



Cost Forecasting and Allocation Models

Review of financial model

March 2012

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Reliance Restricted

The Office of Communications (Ofcom)
Riverside House
2a Southwark Bridge Road
London
SE1 9HA

29 March 2012

Dear Sirs

Review of Cost Forecasting and Allocation Models

Scope and limitations of our work

In accordance with our engagement letter dated 3 November 2010 addressed to you (the '**Original Engagement Agreement**', attached as appendix B), amended by the scope extension letter (the '**Scope Extension Letter**', attached as appendix A), we planned and performed a review, using reasonable skill and care, in the context of your requirements, of certain financial models (the '**Models**', as defined below). The Original Engagement Agreement and Scope Extension Letter shall be referred to collectively as the '**Extended Engagement Agreement**'. The scope and limitations to the scope of our work, including our terms of business, are set out in the Extended Engagement Agreement and this report should only be read in conjunction with the Extended Engagement Agreement.

Our scope of work was limited to the review of the Models as outlined in our Extended Engagement Agreement. In particular, our review was limited as follows:

1. We have not been required to express any opinion on the validity of the assumptions, commercial risks associated with the project nor on the possibility of the financial projections being achieved.
2. We have not made any recommendations to Ofcom, nor have we advocated a particular approach or strategy that Ofcom should follow.
3. Our review focuses only on the contents of the Models as presented to us.
4. We did not test or assess any macros included in the Models.

You notified us that you decided to undertake the review of the Designated Sensitivities (Item 2 of the Additional scope of work requirements in the Scope Extension Letter) yourself, and this was removed from the scope of work requested.

In performing our review, we have taken account of explanations and information provided to us by Ofcom in relation to the intended operation of the Models.

The Models

Within this letter, the updated CF Model, CA Model and RAV Model, all developed by Ofcom, (each as identified below) shall be collectively known as the '**Models**'. This Report should only be used in conjunction with the Models and the findings of this report may not be valid for any versions or variations of the Models other than those identified in this Report.

Cost Forecasting Model (the 'CF Model')

The CF Model was developed by you as a regulatory model to assist in the determination of costs incurred by Openreach / BT (the '**Regulated Entity**') in running the copper network for the local telecommunications access (the '**Project**').

The objective of the CF Model, for the purposes of our review, is to generate the following key outputs: projected costs summarisation, projected profit and loss accounts of the Regulated Entity, and all the outputs with costs, volumes and other parameters to be used in the Cost Allocation Model. Those are presented on an annual basis for six periods starting in 2009/10. (Note: 2014/15 not used.)

The base case CF Model is composed of the file *CF Statement.xlsm*, dated 27/03/2012 and size 1,444,676 bytes.

Regulatory Asset Value model (the 'RAV Model')

The RAV Model was developed by you to restate the value of copper and duct assets acquired prior to August 1997 from a Current Cost Accounting ('**CCA**') value to an indexed Historical Cost Accounting value ('RAV Value').

The objective of the RAV Model, for the purposes of our review, is to generate the following key outputs: the Regulatory Asset Value for copper and duct assets and annual CCA costs to be used in the CA Model. Those are presented on an annual basis for six periods starting in 2009/10.

The base case RAV Model is composed of the file *RAV_(Audit).xlsx*, dated 07/03/2012 and size 842,921 bytes.

Cost Allocation Model (the 'CA Model')

The CA Model was developed by you to allocate the cost and asset outputs from the CF Model and RAV Model to individual services to arrive at the unit cost estimates.

The objective of the CA Model, for the purposes of our review, is to generate projected unit costs on a RAV adjusted CCA basis for all services provided by the Regulated Entity. Those are presented on an annual basis for six periods starting in 2009/10.

The base case CA Model is composed of the file *CA Statement.xlsm*, dated 27/03/2012 and size 12,486,003 bytes.

Selected source data

Ofcom have prepared the Models using input data from a number of sources. Ofcom identified certain elements of this data (the '**Selected Data**') in the file *Sources of evidence.xls* (dated 27 January 2012, size 19,439 bytes). We tested the consistency of the Selected Data with the Models and the summary of our findings is shown in item 2 below.

Further comments regarding the Selected Data are set out in appendix C.

Summary of review findings

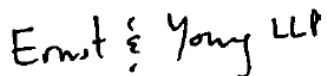
1. We are not aware of any matters which came to our attention in the course of our review to indicate that the Models have not been constructed appropriately, in so far as their logical integrity and arithmetic are concerned, so as to materially achieve the objectives described above under the base case assumptions, except for our comments in appendix C;
2. We are not aware of any matters which came to our attention in the course of our review to indicate that the Selected Data has not been transcribed into the Models in accordance with your explanation of how the Selected Data should be entered into the Models, except for our comments in appendix C.

Distribution and use of this report

This report has been prepared on your specific instructions solely for the purpose of the Project and should not be used or relied upon for any other purpose. This report should not be quoted, referred to or shown to any other parties, except as otherwise permitted in accordance with the Extended Engagement Agreement or with our prior written consent.

We accept no responsibility or liability to any person other than to our client, Ofcom, in respect of this report and accordingly if such other persons choose to rely upon any of the contents of this report they do so at their own risk. Please refer to the attached Disclaimer Notice for further details in this respect.

Yours faithfully

A handwritten signature in black ink that reads 'Ernst & Young LLP'.

Ernst & Young LLP

Appendices

- Appendix A** **Scope Extension Letter**
- Appendix B** **Original Engagement Agreement**
- Appendix C** **Matters arising from our review**

Appendix A Scope Extension Letter

Private and confidential

Director of Competition Finance
The Office of Communications (Ofcom)
Riverside House
2a Southwark Bridge Road
London
SE1 9HA

7 February 2012

Dear Sirs

Review of financial model

This letter is supplemental to our engagement agreement dated 3 November 2010 (the '**Original Engagement Agreement**') relating to the work that you have requested us to perform in connection with the Project (defined below). All terms and conditions in that agreement remain unchanged except that the scope of the work that we are required to perform is expanded to include the work set out in the section below. Such additional work will be covered by all the terms and conditions contained in our engagement agreement, including the limitation of liability provisions. For the avoidance of doubt, the aggregate liability of our firm contained in the limitation of liability provisions will not be increased as a result of this additional work.

Additional scope of work

You have asked us to perform an update review of the Cost Forecasting Model and review two further models, the Cost Allocation Model and the Regulatory Asset Value model.

Cost Forecasting Model (the 'CF Model')

The Cost Forecasting Model was developed by you as a regulatory model to assist in the determination of costs incurred by Openreach / BT (the '**Regulated Entity**') in setting up and running the copper network for the local telecommunications access (the '**Project**').

We performed a review of the Cost Forecasting Model and issued our report dated 1 November 2011. Ofcom have since made changes to the Cost Forecasting Model.

The objective of the CF Model, for the purposes of our review, is to generate the following key outputs: projected costs summarisation, projected profit and loss accounts of the Regulated Entity, and all the outputs with costs, volumes and other parameters to be used in the Cost Allocation Model. Those are presented on an annual basis for six periods starting in 2009/10.

Regulatory Asset Value model (the 'RAV Model')

The RAV Model restates the value of copper and duct assets acquired prior to August 1997 from a Current Cost Accounting value to an indexed Historical Cost Accounting value.

The objective of the RAV Model, for the purposes of our review, is to generate the following key outputs: the Regulatory Asset Value adjustments for copper and duct assets to be used in the CA Model. Those are presented on an annual basis for six periods starting in 2009/10.

Cost Allocation Model (the 'CA Model')

The CA Model allocates the cost and asset outputs from the CF Model and legacy asset RAV adjustments from the RAV model to individual services to arrive at the unit cost estimates.

The objective of the CA Model, for the purposes of our review, is to generate projected profit and loss accounts and unit costs on a CCA basis for all services provided by the Regulated Entity. Those are presented on an annual basis for six periods starting in 2009/10.

The Models

Within this letter, the updated CF Model, CA Model and RAV Model shall be collectively known as the 'Models'.

You anticipate that there will be file links ('**Model Links**') between the CF Model, CA Model and RAV Model.

Selected source data

You have prepared the Models using input data from a number of sources. You may collate together certain selected elements of this data (the '**Selected Data**') and provide this to us in the course of our review, identifying where this data is to be input in the Models.

Additional scope of work requirements

You have asked us to undertake a review of the Models to assist you in determining whether:

1. the Models have been constructed appropriately, in so far as their logical integrity and arithmetic are concerned, so as to materially achieve the objectives described above under the base case assumptions;
2. the Models have been constructed appropriately, in so far as their logical integrity and arithmetic are concerned, so as to materially achieve the objectives described above after adjusting the base case assumptions to reflect certain designated sensitivity cases (the '**Designated Sensitivities**', to be defined;
3. The Selected Data has been transcribed into the Model in accordance with your explanation of how the Selected Data should be entered into the Models.

Our assessment of the Models' logical integrity in accordance with scope of work items 1 and 2 above shall include an assessment of Model Links.

Similar input data may be separately input into the CF Model, CA Model and RAV Model. We will record in our interim findings those observations which otherwise come to our attention in the course of our review in respect of such potential input data inconsistencies. However, we will not perform testing to verify the consistency of input data entered into these separate models.

Limitations to the scope of our work

You do not require us to perform any of the following:

1. verify any of the assumptions, judgements and commercial risks associated with the Project, nor comment upon the possibility of the financial projections being achieved;
2. review any other input configurations other than the base case and the Designated Sensitivities;
3. review comments included in cell notes embedded in the Models, to ensure that they are consistent with the Models;
4. consider the consistency of the Models with any other externally linked files;
5. review any of the macros contained in the Models.

Except as otherwise agreed in this letter, all limitations, terms and conditions in the Original Engagement Agreement relating to the Model (as defined in the Original Engagement Agreement) shall also apply to the Models.

Publication of Final Report

The interim findings, reports and correspondence that we prepare will be subject to the terms and conditions set out in the Original Engagement Agreement, except as otherwise agreed in this letter.

You have requested us to provide our consent for you to publish on your website the final report (the '**Final Report**') that we issue in respect of this additional scope of work set out in this letter. We agree that you may publish the Final Report on your website, subject to the following conditions:

- You will publish the whole Final Report without amendment or redaction by you as a portable document format file in the form that we provide to you;
- the Final Report will be removed from your website after 5 years; and
- you will remove the Final Report from your website, at our request, in the event that you are, or are reasonably expected to become, in material breach of your obligations under this letter or the Original Engagement Agreement.

Fees

[•]

Our fee estimate assumes the following:

1. Model versions

- The Models are provided to us in their final or near final form.
- The number of differences between the updated CF Model and the version we reported on in 1 November 2011 is no more than 100 unique formulae.
- The CA Model and RAV Model versions we are required to review contain no more than 3,000 and 6,000 unique formulae respectively. We note that the draft CA Model (CA_for_Statement_4.xlsm, 12,237 KB dated 22/12/2011) and the draft RAV Model (RAV22.xlsx, 913KB dated 22/12/2011) contain almost 2,700 and 5,900 unique formulae respectively.
- We are required to perform one detailed review of the Model shortly followed by up to two update reviews should any changes be made subsequent to our initial review. You do not expect that the extent of such changes to the Model's base case will be significant.

Should we be required to review additional updated versions of the Models, we will charge additional fees for each additional version of each model, at the lower of our time costs incurred (using an average hourly rate of [•]), and [•].

2. Sensitivity cases

- The Designated Sensitivities do not require any material change to the logic of the base case Models.
- We will only be required to operate and assess the Designated Sensitivities in respect of one version of the base case Models.

3. Source data

- Ofcom to provide extracts of the source data and identify where those should be input in the Models.
- Ofcom to identify common data sources within the Models to assist us in our checking for consistency.
- We are required to check the source data in respect of no more than two versions of the Models. Should we be required to perform additional checks of the source data, we will charge additional fees for each additional check, at the lower of our time costs incurred (using an average hourly rate of [•]), and [•].

4. Other

- We are not required to participate in any meetings in connection with this assignment.
- Our involvement in the Project is completed by 29 February 2012.

We should be grateful if you would confirm your agreement to the terms of this letter by counter signing the enclosed copy and returning it to us. If there is anything with which you do not agree or wish to amend, please do not hesitate to contact us and we shall be pleased to discuss the matter with you.

Yours faithfully

[•]

Partner
Ernst & Young LLP

AGREED BY The Office of Communications (Ofcom):

By (Authorised Representative):

Appendix B Original Engagement Agreement

Private and confidential

[•]
Director of Competition Finance
The Office of Communications (Ofcom)
Riverside House
2a Southwark Bridge Road
London
SE1 9HA

3 November 2010

Dear [•]

Review of financial model

Thank you for choosing Ernst & Young LLP (“we” or “**EY**”) to perform certain professional services (the “Services”) for the Office of Communications (“you” or “**Client**”) relating to the review of a financial model.

This cover letter, together with all of its appendices, exhibits, schedules and other attachments (collectively, this “**Agreement**”), describes and documents the arrangements between us, including our respective obligations. The scope of the Services is set out in the Statement of Work in Appendix A, together with details of our fees and billing arrangements. Any additional terms and conditions specific to the Services are set out in Appendix B, including restrictions on the disclosure and use of our advice and reports.

Please sign and return a copy of this Agreement to confirm your acceptance of these terms. If you have any questions about these arrangements, please contact [•] at [•] or [•] at [•].

We appreciate the opportunity to assist you and look forward to working with you.

Yours sincerely

[•]

Partner
Ernst & Young LLP

AGREED BY The Office of Communications (Ofcom):

By (Authorised Representative):

[•]

Encl:
Appendix A – Statement of work
Appendix B – General Terms and Conditions

Appendix (A)

Statement of work

Introduction

A financial model (the “**Model**”) has been developed by you as a regulatory model to assist in the determination of costs incurred by Openreach / BT (the “**Regulated Entity**”) in setting up and running the copper network for the local telecommunications access (the “**Project**”). This model is commonly known as the ‘Cost Forecasting model’ or ‘CF model’.

The main purpose of the CF model is to consolidate and summarise a set of costs, volumes and other parameters on the basis of the Regulated entity and your chosen assumptions and input data. Those figures are then prepared and formatted for the purpose of being used in the ‘Cost Allocation’ model (also known as ‘CA model’ or ‘Oak model’).

The objective of the Model, for the purposes of our review, is to generate the following key outputs: projected costs summarisation, projected Profit and Loss accounts of the Regulated entity, and all the outputs with costs, volumes and other parameters to be transferred to the ‘CA model’. Those are presented on an annual basis for six periods starting on 2009/10.

You require us to perform certain test procedures in relation to the Model, as set out in “scope of work” section below.

Scope of work

You have asked us to undertake a review of the Model to assist you in determining whether the Model has been constructed appropriately, in so far as its logical integrity and arithmetic is concerned, so as to materially achieve the objective described above under the base case assumptions;

Model versions

Our review will be conducted on the basis that the Model is provided to us in its final or near final form and the model versions we are required to review contain no more than 1,300 formulae. We note that the draft ‘Cost Forecast Modelv16.xlsm’ contains almost 1,250 formulae.

We are required to perform one detailed review of the Model shortly followed by up to two update reviews should any changes be made subsequent to our initial review. You do not expect that the extent of such changes to the Model’s base case will be significant.

Should we be required to review additional updated versions of the Model, we will charge additional fees, at the lower of our time costs incurred (using an average hourly rate of [•]), and [•].

We will as soon as possible communicate to you any material issues or changes to the scope of our work that come to our attention and will not perform any additional work without first obtaining your consent.

Limitations to the scope of our work

You do not require us to perform any of the following:

1. verify any of the assumptions, judgements and commercial risks associated with the Project, nor comment upon the possibility of the financial projections being achieved;
2. review any other input configurations other than the base case;
3. consider the consistency of the Model with externally linked files (if any);

Our review of the Model will be undertaken in isolation of any other services provided to you in respect of the Project. We will not be responsible for ensuring that the information and explanations which may come to our attention in providing such other services are appropriately reflected in the Model or reflected in our interpretation of the Model. Where you require us to assess whether specific matters are reflected in the Model, such matters should be recorded in a data book of assumptions or similar documentation, prepared to support the Model.

Responsibilities

We are responsible for planning and performing a review of the Model, in the context of your requirements, and reporting to you on that basis in respect of those particular points set out in our scope of work.

The Client retains full responsibility for the preparation and contents of the Model and for the projections contained in it.

Model base case

The Model's base case shall be the input configuration of the model in the form in which it is provided to us, subject to the operation of macros or other automated adjustments required for the Model's operation.

In some cases, a model may automatically process a number of alternative input cases; for example, by the use of Microsoft Excel data tables. Such alternative input cases do not form part of the base case and we are not required to assess the operation of the model under such alternative input cases, except as otherwise agreed in our scope of work.

Software defects and known model defects

We will review the contents of the Model in the file format in which it is provided to us. However, we will not carry out any enquiry into, or review of, the software within which the Model operates (such as, for example, Microsoft Excel). Accordingly, we shall have no responsibility for the consequences of any inherent defect in such computer software programmes.

You will inform us on a timely basis of all significant Model defects (in respect of the Model's logical integrity or otherwise) which you are aware of when we commence our work, or which you subsequently become aware of during the course of our review.

Circular logic

Circular logic is present in a spreadsheet when the inputs to a calculation depend directly or indirectly on the results of that calculation. Circular logic can occur, for example, because a model includes a circular reference in its coding or through the use of iterative techniques, such as 'copy-and-paste' macros or goalseek.

When a model employs circular logic, it is possible that more than one solution may exist to the mathematical problem represented by the model. We are not required to perform a mathematical analysis to assess whether multiple solutions may exist in the case that the Model relies on circular logic and, accordingly, we accept no responsibility for the possible existence of multiple solutions in such circumstances. Where we identify that a model contains circular logic under the base case or Designated Sensitivities input configurations, we will record this in our reports for your information.

We are not responsible for investigating whether circular references may present themselves in any input configurations which are not the subject of our review.

Use of the term 'audit'

The review of a financial model differs significantly to the statutory audit of financial statements; for example, the extent to which corroboratory evidence is sought and the applicability of auditing standards and company law. Where our review is referred to as an 'audit', we accept no additional responsibilities which may be implied by a comparison to the statutory audit of financial statements.

Reporting

Reporting – interim findings

During the course of our review we will provide you with interim findings, setting out certain comments and findings which come to our attention, and will provide you with an opportunity to respond to our interim findings and to make amendments to the Model in the light of these matters prior to the issue of our Reports (as defined below).

Our interim findings should not be used for any other purpose or provided to any other party without our prior written consent. Our interim findings are not intended to provide any overall assurance in relation to the Model's logical integrity, even if all potential errors identified in the interim findings were to be corrected.

In performing our review, we may identify and report matters as interim findings that may be of interest to you, but which would otherwise fall outside the agreed scope of our work. By reporting such matters to you, we do not intend to extend the agreed scope of our work and we accept no responsibility for conducting additional testing to ensure that all similar matters are brought to your attention.

We are not required to attach our interim findings to our Reports or otherwise ensure that copies of our interim findings are provided to all addressees of our Reports. Accordingly, addressees of our Reports accept that our Reports may be based on explanations that we have received during the course of our review, regarding certain assumptions and aspects of the intended operation of the Model, which are not recorded in Reports provided to them.

You agree that, where the Model has been developed by parties who are not parties to this engagement letter, we may provide copies of our interim findings to such parties and discuss related matters with them and that such disclosure will not be deemed in breach of any confidentiality agreements between ourselves.

Reporting – final reports

We will prepare one or more reports (the “**Reports**”) to communicate our findings and conclusions in relation to the above scope of work.

The Reports will be addressed to the addressees of this engagement agreement (the “**Addressees**”).

The Reports will be prepared on your specific instructions solely for the purpose of the Project and should not be used or relied upon for any other purpose. The Reports should not be quoted, referred to or shown to any other parties, except that our report may be shown (in each case solely for the purpose of the Project) to:

1. the Addressees’ employees and professional advisers;
2. the Addressees’ affiliates and their employees and professional advisers provided that each affiliate and adviser is informed and agrees before being provided with a copy of the Reports or any part of them that (a) we assume no responsibility or liability whatsoever to them in respect of the contents and (b) they will not show any part of the Reports to any other party without our prior written consent;
3. those persons who are covered by a signed duty of care letter which we have agreed with them;
4. those persons covered by a signed release letter, agreed with us, agreeing that (a) we assume no responsibility or liability whatsoever to them in respect of the contents and (b) they will not show any part of the Reports to any other party without our prior written consent;
5. as required by court order or a regulatory authority;
6. as otherwise permitted with our prior written consent.

We will consider requests that we consent to our Reports being shared with other parties. Where such consent is provided, save as expressly authorised elsewhere in this agreement, we will require each party to agree in writing to certain conditions, including releasing us from all responsibility to them in respect of the access given, before they may be given access to any part of our Reports.

Informal oral comments made in discussions with you or presentations to you, if any, about any Report will not have any greater significance than explanations or other material contained in the Report and reliance should only be placed on information and comments set out in the written Report.

During the course of the engagement we may provide status reports or show drafts of our Reports to you. This is done on the basis that they are provided to inform you of progress and significant findings identified to date, and draft Reports are subject to revision and alteration as further work is performed or further information received.

Fees

Based upon your requirements, a brief review of a draft version of the Model, and the assumptions set out below, our fees for the above scope of work will be [●]. These fees exclude VAT and any reasonable out of pocket expenses that we may incur.

Our fee notes will be addressed to the Company for the attention of [●].

Appendix (B)

General terms and conditions

Our relationship with you

1. We will perform the Services using reasonable skill and care.
2. We are a member of the global network of Ernst & Young firms (**EY Firms**), each of which is a separate legal entity.
3. We will provide the Services to you as an independent contractor and not as your employee, agent, partner or joint venturer. Neither you nor we have any right, power or authority to bind the other.
4. We may subcontract portions of the Services to other EY Firms, who may deal with you directly. Nevertheless, we alone will be responsible to you for the Reports (as defined in Section 11), the performance of the Services, and our other obligations under this Agreement.
5. We will not assume any management responsibilities in connection with the Services.

Your responsibilities

6. You shall assign a qualified person to oversee the Services and take responsibility for management decisions in connection with them.
7. You shall provide (or cause others to provide) to us, promptly, the information, resources and assistance (including access to records, systems, premises and people) that we reasonably require to perform the Services.
8. To the best of your knowledge, all information provided by you or on your behalf (**Client Information**) will be accurate and complete in all material respects. The provision of Client Information to us will not infringe any copyright or other third-party rights.
9. We will rely on Client Information made available to us and, unless we expressly agree otherwise, will have no responsibility to evaluate or verify it. We shall not be treated as having notice of information which may have been provided to EY Firms or EY Persons (as defined in Section 21) who are not involved in this engagement.
10. You shall be responsible for your personnel's compliance with your obligations under this Agreement.

Our reports

11. Any information, advice, recommendations or other content of any reports, presentations or other communications we provide under this Agreement (**Reports**), other than Client Information, are for your internal use only (consistent with the purpose of the particular Services).
12. You may not disclose a Report (or any portion or summary of a Report), or refer to us or to any other EY Firm in connection with the Services, except:
 - (a) to your lawyers (subject to these disclosure restrictions), who may use it only to give you advice relating to the Services,
 - (b) to the extent, and for the purposes, required by law (including subpoena or similar legal process)

or any professional or regulatory obligation (of which you will promptly notify us),

(c) to other persons (including your affiliates) with our prior written consent, on terms to be stipulated by us, who may use it only as we have specified in our consent, or

(d) to the extent it contains Tax Advice, as set forth in Section 13.

If you are permitted to disclose a Report (or a portion thereof), you shall not alter, edit or modify it from the form we provide.

13. You may disclose to anyone a Report (or any portion or summary thereof) solely to the extent that it relates to tax matters, including tax advice, tax opinions, tax returns, or the tax treatment or tax structure of any transaction to which the Services relate (**Tax Advice**). With the exception of tax authorities, you shall inform those to whom you disclose Tax Advice that they may not rely on it for any purpose without our prior written consent.
14. You may incorporate into your internal documents any summaries, calculations or tables based on Client Information contained in a Report, but not our recommendations, conclusions or findings. If you then disclose such internal documents to anyone, you shall assume sole responsibility for their contents and you shall not refer to us or any other EY Firm in connection with them.
15. You may not rely on any draft Report. We shall not be required to update any final Report for circumstances of which we become aware, or events occurring, after its delivery.

Limitations

16. You (and any others for whom Services are provided) may not recover from us, in contract or tort, under statute or otherwise, any amount with respect to loss of profit, loss of data or damage to goodwill, or any consequential, incidental, indirect, or special loss in connection with claims arising out of this Agreement or otherwise relating to the Services, whether or not the likelihood of such loss or damage was contemplated.
17. Our liability to you in respect of breach of contract or breach of duty or fault or negligence or otherwise whatsoever arising out of or in connection with this Agreement and the Services shall be limited in total to £[●] million (or, if greater, the total amount of the fees charged by us to you under this Agreement) to cover claims of any sort whatsoever (excluding interest and costs) arising out of or in connection with this Agreement and the Services.

Where there is more than one party to this Agreement (other than us), the limit of liability will have to be allocated among you. It is agreed that, save where an allocation is expressly agreed between you and stated in the Statement of Work, the limit of liability will be allocated such that you will each have an equal share of it. You shall not dispute the validity, enforceability or operation of the limit of liability on the ground that no allocation was expressly stated in the Statement of Work.

18. If we are liable to you (or to any others for whom Services are provided) under this Agreement or otherwise in connection with the Services, for loss

or damage to which any other persons have also contributed, our liability to you shall be several, and not joint, with such others, and shall be limited to our fair share of that total loss or damage, based on our contribution to the loss and damage relative to the others' contributions. No exclusion or limitation on the liability of other responsible persons imposed or agreed at any time shall affect any assessment of our proportionate liability hereunder, nor shall settlement of or difficulty enforcing any claim, or the death, dissolution or insolvency of any such other responsible persons or their ceasing to be liable for the loss or damage or any portion thereof, affect any such assessment.

19. You shall make any claim relating to the Services or otherwise under this Agreement no later than 3 years after the act or omission alleged to have given rise to the claim.
20. The limitations in Sections 16 to 19 will not apply to any liability (including vicarious liability) for death or personal injury or arising as a result of fraud on our part nor to any liability which cannot lawfully be excluded or limited.
21. You may not make a claim or bring proceedings relating to the Services or otherwise under this Agreement against any other EY Firm or our or its subcontractors, members, shareholders, directors, officers, partners, principals or employees (**EY Persons**). You shall make any claim or bring proceedings only against us.

Indemnity

22. We disclaim all responsibility for any consequence whatsoever should any third party rely on any Report unless Ernst & Young has given its prior written consent. To the fullest extent permitted by applicable law and professional regulations, you shall indemnify us, the other EY Firms and the EY Persons against all claims by third parties (including your affiliates) and resulting liabilities, losses, damages, costs and expenses (including reasonable external and internal legal costs) arising out of the disclosure of any Report (other than Tax Advice), or a third party's use of or reliance on any Report (including Tax Advice). You shall have no obligation hereunder to the extent that we have specifically authorized, in writing, the third party's reliance on the Report. The limitations in sections 16 to 22 are intended to benefit the other EY Firms and all EY Persons, who shall be entitled to enforce them. Otherwise a person who is not a party to this Agreement may not enforce any of its terms under the Contracts (Rights of Third Parties) Act 1999.

Intellectual property rights

23. We may use data, software, designs, utilities, tools, models, systems and other methodologies and know-how (**Materials**) that we own or license in performing the Services. Notwithstanding the delivery of any Reports, we retain all intellectual property rights in the Materials (including any improvements or knowledge developed while performing the Services), and in any working papers compiled in connection with the Services (but not Client Information reflected in them).
24. Upon payment for the Services, you may use any Materials included in the Reports, as well as the Reports themselves as permitted by this Agreement.

Confidentiality

25. Except as otherwise permitted by this Agreement, neither of us may disclose to third parties the contents of this Agreement or any information (other than Tax Advice) provided by or on behalf of the other that ought reasonably to be treated as confidential and/or proprietary. Either of us may, however, disclose such information to the extent that it:

(a) is or becomes public other than through a breach of this Agreement,

(b) is subsequently received by the recipient from a third party who, to the recipient's knowledge, owes no obligation of confidentiality to the disclosing party with respect to that information,

(c) was known to the recipient at the time of disclosure or is thereafter created independently,

(d) is disclosed as necessary to enforce the recipient's rights under this Agreement, or

(e) must be disclosed under applicable law, legal process or professional regulations. You agree that if you receive any request under the Freedom of Information Act 2000 (where you are subject to it) for disclosure of information provided by us, you will promptly notify us of such request prior to any disclosure.

If circumstances arise such that we disclose information to the Serious Organised Crime Agency (**SOCA**), due to the restrictions imposed by law we may be prevented from discussing such matters with you or from proceeding with the Services pending consent from SOCA. If this arises we shall have no liability to you as a result of any suspension or termination of the Services.

26. Either of us may use electronic media to correspond or transmit information and such use will not in itself constitute a breach of any confidentiality obligations under this Agreement. We cannot guarantee the security and integrity of any electronic communications or information sent or received in relation to this Agreement.
27. Unless prohibited by applicable law, we may disclose Client Information to other EY Firms and EY Persons to facilitate performance of the Services, to comply with regulatory requirements, to check conflicts, or for quality, risk management or financial accounting purposes.
28. With respect to any Services, and only to the extent that U.S. Securities and Exchange Commission auditor independence regulations apply to the relationship between you or any of your associated entities and any EY Firm, you represent, to the best of your knowledge, as of the date of this Agreement, that neither you nor any of your affiliates has agreed, either orally or in writing, with any other advisor to restrict your ability to disclose to anyone the tax treatment or tax structure of any transaction to which the Services relate. An agreement of this kind could impair an EY Firm's independence as to your audit or that of any of your affiliates, or require specific tax disclosures as to those restrictions. Accordingly, you agree that the impact of any such agreement is your responsibility.

Data protection

29. We may collect, use, transfer, store or otherwise process (collectively, **Process**) Client Information that can be linked to specific individuals (**Personal Data**). We may Process Personal Data in various

jurisdictions in which we and the other EY Firms operate (which are listed at www.ey.com). We will Process the Personal Data in accordance with applicable law and professional regulations including (without limitation) the Data Protection Act 1998. We will require any service provider that Processes Personal Data on our behalf to adhere to such requirements.

30. You warrant that you have the authority to provide the Personal Data to us in connection with the performance of the Services and that the Personal Data provided to us has been Processed in accordance with applicable law.

Fees and expenses generally

31. You shall pay our professional fees and specific expenses in connection with the Services as detailed in the Cover Letter. You shall also reimburse us for other reasonable expenses incurred in performing the Services. Our fees are exclusive of taxes or similar charges, as well as customs, duties or tariffs imposed in respect of the Services, all of which you shall pay (other than taxes imposed on our income generally).
32. We may charge additional professional fees if events beyond our control (including your acts or omissions) affect our ability to perform the Services as originally planned or if you ask us to perform additional tasks.
33. If we are required by applicable law, legal process or government action to produce information or personnel as witnesses with respect to the Services or this Agreement, you shall reimburse us for any professional time and expenses (including reasonable external and internal legal costs) incurred to respond to the request, unless we are a party to the proceeding or the subject of the investigation.

Force majeure

34. Neither you nor we shall be liable for breach of this Agreement (other than payment obligations) caused by circumstances beyond your or our reasonable control.

Term and termination

35. This Agreement applies to all Services performed at any time (including before the date of this Agreement).
36. This Agreement shall terminate on the completion of the Services. Either of us may terminate it, or any particular Services, earlier upon immediate written notice to the other.
37. You shall pay us for all work-in-progress, Services already performed, and expenses incurred by us up to and including the effective date of the termination of this Agreement. Payment is due within 30 days following receipt of our invoice for these amounts.
38. Our respective confidentiality obligations under this Agreement shall continue for a period of three years following the termination of this Agreement. The other provisions of this Agreement that give either of us rights or obligations beyond its termination shall continue indefinitely following the termination of this Agreement.

Governing law and dispute resolution

39. This Agreement, and any non-contractual obligations arising out of this Agreement or the Services, shall be governed by, and construed in accordance with, the laws of England and Wales.
40. If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact [●], our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

Any dispute relating to this Agreement or the Services shall be subject to the exclusive jurisdiction of the English courts, to which each of us agrees to submit for these purposes.

Miscellaneous

41. This Agreement constitutes the entire agreement between us as to the Services and the other matters it covers, and supersedes all prior agreements, understandings and representations with respect thereto, including any confidentiality agreements previously delivered.
42. Both of us may execute this Agreement (and modifications to it) by electronic means and each of us may sign a different copy of the same document. Both of us must agree in writing to modify this Agreement.
43. You represent that the person signing this Agreement on your behalf is expressly authorized to execute it and to bind you and any of your affiliates or others for whom Services are performed to its terms.
44. You agree that we and the other EY Firms may, subject to professional obligations, act for other clients, including your competitors.
45. Neither of us may assign any of our rights, obligations or claims under this Agreement.
46. If any provision of this Agreement (in whole or part) is held to be illegal, invalid or otherwise unenforceable, the other provisions shall remain in full force and effect.
47. If there is any inconsistency between provisions in different parts of this Agreement, those parts shall have precedence as follows (unless expressly agreed otherwise): (a) the Cover Letter, (b) the Statement of Work and any annexes thereto, (c) these General Terms and Conditions, and (d) other annexes to this Agreement.
48. We may use your name publicly to identify you as a client, but we may refer to you in connection with the Services only if it is a matter of public knowledge that we are providing them (or have provided them)

Appendix C Matters arising from our review

Cost Forecasting Model (the 'CF Model')

Thousand Man Hours ('KMH') inputs

The KMH inputs on the 'CA KMH' sheet do not agree to the KMH per activity on the '3. Vol to KMH Calc' sheet. We also note that the check on the 'CA KMH' sheet shows a difference. The differences range from -5% to +6%. We understand from Ofcom that the differences arise due to the use of estimated static activity allocation percentages. Over the price control period Ofcom consider these differences to be immaterial and unbiased

Regulatory Asset Value Model (the 'RAV Model')

Other Holding Gains

The current cost accounts (CCA) calculations of pre-97/98 assets include various "other HG" input adjustments to both asset cost and depreciation in both historic and future periods. These adjustments are not made in the HCA or RAV calculations and it is not explained in the RAV Model what they represent. For Copper assets, BT have provided a rationalisation of the 2010/11 adjustment as relating to various items including a shift in standard engineering times "from synthetics to work activity units". Ofcom are satisfied that the explanation provided by BT supports the "other HG" included within the Copper CCA calculation and that it has been treated appropriately. For the Duct assets, Ofcom have confirmed that the "other HG" included within the Duct CCA calculation are not relevant to their RAV calculations.

The historic cost accounting (HCA) figures for pre-97/98 Copper assets appear to be under depreciated by £32 million in 2016/17. This amount is used to derive the RAV figures. Ofcom have stated that the existence of this closing balance will not have a material impact on its modelling.

There is a small inconsistency between the RAV and CCA calculations of price indexation / holding gain in the output sheets and the underlying RAV / CCA sheets which is largest in 2010/11 when the CCA gain is £41 million less than RAV gain. Ofcom have explained the RAV methodology is consistent with the use of the model in the previous Charge Control and they are satisfied that the RAV number is correct.

Cost Allocation Model (the 'CA Model')

2009/10 Balance Sheet

The 2009/10 balance sheets on the 'Summary & FA_Product' show an opening balance error. Ofcom have informed us that they believe discrepancies are contained within the 2008/09 closing balance. Ofcom consider these discrepancies will not impact the modelling as BT have reconciled both the 2009/10 profit and loss and the 2009/10 balance sheet figures to the 2010 Regulatory Financial Statements.

Selected Data

Ofcom have prepared the CF Model and CA Model using input data from a number of sources. Ofcom identified certain elements of this data (the '**Selected Data**') in the file *Sources of evidence.xls* (dated 27 January 2012, size 19,439 bytes) and provided comments of how the Selected Data should be entered into the Models.

We tested the consistency of the Selected Data with the CF and CA Models and sought clarifications from Ofcom where data were inconsistent. Ofcom provided explanations for the differences between the Selected Data and the Models. We understand that the differences represent intentional adjustments made by Ofcom to the CF and CA Models' input data. Verification of such intentional adjustments is outside the scope of our work.