Call for Inputs: Review of cost orientation and regulatory financial reporting in telecoms

UKCTA Response to Ofcom

Submitted to Ofcom: 9th December 2011

UKCTA is a trade association promoting the interests of competitive fixed-line telecommunications companies competing against BT, as well as each other, in the residential and business markets. Its role is to develop and promote the interests of its members to Ofcom and the Government. Details of membership of UKCTA can be found at www.ukcta.com.

This UKCTA response is focused solely on the BT regulatory accounting regime and cost orientation obligations as they apply to BT. KCOM is a member of UKCTA and if any UKCTA members wish to raise points in relation to the arrangements for Hull they are free to do so in their own individual response.

UKCTA welcomes this call for inputs, believing it to be a very important policy project. Regulatory Accounting and Cost Orientation underpins the entire UK regulatory regime and it is right that both issues are dealt with together under one project.

As a decade has now passed since Oftel last published its Cost Orientation guidelines the time is now right to review how cost orientation should be assessed in the future. While the current guidelines remain useful, fresh guidance is needed to take into account changing markets and the case law following recent disputes where the matter of cost orientation has been a prominent feature of proceedings.

UKCTA has long campaigned for a fundamental review of the Regulatory Accounting regime as it applies to BT. A reliable and transparent accounting regime is a prerequisite for a robust and accountable regulatory regime which is able to effectively remedy instances of market failure and combat market power. Without detailed regulatory accounting output we'd have no way to ascertain if BT had met its regulatory obligations in relation to cost orientation or charge control compliance. This information is needed more than ever, with BT's regulatory accounting output increasingly used to underpin regulatory decision making.

The 2008 & 2011 restatement and the decision to revalue the asset base in 2009/10 underlines the need for a drains up review of the entire regime. If confidence is to be maintained we need to see some real reforms to improve the quality of the output produced to increase certainty, and remove the opportunity for bias. Only when this is achieved will stakeholders be able to take advantage of the stability in the market to drive investment and benefit end consumers.

Ofcom needs to take steps to create the right kind of culture around the preparation of the accounts. It is vital that cost allocations are made using transparent and objective criteria that are designed to align with regulatory objectives and aren't influenced by the needs of the BT business.

The issues raised in this Call for Inputs are complex and the time allowed to respond was very short. UKCTA has not been able to conclude its thinking on many of the question raised. We have in many cases raised a number of points that we believe require more detailed consideration in the future stages of the consultation process.

The next section of provides an executive summary of the main areas we believe require focus and reform in both setting future cost orientation guidance and restoring faith in BT's regulatory accounting output. The remainder of the response will then focus on the specific questions raised by Ofcom in the call for inputs.

Executive Summary

Cost Orientation

- In circumstances where there is little or no effective competitive pressure and where SMP is found, Cost Orientation remains a powerful and useful remedy that helps to mimic the pricing outcomes that would be achieved in a competitive market setting.

- The Basis of Charging Obligation is clear and unambiguous, with the obligation to both comply and demonstrate compliance residing with BT and BT alone.

- The current cost orientation guidelines are equally clear, with DSAC being a first order test.

- Changing market circumstances may mean that a one size fits all approach doesn't lead to the best outcomes and in order to best mimic a competitive market situation, different cost benchmarks may be appropriate in different markets, with the determining factor being the current or prospective level of competitive market entry.

- The current guidelines are overly generous to BT, with a potentially generous DSAC ceiling being referenced in overcharging cases, while a much lower cost floor could be referenced in margin squeeze cases. This gives BT the benefit of the doubt at both ends of the spectrum and doesn't act in the consumer interest.

- Any future guidance not only has to set cost benchmarks relevant to various market circumstances. Other variables also require to be clarified, including just how long prices can be set outside recognised cost ceilings/floors before a breach is declared. Is even one day of a breach of cost orientation acceptable? Clear guidance is required.

- In reaching a decision on potential overcharging / margin squeeze, Ofcom should always give weight to the pricing outcomes that would be sustainable in a competitive market situation.

- The penalties for breaching the obligation should be reviewed, as there would be little or no incentive to be gained from requiring BT to repay only to the DSAC level and not beyond.

Regulatory Accounting

- Cost orientation obligations are only useful when stakeholders have access to robust and reliable regulatory accounting information.

- The current process for generating the accounts lends itself to too much in-built bias. A move to a more independent basis of preparation is needed. There may be a role for a third party to oversee the process, while BT continues to remain responsible for its regulatory accounting output and pricing decisions.

- The audit as it is currently devised isn't working and needs to be overhauled, moving to a stronger 'Fairly Presents in Accordance With' level of assurance. More product level auditing is required to give the accounts proper credence.

- The money spent preparing the accounts is money well spent given the volumes of SMP products purchased. More resources should be invested in preparation, not less.

- Ofcom itself needs to have a much firmer role in developing the guidance that should be followed when preparing the accounts. A regime that fines for late submission and significant inaccuracies would be welcomed, encouraging good practice.

- Well presented detail is the key to transparency. Less detail is not the answer, with more effort put into better presentation and more accessible formats.

- Communication Providers need a direct and formal means of raising questions around the accounts should they arise and the answers provided should be prompt and given without fear of the consequences of compromising BT's commercial interests.

- Linking the Regulatory Accounts back to real world accounting is a laudable aim and it should be accomplished where possible, however where this isn't possible then a solid approach to the formulation of the regulatory accounting numbers should be promoted. This will ensure that regulatory accounting output is not compromised.

Q&A

Cost orientation

Objectives of cost orientation

Q1. How important is cost orientation as a regulatory remedy in telecoms? Why is it important to you in particular?

Cost orientation is the core economic constraint for operators with SMP because:

- None of the other available remedies (price controls (at least in the way they are currently applied to a basket of services), non discrimination, transparency, etc) are able to prevent operators with SMP charging either too much, or not enough, in a way that favours their own business to the detriment of their competitors;
- It is the remedy that Ofcom has currently put in place in order to limit charges generally and to constrain the movement of individual charges within the scope of a wider charge control remedy;
- It is one of the remedies laid down by the EU regulatory framework for electronic communications services and as such it is an important part of the objective of achieving a consistent approach to regulation across the EU.

It is important to us in particular because it is the remedy that has been imposed on BT to provide important protection in particular markets and we have a good understanding of what it seeks to achieve and how it aims to promote competition in the market.

Q2. What should we seek to achieve with cost orientation, and in what circumstances?

Cost orientation should be used to control prices in the absence of effective competition in a market. It is important that prices are neither allowed to be too high, or too low, in such a way that they favour the dominant provider.

In circumstances where competing operators require access to SMP services in order to compete it is important that the price of accessing those services is not allowed to exceed the cost of providing them. If it is then either excessive prices will be passed on to consumers, when there is no ability to compete away, or competing operators will be disadvantaged against the SMP operator. In practice a combination of both is likely to happen.

In circumstances where there is the potential for investments that may ultimately help drive a more competitive environment, it is important that the SMP operator is not able to price potentially competitive assets below a sustainable efficient cost of providing them in order to discourage such investment. This may be done because of the ability to recover the cost on other SMP services (that may be less likely to become competitive) or with a view to the longer term benefits that can be derived from maintaining the dominant position.

It should be recognised that certain circumstances will justify a different assessment of costs than others. For example, certain interconnect services are only required to be consumed by competing operators and not the incumbent themselves. This provides the incumbent with an incentive to allocate as many common costs as they can against such services. Likewise when add on services (such as enhanced care packages) are frequently purchased alongside the core SMP service, it is easier for the SMP provider to inflate the price for the add on service, effectively raising the overall price for the service and hampering competition.

Accordingly, for such services it may be appropriate for Ofcom to stipulate that only incremental costs should be recovered, whereas in other cases it will be appropriate for common costs to be included.

Even in circumstances where a charge control has been imposed it is still important to ensure that individual charges are not allowed to increase or decrease to a level that is likely to harm competition.

Q3. How should cost orientation interact with other remedies, such as charge controls or non-discrimination?

The interaction between cost orientation and other remedies is important.

Where a charge control is placed upon an SMP service we believe this should be seen as the primary mechanism for constraining overall charges and driving prices towards an efficient level. However, as discussed in our answers to Q1 and Q2, charge controls that contain a basket of charges (as most now do) allow a degree of control for the SMP operator to set charges for individual services and it is important that these are constrained to prevent any of the problems described in our answer to Q2. The has to be borne in mind when wide baskets are set, as the pricing for individual services within the basket can be adversely affected and Cost Orientation is frequently the only remedy in place to prevent individual prices rising further.

The interaction with the non-discrimination obligation is also important as the potential for discrimination cannot be avoided merely by ensuring the same price is charged in all the same circumstances. As different proportions of different services are often purchased by the SMP operator in comparison with its competitors it is vital that common costs are recovered from different services in a way that does not discriminate.

Thirdly, it is important that a high level of transparency of cost accounting information is provided, as experience has shown that it is often only network operators themselves who spot inconsistencies in the way costs are allocated or prices set.

Q4. Are there other remedies that could potentially avoid the need for a cost orientation obligation, and if so what would you propose? (E.g. safeguard price caps).

In theory it would be possible to change the structure of charge control remedies in such a way as to avoid the need for cost orientation but we believe Ofcom would consider that to be overly intrusive.

Safeguard caps on their own would not be sufficient. It would be necessary to specifically consider the cost of each and every charge in order to determine the correct starting charge and the correct level of any safeguard cap. A safeguard cap that starts from a price set by the SMP operator and is not set in recognition of the cost of the specific service would not address the requirement.

However in any event cost orientation is required to prevent charges being set too low as well as too high and therefore a fundamental change would be required to charge control design that also constrained the lower limit of charges if the cost orientation obligation were to be made redundant.

The combination of these two factors would mean that such a charge control would be far more complex than those that are implemented today, which given the current difficulties of monitoring compliance with charge controls, would further exasperate the situation. Furthermore, charge controls set in such a way would also be far more restrictive in terms of the flexibility for the SMP operator to set individual prices, as Ofcom frequently expresses a desire when setting charge controls to enable the SMP provider to vary pricing within a basket structure.

In addition there are instances where charge controls are not appropriate (either because they are difficult to set or considered to be not the right tool for the circumstance) and cost orientation is considered a better alternative, as long as an appropriate level of transparency of compliance is achieved.

Current use of cost orientation

Q5. How well defined is our implementation of the basis of charges obligation? How useful are the current guidelines, and why?

The current implementation of the basis of charges obligation is clear in most respects. We list the most and least clear in our answer to Q6.

The current guidelines do provide important information on the basis of charges obligation but we would support a review of those guidelines:

- They are now 10 years old;
- The PPC dispute and subsequent appeal necessitated a practical application of the workings of the cost orientation obligation and it is appropriate to consider that experience and how the guidance can be improved;
- BT appears to have too much discretion over the method of calculation of the floors and ceilings which erodes trust and confidence in the remedy and increases the likelihood of disputes; and
- In the future the migration towards NGN services suggests that common costs will become a higher proportion of overall costs and we need to consider the implications of that on the obligation.

Q6. Which elements of our implementation of cost orientation are least clear / clearest?

Most clear

- The obligation is applied to each and every charge;
- The use of DLRIC and DSAC provide the initial basis of the appropriate recovery of common costs;

- The DLRIC and DSAC test is a first order test of compliance;
- The burden of proof in respect of compliance is on the SMP operator

Least clear

- The full spectrum of subsequent tests that may be considered – although we understand that these are not necessarily a matter for Ofcom to propose;
- How the assessment of cost orientation should be varied in the event that prices are set materially and consistently above FAC for a wide range of services that share the same common costs.

Q7. How well do you understand how BT / Kcom demonstrate compliance with the basis of charges condition? Why is that?

We understand that BT chooses to use its Regulatory Financial Statements ("RFS") as its primary method of demonstrating compliance with the basis of charges condition. As part of BT's cost accounting procedures it runs current cost accounting and long run incremental cost analysis and these are used to provide Fully Allocated Costs ("FAC"), Distributed Long Run Incremental Cost ("DLRIC") floors and Distributed Stand Alone Cost ("DSAC") ceilings under the heading of 'cost orientation'

We understand these demonstrate only compliance with the first order test and that there could be further justification that either:

- Charges outside of the DLRIC and DSAC could be considered to be cost oriented; or
- Charges within the DLRIC and DSAC may not be considered to be cost oriented

We also understand that neither Ofcom nor BT consider it to be practical to include each and every charge that is subject to the cost orientation obligation in the RFS with its associated unit costs. We are therefore not clear about how BT demonstrates its compliance in these circumstances, ie where is does not map each and every charge to relevant unit costs. We are aware of instances where stakeholders have asked BT for greater granularity in situations where they are concerned about compliance and BT has responded by claiming that it was not able to provide any such information. This is a matter of significant concern to UKCTA members, and we would also expect Ofcom to be equally concerned about this. On the face of it, BT's inability to provide information regarding each and every charge suggests that it is not compliant, given that the obligation requires BT to be able to demonstrate that compliance.

The other area we do not understand is the degree of latitude that BT has to amend its cost allocation methodologies and inputs. In recent years it has made a series of changes that appear to change any assessment of compliance. As set out below, the audit regime for BT's resulting accounts appears to sign off each iteration, regardless of that fact that it may completely contradict the previous set of numbers covering the same products. This does not send the right signal to stakeholders about the degree to which the incumbent is held to account in complying with its cost orientation obligations.

Q8. How do the cost orientation obligations in place on BT and Kcom, and our interpretation of them, compare with your understanding of cost orientation obligations on telecoms operators in other countries, particularly elsewhere in Europe?

UKCTA considers that there is little consistency across the EU in relation to the approach adopted in terms of cost orientation, nor is their a huge amount of focus on this issue in the majority of countries at present. The UK is a well established and highly competitive market and it is our understanding that the Commission permits NRA a large amount of discretion in their approach to the issue, but has issued a recommendation to NRAs recognising the importance of effective and transparent regulatory reporting

Although not in the EU, Switzerland is probably among the leading countries as far as transparency is concerned in terms of the basis and structure of cost orientation compliance. The incumbent SwissCom issues an annual 'Model Description' report providing details of the changes which have occurred to the inputs to the modelling over the year compared to the previous two years. This report covers a wide range of products, not just interconnection, but WLR, unbundling and duct access etc. Although not published widely, all interconnected parties receive the report and have the opportunity to discuss it with the incumbent. Such a transparent approach may be worthy of further consideration albeit recognising the different regulatory framework that applies in Switzerland.

Other countries worthy of mention are Netherlands and Spain.

In the Netherlands the regulator is developing a new approach, whereby they are no longer planning to impose full cost orientation but instead will rely upon on the non-discrimination requirement or the implementation of a "safety cap" (ensuring rates can not go up by more than inflation).

In Spain, the Spanish NRA is quite active at the moment in this area, reviewing the cost accounting methodology as they attempt to move towards a LRIC model. In the past there has been a tendency to impose "reasonable prices" instead of cost-oriented prices in some markets, where reasonableness is mainly based on the non existence of price-squeeze.

Q9. What are the credible alternative cost standards that could be applied in interpreting the basis of charges condition? (E.g. LRIC+, DSAC / DLRIC, FAC, etc.)

Assessing whether charges are cost oriented using the basis of charges approach is not necessarily an exact science. This is not least because it allows for an "appropriate" mark-up for [the recovery of] common costs and return on capital employed. Determining what "appropriate" means in different cases may therefore be something of a subjective test and rightly or wrongly allows room for manoeuvre. In light of this, it can be argued that the flexibility inherent in the DSAC/DLRIC floors and ceilings approach is reasonable as a first order test.

However, one of the main weaknesses with the DSAC/DLRIC approach is that it may produce an unduly large range between the floor and ceiling prices, within which prices might be considered cost oriented. This gives BT too much freedom to game the system, and it goes against the need for a cost orientation remedy to provide certainty and transparency. DSAC can only be a first order test and cannot be applied mechanistically. It is possible for prices above DSAC to be cost oriented and for prices below DSAC to not be cost oriented. DSAC should only be an initial indicator not a final arbiter.

Therefore on a case by case basis Ofcom should consider whether there are more appropriate standards that could be applied, such as FAC. Whereas DSAC/DLRIC may produce a relatively wide range of prices, FAC will arguably have a more binding effect in that it will more closely mirror the effect of a charge control with a defined outcome. UKCTA considers that it is not appropriate or indeed possible to be overly prescriptive on when FAC might be preferable to DSAC/DLRIC.

UKCTA believe that a more dynamic approach to cost orientation, with different cost standards set for different markets based on the level of current or prospective competition (with a lower cost ceiling set for markets where competitive entry is unlikely and a higher benchmark for markets where competitive entry remains a possibility) may be worth investigating.

Whatever guidelines are set, Ofcom should be as explicit as possible, leaving all stakeholders in no doubt what compliance standard is required. Ofcom will of course retain its discretion to deal with individual matters when they arise, however the guidelines will form an important part of the frame of reference available.

Likewise we believe Ofcom need to be as proscriptive as possible when setting any appropriate mark ups for common costs and take a clear view on issues around efficiency (allocative & dynamic). A more proactive approach overall would be welcomed and ultimately whatever cost standard is used, it is essential that BT is effectively challenged on its methodology and that Ofcom does not simply rely on its figures without due verification.

Q10. What do you see as the advantages and disadvantages of the different approaches, both theoretical and practical?

As alluded to above the advantages and disadvantages of differing approaches to assessing cost orientation will depend on the facts in any given case. From a practical point of view, the extent to which a cost orientation remedy is successful or not will depend on the treatment of common costs and the reliability of output such as DLRIC data, with importance placed on good quality reporting. We would expect Ofcom to focus on ensuring that common costs are not over recovered As could be the case if DSAC were always applied.

As set out below we consider that currently BT enjoys too much freedom in deciding how to address its cost orientation obligations, and has the incentive and opportunity to over-recover its costs over significant periods of time. If a dynamic market by market approach is taken, with different standard set in each any guidance should be clear on what is expected.

Q11. Which approach do you believe we should take, and in what circumstances? How does this depend, for example, on the state of competition and any other regulatory remedies imposed alongside cost orientation?

Currently BT itself determines how it adheres to its various cost orientation obligations and regulatory reporting obligations. It is permitted to establish its own models and cost allocation methods, and publish its own regulatory financial statements which are relied upon by the regulator. On the face of it this is completely inappropriate and does not offer anywhere near the degree of regulatory scrutiny required to make the cost orientation remedy effective.

It does not instil any confidence in the industry that BT's prices are in any way reflective of its costs. This is clear from the disputes which are centred on the basis of charges obligation that the industry is forced to raise in order to compel Ofcom to challenge BT on its figures. It is noteworthy that in such cases, Ofcom has frequently made multiple adjustments to BT's data given its poor quality. BT should be in a position to provide sound verified data the first time around, rather than having to do it during the course of a dispute. Closer linkage with BTs statutory accounts may be a potential way forward (we discuss this issue in greater depth in our answers to later questions).

Regardless of the state of competition, where a cost orientation obligation is in effect Ofcom should focus its efforts on ensuring that BT is held to account for both its approach to compliance and its prices. This must be done in a fair and transparent manner in order to foster confidence in the industry and reduce the need for disputes.

Cost Orientation is an important remedy either in its own right or set in conjunction with a charge control. In each case it must be complied with, in addition to any other remedies set. UKCTA suggests that one practical step Ofcom might consider is to take a more pro-active approach to examining BT's compliance with its cost orientation obligations. For example, it could commit to regular monitoring of BT's approach and methodology rather than waiting for a scheduled market review or industry dispute. In order to be truly effective and transparent, industry would also need to commit to supporting Ofcom, or at least commit to consulting closely on any such work programme. UKCTA members would be happy to do this if it meant a more transparent cost orientation regime with more scrutiny applied to BT practices.

UKCTA considers that in the long run such a monitoring regime would be an efficient use of Ofcom's time and resources. This is not least because Ofcom would be far better placed to "hit the ground running" when conducting market reviews and disputes, as well as benefitting from the likely reduction in dispute referrals.

Q12. What tests should we apply in assessing compliance with the basis of charges condition, for instance in disputes? How should this vary depending on circumstances, for instance different levels of complexity?

Disputes must be resolved in 4 months, so time is of the essence in most if not all Ofcom investigations. Combinatorial tests tend to be very complicated, involving highly complex calculations. Therefore on the face of it they would not appear to be suited to a dispute resolution process, but whether they are feasible and provide useful information will continue to need to be assessed on a case by case basis. Depending on the combination of services chosen combinatorial can provide different results, with the SMP provider likely to advocate a combination of services that would favour their own commercial interest.

As stated above UKCTA considers that, in the first instance, the DSAC/DLRIC approach may be appropriate and reasonable as a first order test. However there are examples of where such an approach simply does not work.

For example in the context of the recent MPF rental dispute, the difference between the floor (60.40) and the ceiling (162.01) is vast. If the obligation is to be between the floor and the ceiling, it therefore sets a range which is so wide as to become effectively completely meaningless..

Q13. At what level of aggregation (e.g. product level, market level, price list level) should cost orientation apply, and why?

Undue aggregation leads to more opportunity for over-recovery, less transparency and less regulatory certainty. There is also a danger that aggregation can distort the real picture and fail to provide a properly competitive environment. For example, it is not possible to mitigate the high cost of BT trunk prices simply by aggregating them with lower priced terminating segments. Distortion can also occur if components (eg trunk and terminating segments) are not bought in fixed proportions, or not bought at the same time. In order to provide the crucial certainty and transparency of an effective cost orientation remedy, it is necessary to maintain a disaggregated approach.

UKCTA considers that the basis of charges obligation reflects this view given that it requires "each and every charge" to be reasonably derived from the costs of provision, ensuring that purchasers only pay for what they use.

Q14. What impact, if any, should changes in technology have on our use and interpretation of cost orientation? E.g. the transition from copper to fibre in the access network, or the replacement of traditional telecoms network switching equipment with more modern equivalents?

We would welcome further discussion around this very important issue, particularly as the EU is currently consulting on what cost standards should apply in what circumstances.
Ofcom should not allow older regulated products to rise in price or not to fall in line with cost reductions simply because newer products emerge. Ofcom and/or BT may have strategic incentives to encourage alternative operators to migrate from a legacy product onto a new product; however in each case the prices applied should be based on underlying costs.

It would not be right to re-cast the cost orientation obligation to make it less attractive to continue purchasing an older product. This is especially the case where there is no efficient migration path from a legacy product to a new one. The proper application of a Modern Equivalent Asset (MEA) principle may mitigate the impact of technology changes, although Ofcom would need to take a more effective monitoring role to ensure that the MEA principle was used effectively. The objective should be to mimic what might be expected in a competitive market

Q15. Are there any other factors or considerations we should take into account in our review of our guidance on cost orientation? E.g. demand patterns over time, or efficiency considerations.

Efficiencies in BT's provisioning processes should be reflected as soon as possible in their costs. Ofcom should ensure that this happens, and one such way it could do this is by enacting a pro-active monitoring regime as described above.

As set out above, UKCTA does not consider that demand patterns should necessarily have any bearing on cost orientation obligations.

Regulatory reporting

Objectives of regulatory financial reporting

Q16. Should we require telecoms operators with SMP to report financial information, and if so why?

Ofcom should look at each case on its merits before deciding if regulatory reporting is required. In some cases when an SMP finding is made, regulatory accounting remedies will be required in order to prevent a SMP provider exploiting their position. In the case of BT, without access to reliable and well informed financial information it would be impossible to judge how BT was behaving and what returns were being made, thus ensuring that consumers were not being harmed. Market price alone is an insufficient indicator and the figures presented in the regulatory accounts are key tools in enabling all market players to understand the market (in which they have little or no choice except to buy from BT) and deter consumer harm. While SMP is determined on a market by market basis, it is essential that regulatory reporting captures all incremental costs and the common costs partly recovered in the SMP market.

In some situations bottom up financial models that determine pricing will be a sufficient alternative remedy to the production of regulatory accounts. It would also not be proportionate to impose a regulatory financial reporting obligation on the large number of non-incumbent players who have individual SMP designations in their respective market for fixed geographic call termination, as comparable benchmarks in the form of other CP's geographic call termination charges are readily available.

Q17. What do you see as the respective purposes of:
• The Published RFS.
• Broader regulatory financial reporting?

The published Regulatory Financial Statements represent the suite of key documents within the regulatory accounting framework and taken together they are the entire published output from the framework. While Ofcom may have access to a greater level of information and are free to probe further, other stakeholders, who have become key in pursing enforcement action to ensure compliance, must rely upon the Regulatory Financial Statements. The key document within the published output is the Current Cost Financial Statements, which in turn is reliant on other publications such as the DAM. Taken collectively, it is the figures provided within the Regulatory Financial Statements that are used to determine BT's compliance with its obligations and ensure that prices for key regulated products are being priced appropriately, thus guarding against consumer harm.

The RFS can't be viewed in isolation and are both part of and supported by a broader framework. The framework serves to support a variety of other remedies such as cost orientation to minimise the negative impact that BT's market power would otherwise have.

For example, where a product is subject to a cost orientation obligation but not a price control, then stakeholders need the RFS to be able to judge whether or not we think the cost orientation obligation is being met. Likewise where a product is also subject to a charge control we need to be able to judge whether we think the charge control modelling is being done in the most appropriate way and that no extra-ordinary events have affected the cost base during the charge control period.

The RFS are only produced in circumstances where BT has SMP. In these circumstances the RFS help stakeholders to understand what is driving the price that that they pay for key wholesale inputs and whether there are any aspects that they could provide more efficiently themselves. In so doing they may enable other providers to engage in competitive supply further up the wholesale supply chain. An example of this is voice conveyance, the majority of CPs now self supply or use another supplier for their Local to Tandem conveyance needs. This has allowed this product to be de-regulated, whereas previously BT was used to supply end to end conveyance products and had SMP in this area. This information acts as a substitute for the range of competitor pricing information that would be accessible in a competitive market.

The framework is a vital tool for both identifying and investigating margin squeeze. As Ofcom appreciate, competition investigations are incredibly complicated and in cases where other suppliers compete with BT (such as in Wholesale Calls), access to reliable RFS data to understand at least part of BT's cost base (eg. conveyance) is critical, allowing Ofcom to focus their investigation on the other costs incurred to ascertain if the retail price set by BT does indeed result in a margin squeeze. RFS detail is also vital if other stakeholders are to meet the complaint information criteria set out by Ofcom when referring any possible Margin Squeeze cases.

Information requests alone would not enable Ofcom to gain a proper insight into BT's cost base and it is crucial that BT is required to maintain and track the costs and returns on key regulated products. Without this base information we would find it difficult to believe that Ofcom could fulfil its role as the competition authority for our industry. Ofcom are also heavily reliant on industry to bring them their concerns, and without the published material this would be very difficult.

The Regulatory Framework is also a key tool for both Ofcom and industry to investigate issues around suspected discrimination or to assess differences in products supplied externally to those supplied internally. Even if insufficient data is available within the Regulatory Financial Statements, in most cases the information presented within the RFS would allow an informed line of questioning and investigation to be followed. In the recent case of BT's PPC Point of Handover charges, while the RFS detail fell short of what was required, it provided a basis for stakeholders to pursue the matter to ensure the charges (which dropped from around £11M per annum to less than £3M) were more appropriately derived, even if took a referral to the Competition Commission to achieve such an outcome.

The regulatory framework also helps to underpin the financial aspects of equivalence and Equality of Inputs, helping to ensure that the spirit of the undertakings are being complied with.

Q18. To what extent do you consider that the information currently published achieves the purposes you set out in response to the question above? Where do the current Published RFS meet, fall short of, or go beyond, these purposes? Please be as specific as possible, in terms of content, format, structure, or any other parameter.

We believe it would be helpful to break the answer to this question down into three parts: (1) the reliability of what BT produce; (2) the scope of what is produced and (3) the detail that is presented.

(1) reliability

Our confidence in the Regulatory Financial reporting regime covering BT has been severely dented in recent years with two restatements and a massive asset revaluation, all of which benefited BT at a time when the company was subject to a charge control review and series of commercially sensitive overcharging investigations. We firmly believe the timing of these changes by BT was no coincidence and Ofcom has proved powerless to intervene. Instead it chose to make adjustments to the BT supplied figures, demonstrating that Ofcom also has deep reservations about the figures produced.

BT's ability to bend and flex the figures to suit their own commercial ends is a deep cause for concern and an audit regime which apparently signs off each iteration, regardless of that fact that it may completely contradict the previous set of numbers covering the same product areas highlights the chronic weaknesses in the current framework. While we firmly believe BT is best placed to own/produce the data, we believe the incentives on BT to change the numbers should be removed, with the accounts produced in a more independent and commercially sterile environment, for example produced by a ring fenced independent body (such as or similar to the Equality of Access Office). A board of Independent overseers should be required to make some of the fundamental attribution decisions. The board could have appointed to it a majority of independent members (drawn from outside BT Group) and have the final say in how the accounts are derived, although BT would remain responsible and accountable for the output produced. The current situation is untenable as we have little confidence that numbers presented each year will still be relied upon six months later as the possibility of restatement or Ofcom adjustment are now common place.

2) the scope of what is produced

There is inevitably tension between BT and industry about the scope of the information provided and the business as usual consultations conducted by Ofcom each year serve to highlight the various tweaks that have occurred over the years as information is removed from or added to the regulatory financial statements. Broadly speaking in any market where there is failure and where BT has been found to have SMP, regulatory financial statement detail is required. This necessitates the need for regulatory reporting to cover all incremental and common cost buckets.

(3) the detail that is presented.

Ideally the information should be presented at a product level and contain details of internal and external pricing, volumes, revenue and costs, with both FAC floors and DSAC ceiling produced. Rules around the materiality of small products and aggregation of products need to be set, with due consideration given to growing and emerging products, as generally speaking the more aggregation that occurs the less useful the information. A materiality threshold of £5M is probably appropriate, but it should be a guide rather than a hard and fast rule and potential impacts on downstream competition should also be taken into account when considering materiality. The basis of preparation wrap also needs to be included. We explore the detail of what is required further in our answer to question 20.

Current use of regulatory financial reporting

Q19. Please explain how the Published RFS are used in your organisation. In general terms, please explain if and how the Published RFS are used, and in what contexts. Please explain in each case how the information in the Published RFS is used alongside other sources of information.

The primary external audience for the Regulatory Financial Statements are other CPs who have no choice but to purchase BT's products in markets where it has SMP. Regulatory Financial statements are specialist publications not designed for general consumption and will require a degree of expertise to interpret. Ofcom is also a primary user of BT's Regulatory Accounting output; however Ofcom is not considered a primary user of the published material as Ofcom's information requirements are accommodated separately by BT.

Most CPs make active use of the RFS information as a reference source. Many spend tens or even hundreds of millions of pounds on regulated products and it is vital that CPs are able to understand the underlying costs used to derive the regulated charges they pay. This is particularly the case if they are in a market (which is the norm) where they are competing head to head with BT's own retail offering and the regulated component makes up a large proportion of the cost base.

CPs use the accounts:

- To investigate issues that come to light. e.g in Ofcom consultations, through carrier buying relationship with BT, other regulatory projects – this is reactive use of the information; and
- Proactive use – i.e reading the accounts in order to try and get a better understanding of how BT determines its costs and how they map to prices

It is the detail that is important, particularly volumes and breakdown of costs by individual components. The market statements provide context and help guide the reader into the document. The accounts are used mainly by the regulatory teams, consultants working on behalf of the communication providers or by the carrier relations teams.

The headline objective of any Regulatory Financial Statement has to be the ability to demonstrate cost orientation. This is true for charge controlled and non-charged controlled products. The accounts must also demonstrate that BT has not discriminated in favour of BT Group businesses in downstream markets. Evidence of compliance is an essential tool as it both deters BT from acting in a discriminatory manner and provides data that is essential for CPs to monitor compliance.

Where applicable, the financial aspects of equivalence should be open to scrutiny. Where a product has SMP and is a key wholesale input into other CP-provided telecommunication services, CPs need to understand the cost drivers behind the SMP product to ensure that it is being efficiently provided. Decisions over cost apportionment (which can be arbitrary) should be clearly documented to enable scrutiny – thus promoting best practice and competition within the sector.

The publication of this information at a product level should allow Margin Squeeze analysis to be carried out in a straight-forward and transparent way.

Q20. More specifically, please explain how you use specific sections or tables in the financial statements, noting which sections or tables you use, which are helpful, and which are not.

Section 7 *Review of Access Markets* and Section 8 *Review of other wholesale markets* are the most valuable to users. These sections contain the most important tables which set out the underlying cost, volume and revenue information, including key indicators like DLRIC FAC and DSAC values for each product. Volume information relating to both internal and external sales is very useful. Depending on what product mix is purchased, each UKCTA member (and indeed anyone buying regulated products from BT) will have a particular product focus. The other supporting information and reconciliation statements are also useful, particularly if an issue is being looked at in more detail. The least useful parts of the current publication are perhaps the text based sections such as the audit report and the basis of preparation which are often only referred to if a specific change has occurred.

The table below attempts to set out the relative importance of the information contained with the Regulatory Financial Statements:

	Cost	*Charge*	*Price*	*Margin*	*Discrim*	*EoI*
Product revenues	✓✓	✓✓	✓	✓✓1	✓✓	✓✓
Product costs	✓✓	✓✓	✓✓	✓✓1	✓✓	✓✓
Product volumes	✓✓	✓✓	✓✓	✓✓1	✓✓	✓✓
Product usage (of components)	✓✓	✓✓	✓✓	✓✓1	✓✓	✓✓
Above information split between internal & external supply	✓✓	✓✓	✓✓	✓✓1	✓✓	
Component costs	✓✓	✓✓	✓✓	✓✓1	✓✓	✓✓
Costs shown as operating costs, depreciation, capital employed	✓✓	✓✓	✓✓	✓✓1		
Understanding of common vs direct costs	✓✓	✓✓	✓✓	✓✓1		
Internal purchases of SMP products (costs and volumes) 2				✓✓1	✓✓	✓✓
Details of costing methods	✓✓	✓✓	✓✓	✓✓1	✓✓	✓✓
Details of attribution methods	✓✓	✓✓	✓✓	✓✓1	✓✓	✓✓
Reconciliation to financial accounts	✓✓	✓✓	✓✓	✓✓	✓✓	✓✓

Key
✓ - Useful Information ✓✓ - Required information
Notes
1 - where market under investigation has SMP, if not some of these will not be possible
2 - in downstream markets to those being notified

Q21. One of the issues we are likely to consider is the level of detail provided in the Published RFS. To inform this review, it would be helpful if you could provide examples of the way you have used the Published RFS in the past. Where possible, please link these back to your view of the purposes for the Published RFS provided in response to the question above.
• Problems caused by excessive detail (either in the provision or interpretation of the information).
• Good regulatory outcomes made possible by the current level of detail (please make your examples as specific as possible).
• Better regulatory outcomes that may have been achieved (e.g. more timely resolution of issues) had different information been provided.

Even in their current imperfect state the regulatory accounts have provided an insight into BT's cost base for regulated products and allow both CPs and Ofcom to investigate particular areas in more detail where necessary. They have also enabled CPs to escalate matters or bring formal disputes where appropriate, and over the years a number of cases have been brought before Ofcom that have relied in full or in part on the data contained within the published Regulatory Financial Statements. Several examples are cited below; this list is not exhaustive:

- The 2008 PPC overcharging dispute would never have been possible without RFS data and while there was a great deal of frustration about the inadequate data around PPCs within the accounts, there was enough material to enable a dispute to be referred and for Ofcom to complete an investigation.

- BCMR Consultation: the accounts were extensively used to help CPs respond to and challenge assumptions in the 2008 BCMR and 2009 Leased Line Charge Control. While much of the detail may have been absent, there was enough anomalous information to take the matter further, with BT having to re-price PoH charges as well as other SMP products.

- In 2004 a dispute about the PPP charges for voice was referred on the basis of the information contain within the accounts. This was because year on year these charges moved around significantly relative to their floors and ceilings. Ofcom investigated BT's regulatory accounts to strip out any cost elements which should not have been placed in the PPP category. The dispute resulted in a complete policy review by Ofcom – the PPP cost base now includes marketing costs to BTR as well as BT's competitors and are recovered across all volumes (BT Retail included).

- LLU /WLR 2009 Charge Controls: the accounts were used extensively by CPs responding to the consultation process and in the subsequent challenge of the charge control decision. The accounts were crucial in identifying areas that needed greater investigation and where further probing was required.

- ISDN 30 Intervention: Ofcom launched a policy project to investigate BT's high returns in the market for ISDN30 services.

In summary had industry not had access to RFS material, BT's profits would have been greater as it was able to leverage its market power in SMP product areas to the detriment of its competitors and ultimately consumers. Ofcom relies upon industry to raise matters, so without the published accounts UK consumers would be significantly worse off and competition would be weaker.

Q22. How do the regulatory financial reporting obligations in place on BT and Kcom compare with your understanding of regulatory financial reporting requirements on telecoms operators in other countries, particularly elsewhere in Europe?

As UKCTA is a UK focused organisation we have little direct experience of the regulatory reporting regimes developed elsewhere. Achieving the right regulatory accounting outcome is a challenge for any regulator and as the UK market is one of the most competitive in Europe the issues at stake are more frequently aired and the debate is more advanced. The frequency of BT's restatement/revaluation action is to our knowledge unique in Europe so even if a best practice example was available, it might not map well onto to the UK's circumstances. We would welcome Ofcom's insight into the approach of other NRAs. In the UK other sector regulators have different approaches that we believe may be a useful reference point, for example:

Ofwat & Ofgem has fined heavily for misreporting:

Ofwat

- Thames Water - £9.7m (0.7% of turnover) in April 2008 for misreporting customer service information.
- Southern Water - £20.3m (3.6% of turnover) in February 2008 for Deliberately misreporting customer service information
- Severn Trent Water - £35.8m (3% of turnover) in July 2008 for Deliberately misreporting customer service information

Ofgem

- CE Electric - £7.6m in June 2007 for misreporting customer interruptions information. Rather than a financial penalty, this was imposed as a modification to the licences held by CE Electric.

Ofwat also appoints a Reporter to oversee the regulatory accounting process. The Reporter has a primary duty of care to Ofwat and is appointed and paid for by the company. The Reporter undertakes a Technical/engineering/financial review of business plans and works with auditors to review assumptions, methodologies, benchmarks & investment plans. Ofwat not only uses reporters but sets out detailed regulatory accounting guidelines that they and the water companies must follow.

The FCC in the United States also manages a reporting regime for the regional telephony providers. The regime is generally regarded as transparent (with information published in full and available online in accessible format - excel or similar). The accounts structure and allocation methodologies are set by regulator

Options for regulatory financial reporting

Q23. What high-level principles should regulatory financial reporting follow? Or, put another way, how would you describe good regulatory financial reporting? (E.g. "the Published RFS should link closely to the statutory accounts or management accounts".)

As stated above the headline objective of any Regulatory Financial Statement has to be the ability to demonstrate cost orientation. This is true for charge-controlled and non charge-controlled products.

The accounts must also demonstrate that BT has not discriminated in favour of BT Group businesses in downstream markets. Evidence of compliance is an essential tool as it both deters BT from acting in a discriminatory manner and provides data that is essential for CPs to monitor compliance.

Where applicable, the financial aspects of equivalence should be open to scrutiny. Where a product provided by an operator that has been found to hold SMP is a key wholesale input into other CP provided telecommunication services, CPs need to understand the cost drivers behind that product to ensure that it is being efficiently provided. Decisions over cost apportionment (which can be arbitrary) should be clearly documented to enable scrutiny – thus promoting best practice and competition within the sector. The publication of this information at a product level should allow Margin Squeeze analysis to be carried out in a straight forward way.

Like in the case of Ofwat, there may be role for Ofcom in setting firm guidelines around the preparation of the accounts.

While it is always preferable to base the accounts on real world management accounts, the nature of regulated products means this is often not possible, especially where regulated and non-regulated product share common assets, making the fair apportionment of the assets key.

Q24. What credible options could we take for our approach to the Published RFS and wider Regulatory Financial Reporting Framework? The options could vary on a number of dimensions, for example:
• The level of detail provided.
• The cost standard(s) used.
• The estimation of asset values, and the treatment and presentation of holding gains and losses when using current cost accounting (CCA).
• Publication vs. private provision of information to Ofcom.

The current regime does need a radical overhaul to ensure that the basis of the reporting framework is both more independent and less partisan. A redesign of BT's accounting structure is also required, where the activities and costs associated with all regulated products are separated out as far as possible. This is more straightforward for Openreach, buy may be more problematic for BT Wholesale, where there is more of a mix of regulated and non-regulated products.

Openreach is critically different to the rest of BT as it represents an enduring monopoly power and competition is limited. If Openreach was supported by a separate statutory/management accounting regime, with minimum transfers from 'group' to Openreach, then ideally more data could be used to populate the Regulatory Accounts and in a more useful way. Examples might include:

- Ensuring no cost data is confidential
- Simplifying accounting structure and allocation methodologies
- Restructuring of general ledger

- Providing full, on-line, quarterly publication of results
- Allowing Ofcom to oblige BT to change its allocation rules if unreasonable.

For BT Wholesale the same broad principles should be used, with an acceptance that it will be more complicated as not all of BT Wholesale's services are regulated. This approach would:

- Simplify cost allocation methodologies
- Provide a clearer split of costs between Wholesale and other parts of BT – Retail, Group and other
- Enable greater transparency of costs of regulated services

Concerns would still be felt around the reliability of the data and allocation of costs around the group, although an independent approach to preparation would go some way to alleviate these concerns.

UKCTA also has concerns about the fluctuations in DLRIC and DSAC values, with BT's numbers changing significantly year to year. It might be worth exploring a more straightforward means of calculating floors and ceilings, by for example consider applying a range of standard floors and ceilings for different types of services.

For example: a +/-X% of FAC as proxy for DSAC/DLRIC for use in charge controls for service type X

- Ofcom can do a detailed review of individual ranges when appropriate – which would arguably encourage BT to demonstrate compliance with SMP obligations on a more regular basis
- This would be significantly more straight-forward to produce, understand and would be far less prone to fluctuation.

Q25. What factors should we take into account when weighing up the different options, and why? Which factors do you see as most important? Examples might include timeliness, accuracy, ease of use, transparency.

Accuracy along with predictability are the most crucial factors. It is very unhelpful to see large swings year to year when there is little underlying change in both the supply, demand or indeed the real cost of providing the service. This does not foster confidence or trust in the data. Transparency is also crucial, and BT has in the past staked a far wider claim of confidentiality than can be justified.

If the accounts were in a more user friendly format that would also aid usability, understanding and transparency. Timeliness is important; while sufficient time should be allowed to enable BT to prepare the accounts, extensions should only be granted in exceptional circumstances and we should end the annual delay period that results in late accounts year on year.

Q26. How would you rate each option against these factors? Bear in mind the trade-offs between different possible factors; for example, increased amounts of detail might very well *increase the length of time that the Published RFS take to produce each year. Or decreased detail might increase ease of use but might also reduce overall transparency.*

Accuracy and detail are the top two requirements. If the publication format was more accessible then this would aid transparency. The accounts are always going to be specialist publications, designed for industry experts so the detail is important. Quickly prepared accounts that lack detail are not the answer and would not meet the needs of industry, with consumers ultimately suffering as issues would go unnoticed. Where there are questions there should be a formal mechanism for these to be answered, as to date BT has chosen to ignore difficult questions, especially when disputes are ongoing and they perceive their answers may damage their commercial interests. This ultimately gives rise to a general reluctance by BT to engage with industry, which again does not help confidence or the sense of transparency in the process.

Q27. How should regulatory financial information relate to statutory financial information, if at all?

In a perfect world it would be ideal to trace everything back to statutory financial information; and where this is possible it should be done, but not at all costs. In the case of Openreach, particularly if it was a more ring fenced organisation this would be possible. For other parts of BT it would be far harder to achieve, although it should still be possible to trace the formation of the RFS data to the real statutory accounting information.

Q28. Who should control the detailed "rules" by which regulatory financial reports are prepared? What do you consider to be the advantages and disadvantages of responsibility for the decisions on the appropriate allocation methodologies resting with BT, with Ofcom or with a third (independent) party?

It is clear that the current arrangements are not working, with BT having far too much control and Ofcom being unable to influence BT's approach, instead having to resort to making post accounting adjustments. While BT should formally own and be accountable for the data, the rules governing the basis of preparation and attribution decision should be determined by an independent third party such as Ofcom or an EAO type organisation that has an independent element to its composition. This would help to ensure any regulatory accounting rules are set autonomously and cannot be influenced by BT's commercial interests.

Q29. What would you consider to be the advantages and disadvantages of requiring some of BT's regulatory financial reporting information – for example the DSAC / DLRIC estimates – to be prepared by a third party other than BT?

There would be a significant advantage in having a third party involved in the preparation of the accounts provided they were given full access to all the information required and BT retained ownership/accountability of the numbers produced. For example the DLRIC output is currently not subject to an audit, so a new LRIC model, overseen by an independent body would be a useful exercise and would hopefully highlight the inadequacies in the FAC data.

The current incentives on the individuals tasked with preparing the accounts are fundamentally flawed, with BT's own commercial interests getting in the way of its obligation to comply with its regulatory duties.

Q30. How can we best ensure timely and accurate delivery of regulatory financial information?

If we set a realistic timetable for publication such (eg. 14 weeks after year end) and ensure extensions are only granted in exceptional circumstances, with a hefty fine structure in place for late publication, this will drastically improve the delivery of the information and ensure adequate resources are deployed and that BT places the appropriate emphasis on preparing this vital information. Given the hundreds of millions spent on BT SMP products, BT should invest the appropriate time and resources to ensure that quality accounts are produced and it should be compelled to do this if necessary.

Audit of Published RFS

Q31. How much assurance do you take from the audit opinions currently provided on the Published RFS? Do you take a different level of assurance from a 'Fairly Presents' opinion compared to a 'Properly Prepared' opinion?

UKCTA members have little confidence in the current audit approach as it has failed to prevent a series of damaging restatements and asset revaluations. Ofcom has rightly highlighted that not all parts of the Published RFS are currently audited; and the audit is carried out at market level rather than product level. These limitations need to be carefully addressed in order to build a level of confidence that can give the assurance that we believe is necessary.

Although BT specifies and pays for this audit, the auditors also have a duty of care to Ofcom, In practical terms, we are unclear just how effective the duty of care to Ofcom has proved to be and we'd welcome some insight from Ofcom on how duty of care is viewed, the extent of the dialogue that currently takes placed between the auditor and Ofcom, and whether there is any way in which the duty of care to Ofcom can be strengthened, for instance by Ofcom taking a greater role in the instructions that are given to the auditor prior to their audit.

'Properly prepared in accordance with' provides assurance that the statements in question have been prepared in line with the accompanying accounting policies; it does not consider the merits of those policies. 'Fairly presents in accordance with', on the other hand, goes further, in that it assesses the merits of the significant judgements involved in preparing the statements.

Given the enduring bottleneck in relation to fixed infrastructure delivering access connectivity, the RFS have a unique role to play in ensuring BT's compliance with SMP conditions. The absence of a *Fairly Presents in Accordance With* opinion is severely damaging to the investment conditions faced by new market entrants. The restatement of BT's RFS in 2008 was a serious concern and the 2011 restatement of DSAC methodology has undermined and diluted our confidence in the level of audit that has been applied. We believe it is time to increase the scope of the audit down to a product level and enhance the assurance provided by requiring the auditor to provide a 'fairly presented in accordance with' opinion. An enhanced duty of care to Ofcom is also something we would see merit.

Q32. How should the audit framework function for the Published RFS?
• Which parts of the Published RFS should be audited, and to what level of detail?
• Should there be rules around the appointment of auditors of the Published RFS, and if so what should these be?
• To what audit standard should any audit of the regulatory financial statements be carried out (I.e. fairly presents / properly prepared)?

Which parts of the Published RFS should be audited, and to what level of detail?
We observe that the problems leading to and deriving from the recent restatements would have been much less likely to occur had the Secondary Accounting Documents, namely the Detailed Attribution Methods, the Detailed Valuation Methodology and the Wholesale Catalogue fallen within the scope of audit.

We would strongly favour the extension of the scope of audit to include these secondary documents in addition to the published DSAC & DLRIC numbers and any related underlying assumptions.

Should there be rules around the appointment of auditors of the Published RFS, and if so what should these be?

We acknowledge that any audit can be an onerous process and that the auditor may be called upon to exercise degrees of judgment in reaching its opinion, particularly when the audit opinion meets the 'properly prepared' standard. Any requirement that may result in separate auditors working on the two sets of accounts would not only increase expense but also may result in inconsistencies of approach where judgment is applied. In our view therefore, Ofcom should only seek to amend the rules relating to the appointment of auditors in the event that sufficient confidence cannot be gained by strengthening (i) the instruction and scope of audit and (ii) the level of audit opinion obtained.

Overarching questions on regulatory financial reporting

Q33. What other issues should we consider in relation to regulatory financial reporting?

As we stated at the outset, given the short time allowed UKCTA has not been able to conclude its thinking on many of the questions raised and we look forward to ongoing dialogue with Ofcom. It is abundantly clear to us that detailed, accurate and transparent regulatory accounting information is essential. As much material as possible should be published as the data only relates to markets where BT has significant market power. Claims of confidentiality should be treated with caution and material should only be withheld from publication where there is clear and justifiable concerns surrounding its publication.

We can't envisage how Ofcom could continue to perform its role as a sector regulator when concluding market reviews, setting forward looking charge controls or resolving complaints/disputes if RFS material wasn't available. Likewise if there was a significant reduction in the detail published then we believe there would be a serious impact on consumers as matters to their detriment would be left unresolved/undiscovered. If this situation were ever to occur how Ofcom could expect to perform its duties?

We understand that Ofcom has access to a large amount of unpublished BT RFS material in the form of the 'flat file'. It is not clear to us how that information is used or indeed if it is even comprehensible to Ofcom. We would like to see far more proactive use of this information as it is undoubtedly in the consumer interest if issues are identified early or indeed at all. The current information asymmetry prevents other communication providers from taking an active role in identifying many matters of worthy of further investigation.

Q34. In summary what major changes, if any, do you consider need to be made to the regulatory financial reporting currently imposed on BT (and Kcom) and what do you consider should be Ofcom's top three priorities for its review of the regulatory financial reporting framework?

To recap, we believe the following issues are key to this review:

- The current process for generating the accounts has resulted in a series of well documented flaws and errors. A move to a more independent basis of preparation is needed.
- The audit as it is currently devised isn't working and need to be overhauled.
- Ofcom itself needs to have a much firmer role in developing the guidance that should be followed when preparing the accounts.
- Well presented detail is the key to transparency. Less detail is not the answer.

- END -