

PRS Bad Debt Surcharge (Section 6)

Question 9: Do you agree with our assessment of the potential options regarding the structure of the recovery for bad debt on PRS calls?

Although in principle it is correct to charge the bad debt separately for PRS calls, we strongly question this as a reasonable practice. In reality and in practice PRS bad debt is part of BT's general overhead and is treated as such by BT.

- The lack of detail available from BT's systems is astonishing. It leads to the obvious conclusion that it is not of interest for BT to manage and report this debt separately. A process for BT to target and specifically improve the level of PRS bad debt is clearly not forthcoming. We do not accept that BT's general debt management process will necessarily lead to a reduction in PRS bad debt without this targeted focus.
- We believe bad debts on PRS calls need to be identified with a re-assuring level of precision by customer, service and price point with specific preventative and recovery measures targeted at this call type and regular management reporting.
- Notwithstanding the BDO report, the lack of transparency in BT's calculations for PRS bad debt does not help re-assure that the very basic and significant initial accounting errors have been fully corrected. Given their extent it also suggests that their management review processes are inefficient and of questionable practice.
- As the bad debt recovery mechanism is generic for all BT customers we have reservations as to whether the same method of debt management for PRS customers is either appropriate or efficient. For example a more specifically targeted process may have lower costs if not having to support the large inappropriate systems involved with BT's higher volume processes.
- The comparatively low volume of PRS calls suggests that this area of the business does not have the focus of other areas with a more standardised bad debt profile. Whilst BT may believe this is more efficient, it also means that it incurs a proportion of the overheads associated with high volume traffic, which may not be the most cost effective.
- It is not clear whether the level of bad debt is closely linked to revenue per call or per customer. Clearly high spending customers are not all making PRS calls. We agree with C&W that bad debts by service, or at the very least by price point, should be more precisely determined and accurately reported. Installing new systems (Avalon) which reduce visibility merely confirms BT's lack of focus on PRS debt. The accounting apportionment of such charges is insufficient to determine the charge to the industry and statistical analyses to explain these charges is similarly unconvincing. For the fees the industry is charged, what is required is a separate PRS bad debt management focus supported by simple, accurate and definitive reporting.

Question 10: Do you agree that BT's attribution methodology for bad debt is an appropriate starting point to use in assessing the incidence of bad debt on PRS calls?

Whilst the attribution methodology may provide a "robust foundation" for estimating the incidence of PRS bad debt, we do not believe the mechanism is fit for the purpose of appropriately charging the cost where it can be efficiently controlled.

- The deficiencies in BT's accounting information and systems bring into question the use of BT's own information regarding the calculation of bad debt. We believe improved reporting and industry comparisons (perhaps from a formal request to other Network Operators selling PRS and high value services to consumers) are essential. In addition a separate management focus would help demonstrate 'value for money'. There is little rational in separating out the PRS element if it cannot lead to improved PRS bad debt management. If the cost behaves as a general BT overhead it should be charged as such. In the environmental principle of 'the polluter must pay' the polluter must also be in charge of its emissions.
- We strongly believe that transparency of reporting is required so that BT's level of efficiency in managing PRS bad debt can be assessed. Given this specific charge to the industry, a separate annual report of the process would seem reasonable and good practice. It is standard industry practice for fees for any service to be accompanied by either a specific deliverable or a report of performance. This is separate from the post event non-compliance audit that BDO conducted. The failure to do this should result in a reduction in the claim, at least retrospectively.
- We agree that there should be a cap for a minimum period and as per Q9 that future reports from BT should be dramatically improved, but we believe these should include detailed bad debt recovery performance and explanations of any market changes impacting such. Nowhere is there any explanation from BT of the reasons for the dramatic bad debt increase, further evidence of a lack of efficient management focus by BT. In a declining market, these dramatic increases in cost seem counter intuitive. The Virgin Media comment to the contrary is ad hoc and at best inconclusive. It would be helpful to identify sources.
- The initial error of 9.7% instead of 5.5% is further evidence of the cursory attention given to PRS bad debt by BT. This again points to a separation of PRS debts by BT as being an academic accounting exercise and not a relevant mechanism for their genuine recovery.

Question 11: Do you agree with our view that no adjustment should be made to the PRS Bad Debt Surcharge for inefficiency? If not, please provide analysis and evidence to support your arguments

- Whilst the method of calculation has not changed, the increase from 3% to 5.2% is clearly significant. The lack of transparent and meaningful reporting by BT means it is impossible to determine whether this is due to a genuine deterioration in consumer behaviour, or a reduced efficient focus by BT on its PRS consumer debt recovery.
- Although BT's overall debt procedures are deemed good practice by BDO, clearly from its significant bad debt level, the PRS market requires exceptional attention. If this hasn't occurred (eg if BT have reduced their PRS bad debt recovery activities, perhaps secure in the knowledge that these debts would be recovered in additional fees to the industry) then clearly an efficiency charge to BT would be appropriate. Without any reporting requirements placed upon BT's PRS bad debt recovery it is not possible to substantiate this one way or another.
- The reduction in information from the implementation of BT's new Avalon system does suggest poor attention to the details of PRS bad debt. Indeed, looking at it another way, the fact that the debts have increased without a reported understanding and explanation certainly does not indicate good efficient management by BT. It's a general industry norm that management gets what it inspects.

- Although BT have stated that separate management would introduce additional costs, we believe that proper reporting and an additional focus is good management practice and standard in a service industry not otherwise rewarded by results.

Question 12: Do you agree that in the current circumstances it is appropriate for the PRS Bad Debt Surcharge charge control to have effect on the first of the month following our final statement? If not, please supply reasons why this would be the case.

It is appropriate for any accepted increase in charges to be effective from the date Ofcom rule is reasonable. It is not appropriate for BT to be able to back-date this charge to the beginning of July 2010. The main reason for this are:

- The initial accounting errors introduced into the process which have caused the delay
- The additional time spent by the industry and regulators in responding to information requirements as a result
- The lack of a proper report and explanation by BT of the increase, which partly necessitated an independent review by BDO
- The lack of a specific focus by BT on PRS bad debt and the expectation by them that the industry would bear the cost of such increase regardless
- The questionable management attention to PRS bad debt in the intervening period.