth | £ | (ux) | (sx) | £ | x.xx | x.xx | x.xx |
| External other ethernet all bandwidth | £ | (ux) | (sx) | £ | x.xx | x.xx | x.xx |

#### Connection

|                                       |   |      |      |   |      |      |      |
|---------------------------------------|---|------|------|---|------|------|------|
| Internal other ethernet all bandwidth | £ | (ux) | (sx) | £ | x.xx | x.xx | x.xx |
| External other ethernet all bandwidth | £ | (ux) | (sx) | £ | x.xx | x.xx | x.xx |

### Excess Construction Charges

|                                      |   |      |      |   |      |      |      |
|--------------------------------------|---|------|------|---|------|------|------|
| Internal Excess Construction Charges | £ | (ux) | (sx) | £ | x.xx | x.xx | x.xx |
| External Excess Construction Charges | £ | (ux) | (sx) | £ | x.xx | x.xx | x.xx |

### Other Services

|                    |   |     |   |   |      |      |      |
|--------------------|---|-----|---|---|------|------|------|
| Service 1 Internal | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| Service 1 External | £ | y x | £ | £ | x.xx | x.xx | x.xx |
|                    |   | y   |   |   |      |      |      |
| Service 2 Internal | £ | y x | £ | £ | x.xx | x.xx | x.xx |
| Service 2 External | £ | y x | £ | £ | x.xx | x.xx | x.xx |
|                    |   | y   |   |   |      |      |      |

£

(sx) This service comprises a number of individual prices as indicated by the value of x  
 (ux) This service comprises a number of individual volumetrics as indicated by the value of x

#### **Key**

Service which has amalgamated other services  
 Service which has been amalgamated into other services  
 New services reported in the year



