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**IN THE COMPETITION**  
**APPEAL TRIBUNAL**

Case Nos. 1205-1207/3/3/13

Victoria House,  
Bloomsbury Place,  
London WC1A 2EB

8<sup>th</sup> November 2013

Before:  
**THE HON. MR. JUSTICE ROTH**  
(The President)  
**STEPHEN HARRISON**  
**PROFESSOR COLIN MAYER**  
(Sitting as a Tribunal in England and Wales)

BETWEEN:

**BRITISH TELECOMMUNICATIONS PLC** Appellant

- and -

**OFFICE OF COMMUNICATIONS** Respondent

AND BETWEEN:

**(1) CABLE & WIRELESS WORLDWIDE PLC**  
**(2) VIRGIN MEDIA LIMITED**  
**(3) VERIZON UK LIMITED** Appellants

- and -

**OFFICE OF COMMUNICATIONS** Respondent

AND BETWEEN:

**(1) BRITISH SKY BROADCASTING LIMITED**  
**(2) TALKTALK TELECOMMUNICATIONS GROUP PLC** Appellants

- and -

**OFFICE OF COMMUNICATIONS** Respondent

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**H E A R I N G D A Y N I N E**

## A P P E A R A N C E S

Mr. Rhodri Thompson QC, Mr. Graham Read QC, Ms. Sarah Lee, Mr. Ben Lynch and Ms. Georgina Hirsch (instructed by BT Legal) appeared on behalf of the Appellant, British Telecommunications PLC.

Mr. Meredith Pickford and Mr. Julian Gregory (instructed by Herbert Smith Freehills LLP) appeared on behalf of the Appellants (1) British Sky Broadcasting Limited and (2) TalkTalk Telecommunications Group PLC.

Ms. Dinah Rose QC and Mr. Tristan Jones (instructed by Olswang LLP) appeared on behalf of the Appellants (1) Cable & Wireless Worldwide plc, (2) Virgin Media Limited and (3) Verizon UK Limited.

Mr. Pushpinder Saini QC, Ms. Kate Gallafent, Mr. Hanif Mussa and Ms. Emily Neill (instructed by the Legal Department, Office of Communications) appeared on behalf of the Respondent.

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1 THE PRESIDENT: Yes, Mr. Thompson.

2 Dr. GEORGE HOUPIS, Recalled

3 Cross-examined by Mr. THOMPSON

4 Q Good morning, Dr. Houpis. I have been placed under strict instruction to be as quick as  
5 possible, hopefully half an hour, so I think that means some teamwork between you and me,  
6 but we will do our best. We are now dealing with the issue of interest and I would say it  
7 comes down to two issues essentially: incentives and commercial certainties, do you agree  
8 about that? Those are the two issues that are live in this case? The incentives of BT and the  
9 CPs and the issue of commercial certainty and I am proposing to deal with those two issues?

10 A I think the answer to both of them is yes, but in terms of the incentives, because in my first  
11 report I considered the impact on BT, just to clarify that, given what the claim is in terms of  
12 interest, what has been requested if interest was to be payable, what is the objective of that?  
13 I think the primary concern is the incentives on BT, just to clarify.

14 Q You focused on BT and Dr. Maldoom, to some degree on the CPs. That is fair, is it not?

15 A I understand that Dr. Maldoom has also covered the CPs, I am just giving my view.

16 Q Before we look at that issue of incentives, we just need to close off the discussion we were  
17 having of dynamic efficiencies yesterday, and to look at three pieces of evidence which are  
18 relevant both to that issue and to the issue of the incentives of the CPs. You made the point  
19 to Mr. Saini that the CPs had, between 2004 and 2008, targeted the profitable and least  
20 costly business of high bandwidth customers in geographically limited areas, do you  
21 remember that?

22 A Not quite in those terms, if you maybe ask me the question the way it was asked then I can  
23 answer it.

24 Q You made a point about the business where the CPs had expanded and you said it was the  
25 high bandwidth areas in geographically limited areas, do you remember that?

26 A I was asked the question as to why do I think that entry occurred in that part of the market  
27 and I gave the answer as to why I think that happened.

28 Q You said it was profitable and geographically limited, did you not?

29 A To be precise what I said was that the revenues in those areas when potential entrants think  
30 about a market that they target, they will look at the revenues and it will compare those to  
31 the costs ----

32 Q Exactly.

33 A -- to enter, and one of those things for this area is revenues are higher and costs are lower,  
34 that's the point.

1 Q The same thing happens in the postal area, it is a classic cherry-picking exercise, there is  
2 nothing wrong with that, it is exactly how one would expect a market entrant to proceed, is  
3 it not?

4 A I think you are talking about cherry-picking now, I didn't say anything about cherry-picking.  
5 I have made the simple point which is that when somebody thinks about different markets to  
6 enter, it could be the way you are presenting it, it could be a different market, they will look  
7 at the revenues and the costs.

8 Q And then we discussed whether a stringent cost orientation or cost control regime might  
9 restrict entry or expansion on the wholesale market and the way I would put it, it would  
10 effectively act as regulatory barrier to entry on the wholesale market. Do you remember our  
11 discussion about that issue?

12 A I think in broad terms, yes.

13 Q We discussed it in general terms, but there are two specific pieces of evidence in relation to  
14 one of the companies that has instructed you, TTG, that I would like you to look at, and the  
15 first is in the bundle for the factual witnesses, which is core bundle C, tab 16, and see the  
16 statement of Mr. Morawetz?

17 A Mr. Morawetz doesn't work at TalkTalk.

18 THE PRESIDENT: No, all Mr. Thompson said is there are two pieces of evidence he we would  
19 like you to look at.

20 MR. THOMPSON: It is not evidence of TalkTalk, it is evidence about TalkTalk?

21 A All right, okay.

22 Q It is p.4 para. 15?

23 A Yes.

24 Q Where it says:  
25 "Virgin operates in a competitive market for the provision of Ethernet services to  
26 customers such as local authorities, business enterprises and telecoms carriers.  
27 Notable competitors are BT Wholesale, Cable & Wireless, Colt and TalkTalk  
28 (operating as TalkTalkBusiness)."  
29 So you would accept from that that TalkTalk is active on the wholesale market? That is  
30 correct, is it not? (After a pause) It is a simple question, it is simply that that is what Mr.  
31 Morawetz says.

32 A I accept that that is what Mr. Morawetz says. Whether TalkTalk is active on that market I  
33 don't have a way of knowing.

34 Q You do not know yourself?

1 A No.

2 Q The second is a piece of evidence which has arisen in quite a curious way, and one finds it  
3 in the authorities bundle 5, tab 68?

4 A I have 67.

5 Q 68 should have been added. I thought this had been sorted out.

6 THE PRESIDENT: I have it.

7 A Is this approved Judgment?

8 MR. THOMPSON: Yes, it in the Court of Appeal, and it is a very recent Judgment, delivered last  
9 week.

10 MS. ROSE: I do not think we have been provided with this.

11 MR. THOMPSON: It was circulated on Sunday by email and I thought hard copies were handed  
12 out on Wednesday.

13 MS. ROSE: No, no hard copies have been handed around.

14 MR. THOMPSON: It is a Judgment between TalkTalk and Ofcom.

15 MS. ROSE: A cache has been found in the possession of Ofcom! (Laughter)

16 MR. THOMPSON: One can look simply at para. 2 where one will see that TalkTalk is described  
17 as:

18 "a leading provider of retail fixed line rental, voice calling and broadband  
19 telecommunications in the United Kingdom. ... Retail broadband services are the  
20 services provided directly to members of the public. They are to be distinguished  
21 from wholesale broadband services, which are the means by which  
22 communications providers sell access to broadband to each other.  
23 The principal provider of wholesale broadband services in the WBA markets is  
24 BT. It is by virtue of BT's significant market power in large sections of the country  
25 that Ofcom has considered it necessary to impose price controls on it in those areas  
26 where it is strongest."

27 Then, the next sentence:

28 "The effect, however, of such price controls is to make it more difficult for  
29 TalkTalk to recoup the cost of competing with BT in such areas. Hence its interest  
30 in this appeal."

31 So that is the first passage. Then this is spelt out at para. 30:

32 "TalkTalk 's evidence, in the form of a witness statement from Mr Heaney,  
33 demonstrated that already as at 12 September 2011, only a few weeks after  
34 Ofcom's charge control determination, 153 further exchanges, including 92 market

1                   1 exchanges had gone 'live', and hundreds more were already in the pipeline for  
2                   going live that year."

3                   And then the sentence I had wanted you to see is:

4                   "However, the imposition of price controls in the very market in which TalkTalk  
5                   had committed to roll out its unbundling programme was said to put a potential  
6                   burden on the economics of TalkTalk 's programme with the danger of making  
7                   rollout in a number of exchanges unviable."

8                   So I just put it to you as relevant to the discussion we were having about the effect of price  
9                   controls on market entry and expansion on the upstream market, and you see that TalkTalk  
10                  itself has expressed such concerns.

11                A           As I explained yesterday, in 2004 Ofcom - to put this in the context of our discussion  
12                yesterday which I think is the point you are trying to make - Ofcom was facing a choice  
13                between the cost orientation and price control and I did say one of the reasons Ofcom did  
14                not choose the price control in 2004 was that if it got the price control wrong and therefore  
15                it set prices too low that would deter entry in the market. I think the discussion here to me  
16                seems consistent with that statement. What happens is Ofcom has a price control for WBA  
17                services. The way I understand competition works in this market is that TalkTalk and other  
18                players like TalkTalk buy a further upstream service, which is called "LLU", and then  
19                effectively by buying that service LLU they are competing in the WBA market, which is  
20                the downstream market, it is also the wholesale market, but it is downstream from LLU.  
21                My understanding of what Mr. Heaney is saying is if the prices for that market are set too  
22                low then the margin between the wholesale bitstream market, the WBA market, and the  
23                LLU market would be too low, in order to enable investment to happen from TalkTalk ----

24                Q           I think I am simply making the point ----

25                A           -- and I think that is consistent with what I said yesterday.

26                Q           I am simply making the point, it is really the same point that Mr. Morawetz made on behalf  
27                of Virgin, that a trade-off between high and low prices on the wholesale market, and high  
28                and low prices on the downstream market, because the higher they are in the wholesale  
29                market the easier it is to enter. That is the only point I am making?

30                A           I don't think it is the same point. I can explain if you want me to. My understanding of  
31                what Mr. Morawetz was saying is that there is some part of the market in which Virgin  
32                competes with BT and Mr. Morawetz was saying that if BT raises retail prices in that part of  
33                the market - wholesale prices - and therefore retail prices in that part of the market, then that  
34                provides more margin for Virgin to compete, and I think that was one side of his argument

1 as to why he said if they face higher wholesale prices that also means higher retail prices for  
2 some part of the market. As a result of that that is welcome to the extent that they do not pay  
3 the prices for the wholesale services because Virgin also competes with BT.

4 Q That is not what TalkTalk are saying here, is it? They are talking about how difficult it is to  
5 enter the wholesale market?

6 A If I finish and then you can ask me again. So, therefore, I think what Mr. Morawetz was  
7 saying is that is the one effect, so when wholesale prices are higher retail prices are higher,  
8 and they welcome that as Virgin, as a rival, but at the same time they also purchase products  
9 from BT and when those prices go up they don't welcome that. That has a negative effect,  
10 and I think in response to Professor Mayer's question, what he said is, I think, three years  
11 ago, because they were not purchasing so many products from BT, they would probably  
12 welcome an increase in the price, but more recently because they're purchasing more and  
13 more wholesale products, they would not welcome an increase in the wholesale price. If I  
14 may just add something to the earlier discussion, it is in my report, but it's based on Ofcom's  
15 analysis, there is some competition in the market, that has not been denied, but I think it's  
16 important to put those two things in context. BT was found in 2008 and 2009 to have 75 per  
17 cent market share in the lower bandwidth AISBO market. The second next competitor to it  
18 was Virgin, and they had 7 per cent market share. So I think we need to put the relative  
19 power of the companies into context.

20 Q The third piece of evidence is one that I put to Dr. Maldoom, and you may well remember  
21 it, and it relates to the incentives to the CPs on the downstream market, where you may  
22 recall that we looked at evidence that TTG had positively asserted in the context of this  
23 dispute that it had passed through overcharges to its retail customers - do you remember  
24 that? It does not sound like you do. Can we look at CBB 10.80, which is at p.147.

25 A Paragraph 10.80?

26 Q I think probably 10.82 is sufficient.

27 "[TalkTalk] claims that some of the higher WES/BES prices would have been  
28 passed on in higher retail prices (see paragraph 10.46 above), although it does not  
29 provide supporting evidence."

30 So TalkTalk made the point that it was passed on?

31 A Yes.

32 Q Can we now move on to the substance. There are two reports where you address the issue  
33 of interest, a very short report, your supplementary report, and then at somewhat more  
34 length in the fourth report - do you remember that?

1 A Yes.

2 Q In particular, in the fourth report, para.4.3, p.39, you say in the middle of the paragraph:

3 "Whilst the issue of the appropriate level of interest is not under consideration at

4 this stage, for the avoidance of doubt, the aim of requiring BT to pay interest when

5 found to have overcharged is to remove the benefit derived by BT from the

6 overcharge and leave it no better off than it would have been without the

7 overcharge."

8 That is what I think a lawyer would call a "restitutionary approach", taking away all the

9 benefit that BT had. Do you understand that?

10 A I understand that this term is used, yes.

11 Q Can you turn to ST1-1-5, and you should find the expert report of Mr. Francis - do you

12 remember that?

13 A Yes.

14 Q And in particular can you look at para.1.3. You will see in 1.3.1, Mr. Francis was instructed

15 by Herbert Smith to give his opinion on what were:

16 "... the appropriate measures to be used to calculate the interest owing on a

17 restitutionary claim in relation to any overpayment of charges to BT on the

18 following two distinct assumptions."

19 So you see the word "restitutionary" used, and then again at 2.1.1:

20 "The advantage of estimating damages on a restitutionary basis is that it aims to

21 remove the benefit derived by BT and leave it no better off than it would have been

22 without the overpayment."

23 Do you see that?

24 A Yes, I see that.

25 Q You will remember what happened is that this report was not put into the bundle, and you

26 were asked at short notice to prepare a supplementary report - that is correct, is it not?

27 A That's correct.

28 Q I just want to be clear: were you instructed on the same basis as Mr. Francis?

29 A I think my instructions are clear at the front of my supplementary report. In Houpis 4 if you

30 go to - sorry, not Houpis 4, it could be Houpis 2, the supplementary report. It is at 1.3.

31 Q You were presumably aware of Mr. Francis's report, he is a colleague of yours, is he not?

32 A He is a colleague of mine, yes.

33 Q Are you saying your instructions were varied from those of Mr. Francis for the purposes of

34 your report?



1 A I'm saying that Mr. Francis originally was instructed because the expectation was that the  
2 issue of the level of interest as well as whether interest would be payable would be  
3 considered, and my understanding is, in the case management conference that took place,  
4 the view was that those two issues would be separated, and therefore I was instructed, and I  
5 think that was at the request of the Tribunal. I was instructed to write a short report to  
6 address the issue of whether interest should be payable because that was the objective of the  
7 current proceedings. My understanding was that if the view was taken that there was no  
8 need to pay any interest, then there was obviously no reason to decide what the interest  
9 might be. So there was a narrower scope, which was just to address the question of whether  
10 interest should be payable. That was my understanding.

11 Q Can we now turn to para.4.6 of the same report.

12 THE PRESIDENT: Dr. Houpis's report?

13 MR. THOMPSON: Yes, Dr. Houpis's report.

14 THE PRESIDENT: Do you want us to keep out, Mr. Francis's report?

15 MR. THOMPSON: No, we do not need that. That was purely for the appropriate instructions. It  
16 is p.41:

17 "The key issue in terms of economic efficiency is whether the overall framework  
18 within which BT operates is effective in providing adequate incentives to BT to  
19 comply with its cost orientation obligation."

20 Do you see that?

21 A Yes.

22 Q For my part, I would agree with that. I would say that was well put, and is similar to the  
23 point that Dr. Maldoom was making about the "regulatory knob" turning it up or down, and  
24 you need to look at the overall situation. You emphasised the word "overall".

25 A I think this is a very specific question, and I am writing that in response to Dr. Maldoom's  
26 report, which responded to my supplementary report. Dr. Maldoom devoted quite a number  
27 of pages in order to address the issue of, I think it is, clause 4.3. My recollection is that  
28 there is a clause in those contracts which specifies that no interest would be payable, and  
29 Dr. Maldoom set out his views as to why, if Ofcom, was to actually decide that interest was  
30 payable, why that would obviously be inconsistent with that clause and what that would  
31 imply for contractual certainty and for the future, and it was that narrow point I was  
32 responding to. My point is that when one looks at - and it's not a legal point, I'm making an  
33 economic point, which is when one looks at the behaviour of a regulated company and you  
34 see that there has been non-compliance, and significant non-compliance with a particular

1 obligation, then it seems reasonable to me - if I may just finish. It seems reasonable to me  
2 to look at the different clauses which could have affected non-compliance. Then the point  
3 I'm making is if, in that process, the view is taken that there is some other clause, some  
4 other part of the framework, which could have contributed to this non-compliance, or,  
5 conversely, if this was changed it would decrease the likelihood of non-compliant behaviour  
6 in the future, then as long as this could be explained, so it wasn't an arbitrary removal of the  
7 clause, as long as a decision is taken by a regulatory authority or by the Tribunal which  
8 explains why this is happening, my point was I think that that should not have a material  
9 impact on regulatory certainty for the future. It's not an arbitrary removal of a clause, it is a  
10 removal of a clause which is explained within a specific context.

11 Q I think you are misunderstanding. I am not talking about the contract or commercial  
12 certainty, I am just looking at what you say there. You say that you need to look at the  
13 overall framework. That is what you say, and I agree, so can we move on?

14 A As I explained, this is my paragraph, the only paragraph in my report where I respond to a  
15 significant part of Dr. Maldoom's report where he addressed this issue. You can read the  
16 sentence as is ----

17 Q I do not want to interrupt you. I will come back to contractual certainty at the end, but I am  
18 working on a tight timetable, and we are now talking about incentives, and you have said  
19 you need to look at the overall framework, and I agree, so can we move on?

20 THE PRESIDENT: There is no need to question, in a sense, Dr. Houpis on that. That is his  
21 starting point, to look at the overall framework. Then he moves on later in the paragraph to  
22 see why he thinks it is appropriate here to make some adjustment. You are just establishing  
23 the point.

24 MR. THOMPSON: Yes. So it is not a matter of punishing BT or rewarding CPs or even  
25 compensating CPs - that is not what we are dealing with here, is it?

26 A I think that's correct.

27 Q They have not proved they suffered loss and they have made a point that harm to consumers  
28 resulted from pass-through, have they not?

29 A On the first part, I'm not familiar with whether there was any claim of loss or not. I'm not  
30 familiar with that. As for your second point, if I understood it correctly that CPs said that as  
31 a result of the behaviour of the BT the higher prices of wholesale services were passed on to  
32 some extent to retail consumers and that caused harm, my understanding is, as you said, that  
33 that was the case.

34 Q We are considering an administrative act by Ofcom intended to complement the existing

1 compliance incentives by imposing a financial burden on BT. That is what we were talking  
2 about?

3 A That seems to me like a legal question. I'm not sure what you mean by "administrative act".  
4 I'm not familiar with that.

5 Q In your report you naturally focus on the compliance incentives of BT, but you would  
6 accept, I think, that we have to look at the position in the round?

7 A As I explained - when you say I accept that we would have to look at the position in the  
8 round, my view is that the first question is you have to look at the - when you're considering  
9 interest, you have to look at the specific impact that you would expect the payment of  
10 interest to have or not have on BT, and that was the focus of my supplementary report.  
11 Then Dr. Maldoom made the point, because I hadn't covered this point about the contractual  
12 certainty, that if you were to award the interest then this could have an impact on  
13 contractual certainty and therefore this could have an impact for regulatory certainty in the  
14 future. In the response to that point, I have made the points that I have made in para.4.6,  
15 where I think I am making quite a narrow point which is that if you find that a company has  
16 - it's not a legal point - if you find that a company has not been compliant with an obligation  
17 and there has been a breach which has been consistent over a long period of time, then it  
18 seems to me reasonable for an authority to look at the different ways in which that  
19 behaviour may have occurred. One of them I think would be to look at the payment of  
20 interest. As long as it can be explained why, by Ofcom or the Tribunal, a decision was  
21 taken to award interest, then I don't think that would necessarily have a material impact on  
22 regulatory certainty. That's all the point I'm making, I'm not expressing a view as to the  
23 legal process, the contractual process, etc.

24 Q Can we look at the compliance incentives on BT, first of all. I think you will understand  
25 that they are subject to SMP and non-SMP conditions imposed under the CRF, and notably  
26 fair terms obligations and non-discrimination terms. You are aware of that, are you not?

27 A I am aware that BT is subject to various obligations. I'm not fully aware of the full range of  
28 obligations that BT is subject to.

29 Q You are presumably aware of the enforcement of penalty powers available to Ofcom,  
30 including monitoring powers and powers to impose severe penalties to require compliance.  
31 That is actually sections 96 to 104. I do not suppose you know the sections, but you know  
32 they have powers?

33 A I don't know the sections, but I am aware that there are certain powers, yes.

34 Q They are equivalent to the competition law powers. They go up to 10 per cent of turnover,

1 so they are very significant powers.

2 A I am not familiar with that.

3 Q I am sure you are familiar with the Competition Act, and that there are such powers in the  
4 Competition Act where a party breaches its obligations under the Competition Act. You are  
5 presumably aware of that?

6 A I am aware that there can be a fine up to 10 per cent of turnover.

7 Q And you are presumably aware of the equality of input undertakings that BT entered into in  
8 2006, I think, which are enforceable by Ofcom as well. You are aware of those?

9 A Not in detail, no.

10 Q You are not aware of them at all, or you are not aware of ----

11 A I'm aware that BT is subject to certain undertakings, but I'm not aware of the detail of those  
12 undertakings, no.

13 THE PRESIDENT: You know that they include an equality of input?

14 A I am aware that they include an equality of input, yes.

15 Q That is all you were being asked.

16 MR. THOMPSON: Are you aware that there is a specific right to claim damages under each of  
17 those regimes, both in relation to breaches of SMP obligations and breach of the  
18 undertakings and, as a matter of civil claims, under the Competition Act? Are you aware of  
19 that?

20 A Sorry, could you ----

21 THE PRESIDENT: Can you unpack it a bit? Just deal with this point, that for breach of an SMP  
22 obligation what was put to you first is that there is power from the statute for Ofcom to  
23 impose a penalty.

24 A I think I answered that I am aware that that exists.

25 Q You answered that and you said you are aware of that.

26 A I think I answered that already, yes.

27 Q Yes, you did and you said you were aware of that. What you are now being asked is are you  
28 also aware that there is a power in the statute for people to bring civil claims for damages  
29 suffered through a breach of an SMP obligation? Is that something you know?

30 A In general principle I am aware that this can happen. In the specific context here, as it is ...,  
31 I am not fully aware. I am aware that generally you can bring damages where you suffer --  
32 if you suffer from a breach but I am not aware specifically in this context exactly what the  
33 process is or exactly what ----

34 Q When you say "generally when you suffer from a breach", specifically if you breach an

1 SMP price control obligation you can be subject to a civil damages claim. Is that something  
2 you know?

3 A I was not aware of that, no.

4 Q You were not aware of that?

5 MR. THOMPSON: There is a statutory right of action under the Act for breach of a condition,  
6 including SMP conditions.

7 THE PRESIDENT: Yes. I think Dr. Houppis said he was not aware of that.

8 MR. THOMPSON: Were you aware that there is a specific statutory right of action under the  
9 Enterprise Act for breach of an undertaking such as the equality of input undertaking?

10 A Could you go a little bit more slowly, if you may?

11 Q I am just saying, were you aware that there is a statutory right of action for breach of an  
12 undertaking under the Enterprise Act, such as the equality of input undertaking? So if BT  
13 breaches that undertaking, there is a right of action under s.167 of the Enterprise Act. Were  
14 you aware of that?

15 A I am not aware of -- I mean, you are using terminology which is specific to the context. I  
16 am not specifically aware of what you just mentioned now.

17 Q What about the Competition Act? There is a general right of action and also a specific right  
18 of action in front of the Tribunal, which is about to be expanded, for breach of competition  
19 law. Are you aware of that?

20 A Sorry, am I aware of whether under competition law is someone is found to have abused a  
21 dominant position then people that may have been affected by that behaviour could bring  
22 damages against the company that had been found or the entity that has been found to have  
23 breached the condition? At that level I am aware, yes.

24 Q Is there a reason then why you did not mention any of these factors in your analysis of the  
25 overall incentives for BT to comply with its regulatory obligations? Why did you not  
26 mention that?

27 A I think, as I said, there are a couple of points to make in response to that. The first one is, I  
28 am not aware of this actually having arisen. I am not suggesting that it may not have  
29 happened. To my knowledge, I am not aware of damages cases against BT in this context,  
30 in relation to the kind of issues we are considering now. I was not aware that that has  
31 happened before. And the second point I think I have made already, is that there was a  
32 limited amount of time for me to respond, so you are asking a range of questions about the  
33 whole legal framework. I had the focus in my first report on specific issues I was being  
34 asked and then in my second report I responded to what Dr. Maldoom had said.

1 Q Yes, but in your second report, which I think you were not in any particular rush about, I  
2 think it was prepared in July.

3 A Sure.

4 Q You make a positive point that you have to look at the overall framework but you do not  
5 mention any of it. You miss it all out. Nothing.

6 A As I explained earlier, again two points I am going to make. The first one is I responded to  
7 the specific point that Dr. Maldoom made and I think as part of that Dr. Maldoom himself  
8 did mention, but only in passing is my recollection, only in passing, he did say, I recollect it,  
9 in one of the paragraphs of quite a lengthy report, he said there are potentially other  
10 instruments. As I recall Dr. Maldoom's report, he never said, "Look, here there is an instant,  
11 there is an example where actually BT behaved in this way and communication providers  
12 brought a claim against it", not under the current context but using the kind of framework  
13 that you are mentioning, "and they were successful and therefore, as a result of that, one  
14 would expect, BT having been penalised in that way, for that to act as an incentive". I did  
15 not see anything like that being said in Dr. Maldoom's report.

16 Q But ----

17 A Can I finish?

18 Q Yes.

19 A I did not see anything like that being said in Dr. Maldoom's report and Dr. Maldoom was  
20 making just a general point, which is there are these other potential legal instruments that  
21 could potentially be used. So in that context it did not seem to me that appropriate or  
22 necessary to have an extensive discussion about the legal framework and how this could be  
23 used. The specific point I am making is related to the specific clause, which is Clause 12.3  
24 in the contract, which was saying that interest would not be payable and that is the point I  
25 am making in para.4.6.

26 Q Dr. Houpis, you are not a litigant in person. You have got ----

27 A I am sorry?

28 Q -- one of the leading solicitors firms in the country, probably in the world. You have got  
29 very experienced counsel. Are you saying you did not know about these other features or  
30 you just did not mention them?

31 THE PRESIDENT: You have had the evidence of what Dr. Houpis knew and did not know. I  
32 think the point being put, Dr. Houpis, is you state in 4.6 that the key issue is whether the  
33 overall framework is effective in providing adequate incentives as a general conceptual  
34 point. You then go on, as you have explained, to address a particular point made by Dr.

1 Maldoom which is about regulatory certainty. But leaving that aside, what you are being  
2 asked is, given that you consider that the key question is whether the overall framework in  
3 which BT operates provides sufficient incentives, why did you not somewhere, in either the  
4 supplementary report or this report, say, "Well, in considering the overall framework, I have  
5 regard to the other pressures or constraints on BT, such as its exposure to civil liability.  
6 Even if nobody has claimed before that is a risk and a relevant consideration". But you do  
7 not mention it. That is the point that is being put.

8 A I think ----

9 Q Not that you do not mention it in this particular paragraph, you do not mention it in any  
10 place. I think that is the point of the question.

11 A I think I understand that but that has to be taken in the context of what I am writing. I am  
12 not writing this paragraph on a standalone basis. It is within the report which responds to  
13 the report of Dr. Maldoom. Now, I think it would seem to be reasonable that if it was the  
14 case that there were examples where the whole of the framework was used, the wider  
15 framework, was used by communications providers, had led to BT being found to have  
16 breached an obligation, to have received a fine, and therefore that was a relevant  
17 consideration to take into account, I think it would be reasonable for Dr. Maldoom, or  
18 anyone writing in that context trying to run the arguments that Dr. Maldoom was arguing, to  
19 actually provide the information and say, "This is the way the overall regulatory framework  
20 has been used or could be used in order to try and have an impact on BT's incentives".  
21 There was no such claim in Dr. Maldoom's report and I do not think there was any similar  
22 claim anywhere else. In that context, I think when you read the sentence it needs to be  
23 interpreted in that context. So, yes, in theory, in principle, one could look at the overall  
24 legal framework, and I think that is a fair comment to make. In practice, the relevance of  
25 that in terms of the specific issue we have before us I think is the extent to which that use  
26 actually could have an impact on BT, and I cannot see, based on in practice what has  
27 happened historically and from what I have seen from Dr. Maldoom's report, it does not  
28 appear to me that that framework has been used, and if it had been used in the past, frankly,  
29 if BT was able to charge prices above DSAC so persistently for four years, it does not seem  
30 to have been very effective to me.

31 MR. THOMPSON: You are saying that this regime would be completely ineffective because  
32 presumably neither the CPs nor Ofcom have used it? Is that what you are saying?

33 A I am not making such a grand claim. All I am saying is that it has not been put in the  
34 response to my first report. There was no suggestion that that regime has had practically an

1 impact on BT's behaviour in relation to this case. I do not think that was mentioned. I do  
2 not recall this being anywhere. And, given that, I think the implication is that one would  
3 not expect that specifically to have had an impact and, given that, I focused my response  
4 then on the specific issue which is clause 12.3.

5 Q Yes. Can we turn to the position of the CPs? It is effectively the mirror image. In looking  
6 at their incentives, it would be right to look at other rights that they had conferred by  
7 Parliament, including regulatory protections and statutory rights to bring civil claims, would  
8 it not? It would be right to take that into account as well, especially when we are dealing  
9 with five of the large companies in the country. They can exercise those rights, can they  
10 not?

11 A I think you will have to ask them. Yes, you will have to ask them. I do not know what the  
12 response is.

13 THE PRESIDENT: What is the incentive for the CPs that you are now asking about, when you  
14 say we are coming to the incentives for the CPs?

15 MR. THOMPSON: If we are looking at the incentives of CPs and the effects on ----

16 THE PRESIDENT: On the CPs to do what?

17 MR. THOMPSON: For receiving this money.

18 THE PRESIDENT: To bring ----

19 MR. THOMPSON: Ofcom is thinking about whether to give money to the CPs at the expense of  
20 BT. First of all, we look at BT's incentives because it is trying to make BT comply. In  
21 relation to the CPs, you look at what is the position for them.

22 THE PRESIDENT: The position for them? I am still not quite clear. It may be my failing, Mr.  
23 Thompson. The position for CPs, incentives, there are various kinds of incentives. One is to  
24 delay disputes, that has been argued, or to drag their feet once a dispute is started so that  
25 they can continue trading, and Dr. Maldoom talked about that. But is that the incentive you  
26 are talking about or are you talking about incentive for CPs, the effect on the incentives for  
27 CPs if they receive payment and why that might incentivise their behaviour? I am not clear  
28 which incentive for CPs you are asking about.

29 MR. THOMPSON: It is a broad question about whether they bring these disputes, for example,  
30 that is something that Ofcom will want to consider in the exercise of its discretion, and why  
31 this money should be given to them as against the other sources of revenue that they have.  
32 In my submission, that is a matter that Ofcom is perfectly entitled to take into account.

33 THE PRESIDENT: So why this money should be given to them, that is the incentive you are  
34 addressing? The effect of giving this money to the CPs on their commercial incentives or?



1 MR. THOMPSON: Yes, how they act.

2 THE PRESIDENT: Yes. Perhaps then reframe your question.

3 MR. THOMPSON: In considering whether or not to have BT pay money to the CPs, would you  
4 accept it is relevant what other sources of money the CPs would have in relation to the very  
5 same conduct?

6 A Again that seems to me a legal question. I am not sure what you are getting at.

7 Q What about any limitations on those other sources? Would that be relevant or not?

8 THE PRESIDENT: What are the other sources?

9 MR. THOMPSON: Civil actions under the three different regimes.

10 THE PRESIDENT: Perhaps I misunderstood. Are you saying would it be relevant in deciding  
11 whether – and you are asking an economist this question, not a legal submission, to consider  
12 taking into account the fact that they have the power to bring civil claims for the loss they  
13 have suffered?

14 MR. THOMPSON: Yes.

15 THE PRESIDENT: That is the question?

16 MR. THOMPSON: Would that be a relevant factor?

17 THE PRESIDENT: I think I followed. I think you are being asked in considering the economic  
18 incentives on the CPs' behaviour, when deciding whether they should receive repayment, in  
19 these circumstances an overcharge by an Ofcom decision, is it relevant to consider that if  
20 they have suffered loss they could bring a civil claim for that loss? I think that is the  
21 suggestion.

22 A As I said, I'm not familiar with the details of the legal process. If I may just give an  
23 example and maybe that will help. Are you suggesting that if there's a decision where a  
24 repayment is ordered of an amount of X are you then saying that means that the CPs, on the  
25 basis of that decision, could also bring an additional claim for damages, or the consequential  
26 loss, and therefore does that impact their incentive in the first place to try and bring a  
27 dispute?

28 Q No.

29 A OK, then, so I will move to the other, which is my understanding. So the point is that CPs  
30 have a range of different options in which they can try and protect their interests. Where  
31 they are being overcharged one option is to bring a dispute for the overcharges to Ofcom  
32 and then they have other options. My sense is, from an economist's point of view, I would  
33 expect the communications providers to look at their different options and then pick the  
34 option that would be probably the most effective. As I think has been explained by

1 TalkTalk and Sky, the overcharge is not welcome; they have strong incentives (and I have  
2 explained that in my report as well) to bring a dispute to stop the overcharge as quickly as  
3 they can. Given that, my expectation would be that they would choose the legal instrument  
4 which is most likely to be most effective in stopping the behaviour of the overcharge in the  
5 short term. I would also imagine they are also interested to make sure that BT doesn't get  
6 incentivised to overcharge again in the future. So communication providers will also want  
7 to make sure that the instrument that gets used is as effective as possible, to ensure that BT  
8 is deterred from engaging in similar behaviour in the future.

9 Q Yes, but in referring a dispute, Ofcom then makes a Determination that they have been  
10 overcharged by, let us say, £100 million. Ofcom then decides what to do about that, and it  
11 could make a direction that BT must pay them back that £100 million, or it could decide: we  
12 are not going to make that direction for repayment; you have a right at law (which they do)  
13 to bring a civil claim for the actual loss you can prove you have suffered through that  
14 overcharge, and we will leave you to bring that civil claim. They would note the finding of  
15 overcharge and you can go and bring your civil claim where you actually have to show what  
16 you have lost. Therefore, if you have passed it through, to that extent you will not recover.  
17 What you are being asked is from an economic aspect, in terms of incentives on CPs, is that  
18 relevant that there would be that alternative, and which would be preferable? Do you  
19 understand the point?

20 A I do understand the point, although I'm not sure 100% that was exactly how it was put to me  
21 earlier, but I do understand the point. So the question is that once BT pays the money back,  
22 does that have an impact on the incentives of CPs? And therefore I think there was a  
23 discussion when Dr. Maldoom said in his cross-examination that they (BT) could give it  
24 back to the Treasury. Then the question is should Ofcom award the money back to the  
25 communication providers, or whether the communication providers should make an  
26 additional claim. My sense is I have not looked at this question in detail; I have not been  
27 asked to look at the repayment and what incentives are in terms of the repayment, if it gets  
28 given back to communication providers, or if it goes to the Treasury. Also, I'm not familiar  
29 with if the communication providers were to claim for damages – because that's the account  
30 you are putting to me – I don't know what the likelihood would be of success, what would  
31 they have to prove. I would need to understand better the context in order to give you a  
32 proper economic answer, to be honest.

33 Q I think it is being put on the basis that there is a finding of the overcharge against them and  
34 that would be binding, and in a civil claim they would have to prove what they have actually

1 lost as a result. Therefore, to the extent that they passed it through they could not recover  
2 from BT. Is that the point of your questioning?

3 MR. THOMPSON: Yes.

4 A That's OK. Let me try and see if I can answer that question. I think you are asking me if  
5 the communication providers get overcharged, right, what is the damage they suffer: is it the  
6 £100 million, as we said, or might it be bigger or smaller? I think that is the question I'm  
7 being asked. Maybe I'm not. I don't want to put words into your mouth.

8 THE PRESIDENT: It is on the assumption that it might be smaller, because they may have  
9 passed it through in higher retail charges to their customers.

10 A Well, I don't think that's a fair assumption. I think if you pass the higher price to your retail  
11 customers you will lose market share, depending on the condition of the retail market. If  
12 you lose market share, then as I said in my report (because there are economies of scale in  
13 the downstream market; it's not completely perfectly competitive, I think it would be fair to  
14 say) your average costs will go up. That means your profitability goes down and then that  
15 would push you into --

16 Q We all understand that. I am not saying you have suffered no loss.

17 A But the loss could be well above £100 million. I don't see why the £100 million (which is  
18 the amount of the overcharge) determines the ceiling on the loss of the CPs. I'm not saying  
19 it would necessarily be higher, but I can't see any reason why it should be a ceiling.

20 MR. THOMPSON: But I think you agree that this is not just a restitutionary claim; it is not just a  
21 cash till whereby BT has to pay whatever is found as the overcharge; it is an administrative  
22 fact when you look in detail at the incentives on BT and the CPs. I think that is where we  
23 started?

24 A Sorry?

25 THE PRESIDENT: Was my question the point?

26 MR. THOMPSON: It was exactly, sir.

27 THE PRESIDENT: Then, Dr. Houpis, it may be less than £100 million; it may be more than  
28 £100 million, but it is not necessary that the amount the CPs have lost is identical to the  
29 amount of the overcharge paid to BT.

30 A Let me see if I can try and answer. I accept the point that if prices are higher by £100  
31 million than they would otherwise have been without the overcharge, to the extent that CPs  
32 passed some of that higher price they faced into retail prices, that will be one element in  
33 which the amount of that £100 million might be reduced. However, (and I will not repeat  
34 myself extensively) there are a number of other impacts from that increase.

1 Q The only point is a very simple point: that the amount of the overcharge may not equate to  
2 the amount of damage they have suffered commercially in that the figures might be  
3 different.

4 A With respect, I think I understand that point, but earlier you were saying it's a ceiling; you  
5 were saying whether the amount would be less. That's what I was being asked. My point is  
6 I totally agree with the statement you just made now, but I think earlier the question was  
7 different, which was whether the £100 million is the ceiling. I totally agree it could be  
8 higher, it could be lower, that's what I said.

9 Q Just a minute, Mr. Thompson. In considering whether to order the amount of the  
10 overcharge to be paid to CPs or not with the counterfactual being that they could bring a  
11 civil claim where they would recover the amount they have actually lost (maybe more,  
12 maybe less) they would then recover their loss, their true loss, would that be – and that is  
13 choice Ofcom has to say: we will order repayment or we will not; we will leave you to your  
14 civil remedy; prove your actual loss. Would that be, in terms of the incentives for CPs'  
15 market conduct, preferable?

16 A My point is I don't know, as I said earlier, exactly the legal process for proving damages,  
17 but I can see good reasons for actually the damages to be higher than the overcharge, and  
18 yet if you are actually going down the road of trying to prove those damages you might  
19 expect (because of uncertainty, because of the amount of time it would take to do it, because  
20 you are not 100% sure you have 100% of all the information) why you are well  
21 incentivised to try to take the route that the communications providers have taken rather  
22 than taking the route of going down a damages claim, even if the actual damages were  
23 higher than £100 million.

24 MR. THOMPSON: Dr. Houpis, in a way that is slightly not quite my question. My question is:  
25 is it relevant that these very large companies have three statutory rights of action to claim  
26 for their losses? Is that a relevant factor: they could claim under the Competition Act; they  
27 could claim under the Enterprise Act; or they could claim under the Communications Act. I  
28 am not saying that they would have good claims, but they could in principle bring those  
29 claims.

30 THE PRESIDENT: Relevant to the decision of Ofcom whether to order repayment?

31 MR. THOMPSON: Yes.

32 A But I think in the specific context that we've discussed, it doesn't appear to me to be relevant  
33 because in order for that to be relevant I would have to come to a view. If I understand your  
34 point correctly, Ofcom will have to come to a view and say: OK, the communications

1 providers have been overcharged by £100 million but actually the damages that have been  
2 suffered by the communications providers are not £100 million but £50 million. So  
3 therefore I should take that into consideration when I decide how much the overpayment  
4 should be. Based on my earlier point, my expectation is that I can't see that being  
5 something that it would be possible to do easily. Therefore, my presumption is that I  
6 wouldn't consider it at this point, based on the information I have, to be relevant. As I think  
7 I've said earlier, this is not something I have considered at length in my report, so I'm a little  
8 bit hesitant to give a complete answer. I'm not trying to delay, but it's not something I have  
9 considered and I'm just giving you my answer on the basis of the answer I gave earlier to  
10 the President.

11 Q What about any benefits that the CPs have received? We have talked about possible  
12 benefits on the upstream market, making it easier to enter; and we talked about pass  
13 through, with getting more money from retail customers. Are those benefits relevant to how  
14 much the CPs should receive?

15 A Right, I do not believe these are benefits. I think I've said my answer quite clearly. The  
16 CPs do not, in my view, welcome overcharging. I think both in terms of the theory which  
17 I've set out in my reports, and the practice indicates that it's not welcome, overcharging.

18 Q Not on the downstream market, but on the upstream market it make it easier to enter, does it  
19 not? The evidence is clear on that.

20 A I've had extensive discussions on this. I mean, of course you may have your view, but I  
21 think you know my view. I'm happy to repeat it, but I'm not sure it adds anything.

22 THE PRESIDENT: He does not think that is the case, overcharging to this extent.

23 MR. THOMPSON: Can I move on to the issues raised by Dr. Maldoom. I am aware of the time  
24 so I am going to take it very shortly. As to the nature of the benefit to BT, there was a  
25 lengthy debate between Mr. Pickford and Dr. Maldoom on day 5 and you deliberately do  
26 not engage in that debate in your fourth report (para.4.16). You left that on one side, so I  
27 will leave that on one side as well. At paras.4.8 to 4.12 of your fourth report (I am sure I am  
28 not going to do justice to the intricacies of your reasoning) basically you treat the  
29 overcharge to CPs as a sort of loan to BT with clear repayment terms. You say if that is  
30 what it is then you would not expect pass through, it would just sit there as a sort of a loan.  
31 I think that is basically what you are saying in those paragraphs?

32 A No, that's not what I'm saying in those paragraphs. What I'm saying is that's what Dr.  
33 Maldoom is saying.

34 Q Sorry, yes. But you were here, I think, when Dr. Maldoom gave his evidence?

1 A Yes, I was.

2 Q His idea is not that it is clear on both sides that it was sort of a loan, but that there is  
3 uncertainty on both sides and that is how his theoretical construction arises, in conditions of  
4 uncertainty on both sides, is it not? The overcharge initially is uncertain ---

5 A My report was written before Dr. Maldoom gave his evidence. My fourth report is in  
6 response to the third report of Dr. Maldoom. So, therefore, what I am saying there reflects  
7 what Dr. Maldoom said in his report.

8 Q That is how you understood it, but you now understand he is emphasising conditions of  
9 uncertainty on both sides and that is how the price rise goes up initially and gets passed  
10 through to retail, that is the construction that was debated with Mr. Pickford?

11 A My understanding is that in the response to my response I think Dr. Maldoom has developed  
12 his argument in the joint statement, to try and give more emphasis to that, yes.

13 Q Yes, and then thirdly, the issue of delay. I am not going to debate with you whether or not  
14 the CPs did or did not delay and why they might have done, but you would accept, I think,  
15 that in principle delay is a bad thing for various reasons. It is bad from the regulator's point  
16 of view, it is bad for consumers, and it is bad for certainty, but it is more and more difficult  
17 to see what has happened. You would accept that delay in itself is a bad thing?

18 A Yes, delay in the sense of higher wholesale prices that get passed on to retail customers  
19 continuing that outcome is not desirable, I accept that.

20 Q Can I now just deal briefly with commercial certainty. It is not a topic you mention in your  
21 first report, the supplementary report, you do not mention clause 12.3 at all, that is correct,  
22 is it not? Whereas in 4.6 of your fourth report you deal with it very summarily as part of  
23 your general discussion on incentives. Is that fair? You basically say it can be overridden  
24 by other incentives. It is the last two sentences really:

25 "It seems to me therefore appropriate to consider how the overall historic  
26 framework should be amended to provide the appropriate incentives for BT to  
27 comply with its cost orientation obligation in future. As long as a reasoned and  
28 evidence based explanation for the necessity to modify any contractual clauses is  
29 provided, any wider detrimental impact in terms of deterioration of regulatory  
30 certainty should be limited."

31 So you basically say: "Don't worry about it, as long as the incentives are there it doesn't  
32 matter." Is that fair?

33 A Which incentives are you talking about now?

34 Q You refer to them: "appropriate incentives for BT".

1 THE PRESIDENT: If you look at para.4.6 you refer to incentives?

2 A Yes.

3 MR. THOMPSON: Just to unpack that a little bit. In general terms, do you accept it would be  
4 undesirable for parties to believe that their commercial bargains would not be honoured or  
5 be interfered with by the regulator? In general terms, do you accept that?

6 A Sorry, I believe I have answered. My earlier answer was not "yes, I agree with you", it was  
7 "yes, I read that". I think I have answered that and I have said that in the context of the  
8 specific issue I believe that the contractual clause could be amended in general ----

9 Q I am asking ----

10 A Let me finish. In general, when you change a contractual clause, if you don't provide any  
11 justification, or if the justification was unsound in an *ex post* intervention, I can accept that  
12 could increase regulatory uncertainty as a matter of principle, yes. If that is the question  
13 you are asking me the answer is yes.

14 Q In general terms, good thing, it has been so, certainly under English law for many centuries  
15 ----

16 A Sorry, speak slowly, please.

17 Q It has been the position under English law for many centuries that contractual terms are, by  
18 and large, to be honoured, and there are restrictive public policy rules which change that  
19 situation but, in general, that is something that ----

20 A I am quite knowledgeable about English history, but it would be a little bit immodest of me  
21 to say I am familiar with hundreds of years of English law ----

22 THE PRESIDENT: Dr. Houpis has said that he accepts in general if you change a contractual  
23 clause without strong justification that would undermine commercial certainty and that is a  
24 bad thing. So that is agreed.

25 MR. THOMPSON: Turning to the specifics, would you accept that it is relevant in a regulatory  
26 context that the regulator was present when the terms of the contract were negotiated in  
27 review. Would you accept that was relevant to whether or not the contract should be there?

28 A If the regulator, when the contract was negotiated, would have all of these issues and was  
29 able to actually assess that, and the regulator had given a view, and had said at the time the  
30 contract was negotiated that it is okay not to pay interest, even if BT is found to have  
31 overcharged very significantly by £300/£400 million over a three or four year period, if the  
32 regulator had said that and *ex post* BT was found to have overcharged by £300/£400 million  
33 and then the regulator said: "Now I'm going to ask you to pay interest" then I think it would  
34 be relevant, but my understanding is this is a very specific context we are talking.

1 Q Are you assuming again that although the regulator was there he was not really doing  
2 anything? Is that the assumption ----

3 THE PRESIDENT: Dr. Houpis does not know.

4 MR. THOMPSON: He seems to be saying that we can ignore the regulator because ----

5 THE PRESIDENT: What he is saying is: if this had been specifically approved then it would be  
6 relevant. If the regulator had considered this provision and approved it then that would be  
7 in his view very relevant.

8 MR. THOMPSON: I am not putting it as high as that, I am just saying: was he there when the  
9 negotiations took place, is that relevant?

10 THE PRESIDENT: I think it is the converse to what you said, Dr. Houpis. If the regulator was  
11 present but had not specifically looked at this clause and approved it, is that relevant?

12 A It would not be relevant.

13 MR. THOMPSON: Then there is the middle case, of course, that if he was there and saw the  
14 clause that he did not act. Would that be right ----

15 A I don't think ----

16 MS. ROSE: Sir, there is no evidence that he saw a clause.

17 MR. THOMPSON: Would it be relevant that the parties are substantial commercial parties with  
18 access to competent legal advice at every stage? Would that be relevant?

19 A Relevant to whether Ofcom should award ----

20 Q Whether or not the contract should be enforced?

21 A I am not sure I am in a position to answer. I am not ----

22 THE PRESIDENT: I think it goes back to what you have said, that you need good justification to  
23 depart from the clause. In deciding whether there is good justification is it relevant that,  
24 when the contract was agreed, the parties had highly experienced legal advice in assessing  
25 the justification?

26 A I think the fact that the communication providers are informed purchasers and, as you say,  
27 they would have experienced legal teams, implies, I presume that they would have looked at  
28 that clause and try and understand the implications of that clause and then come to a view as  
29 to what the implications would be to sign. But, having said that, I am not so sure that that  
30 would be hugely relevant in terms of regulatory certainty. If then the regulator or Tribunal  
31 was to find that that clause was to be overridden because, to my mind the fundamental point  
32 was that that clause, combined with the other obligation that BT had, did not prevent  
33 certain behaviour. So I do not see how the legal advisers or in house legal teams could have  
34 foreseen that sort of behaviour at that time.



1 Q The clause was specifically directed to that particular circumstance, so I do not think you  
2 could assume that they had not foreseen it; that was the whole point of the clause ----

3 A All I said the behaviour ----

4 Q -- when Ofcom has made a certain determination.

5 A Yes, it is pretty clear in my report, I am going on the specific behaviour I have observed, not  
6 the hypothetical possibility of BT potentially overcharging by a little. What we have  
7 observed here is that BT has overcharged by hundreds and hundreds of millions, so that is  
8 the behaviour I am talking about.

9 MR. THOMPSON: Finally, would it be relevant that these substantial commercial parties have  
10 never challenged those terms before the regulator over a period of years. Would that be  
11 relevant in terms of commercial certainty?

12 MS. ROSE: Again that is not a fact.

13 THE PRESIDENT: You can answer the question hypothetically.

14 MR. THOMPSON: It is an abstract question and we can debate the facts. I did put it on an  
15 abstract basis. (To the witness): So would it be relevant that these parties had never  
16 contested the terms over a period of years?

17 MR. PICKFORD: Which contains an explicit presumption that they have not done so.

18 MR. THOMPSON: It is an abstract question. THE PRESIDENT: Put it another way, one of the  
19 rights they have under the regulatory regime is they can complain. They do not have to wait  
20 for an overcharge, and they do not have to wait for an argument about interest. You have  
21 said you think it is implicit that they would have looked at the clause, they could have gone  
22 to Ofcom and said: "This is an unfair clause, you should direct an amendment to the  
23 contract." Now, is that power that they have relevant?

24 A I understand. As I said earlier, that clause becomes particularly relevant when there is an  
25 overcharge and a significant overcharge, and so if you are asking me in the abstract would  
26 they have a reason in the absence of any overcharge, or any evidence of an overcharge  
27 would they have reason to go and challenge that clause? To my mind they sign a lot of  
28 contracts, these sort of things I would imagine are matters that take time. It is not that if  
29 there are challenges they would necessarily be able to convince Ofcom that if interest was  
30 payable that would have a deterrent effect, because there would be no overcharge, there  
31 would be no evidence on which to challenge. So in the absence of that I am not quite sure  
32 why communications providers would have necessarily the incentive to go and challenge  
33 that clause because I think the process would be quite costly and the expected likelihood of  
34 succeeding very unclear, and even "success" it is not clear to me what that would mean.

1 When you actually have an overcharge, when you actually see that that clause is not  
2 working then my understanding is that CPs did complain quickly, and my understanding is  
3 they did also say that the interest should be payable.

4 MR. THOMPSON: I can see all that in a consumer context where somebody might say: "I don't  
5 like this exclusion clause in a bank contract", but we are not talking about that, we are  
6 talking about specific commercial contracts between very large companies and in those  
7 circumstances are you still saying it would not be relevant that over a period of years they  
8 never raised the enforceability of the term with the regulator?

9 A My understanding would be that in order to challenge a clause you would have a reason to  
10 challenge that clause so negotiations happened and they ended up with the contract at the  
11 end of that - right? That contract has a number of clauses one of which is this clause in  
12 relation to interest. Now, for the communication providers to go and say: "We don't now  
13 like that clause, you should change it" I don't think this is particularly related to how large  
14 they are or what the legal teams are, etc. In order for them to go and say: "We're going to  
15 go to Ofcom now and challenge that clause" there has to be a reason I would imagine.  
16 There would have to be a trigger that would mean that the communication providers then  
17 would be prepared to put the resources ----

18 Q That is an interesting answer, Dr. Houppis, because you will be aware that the CPs place  
19 reliance on a recent decision of Ofcom, arising out of Gamma challenging an interest clause  
20 in the abstract. You are aware of that, are you?

21 A Am I aware that the CPs place weight on the *Gamma* decision, is that the question?

22 Q Yes. And are you aware that that was a dispute raised in the abstract about an interest  
23 clause, not in relation to a specific dispute but in relation to the interest clause?

24 A I am not aware of the details of that dispute as such.

25 THE PRESIDENT: You have not read the *Gamma* ----

26 A No, I have read part of the *Gamma* decision from Ofcom, which relates to the reasoning as  
27 to whether interest should be awarded and whether they consider different incentives. I am  
28 not familiar with the background of the dispute and why it arose.

29 MR. THOMPSON: In that case I will take it no further. I have no further questions, Sir.

30 PROFESSOR MAYER: You make it clear in your second report in paras. 1.4 and 2.3 that you  
31 are not going to consider the issue of interest payable, which is fair enough, but Dr.  
32 Maldoom, in his evidence, said that interest might be payable but it would be minimal, it  
33 would be a sort of cash deposit rate, which is effectively equal to zero. Can I just clarify  
34 that what you have in mind is not such an interest rate?

1 A That's correct.

2 Q Would it be fair to describe it as an interest rate that is closer to the relevant cost of capital?

3 A I think the answer to that is yes. ... I have not been asked to consider that question, and I  
4 appreciate you have said that in your introduction. I think the answer to the question is, yes,  
5 I would expect it to be closer to the relevant cost of capital, than to zero, yes.

6 THE PRESIDENT: Mr. Pickford, do you have any questions?

7 MR. PICKFORD: I do have some questions, yes.

8 Re-examined by Mr. PICKFORD

9 Q Dr. Houpis, you have been cross-examined now for a period of a day, so there are a number  
10 of points that I would like to pick up on. Could you go, please, firstly, to ST1, volume 3,  
11 which is the Frontier Report that Mr. Thompson took you to yesterday, and go to tab 14,  
12 please. They are slightly confusingly numbered.

13 THE PRESIDENT: The Frontier Report of April 2012.

14 MR. PICKFORD: I am grateful. Could you turn, first, please, to para.9, p.3 of the report.

15 A Yes.

16 Q Could you read para.9, please, to refresh your memory.

17 A Yes.

18 Q Of the two alternatives that you describe here, if applied to a given group of services, is  
19 there actually a difference between them in terms of the prices that are permitted under  
20 them?

21 A I think in terms of what would happen to the resulting prices and revenues compared with  
22 fully allocated costs, you could get the same result.

23 Q The same result. Could you go, please, to annex 2 of your report, which is towards the end.  
24 It does not seem to be a numbered page. If you can find p.33, it is the next one on. You had  
25 a discussion yesterday about whether your test only kicked in if the DSAC test had been  
26 breached or whether it applied in any event. Could you briefly refresh your memory of  
27 annex and then have a look at figure 7, please. Could you please explain figure 7 to the  
28 Tribunal? Take them through it slowly.

29 A That describes the way the test would apply in factors, in two stages, and as you can see,  
30 what it says is in the first stage, or we call it the first test, then if the price is above DSAC  
31 then the cost orientation condition has not been met. I think if you go to the right hand side  
32 arrow it says "no, price is below DSAC at the individual service level", and as you can see  
33 there is a little arrow then which says you go to the second stage. So even if a price is  
34 below DSAC you go to the second stage and check whether the revenues for the group of

1 services is above fully allocated cost. If it is, which is then the left hand side arrow, then the  
2 cost orientation obligation has not been met. If you find out that the revenues for the group  
3 of services were below the fully allocated cost then the cost orientation obligations will have  
4 been met. I think this relates to the discussion yesterday that there was some lack of clarity  
5 potentially as to whether the second stage test applies even if the first stage test is passed. I  
6 think the point is that the report sets out that it would apply, even if the first stage test is  
7 passed.

8 Q You had a discussion with Mr. Saini about certain similarities and certain differences  
9 between price controls and the Sky and TalkTalk proposal, how one should interpret  
10 condition HH3.1. So that I am not putting words in your mouth, if I could quote to you the  
11 relevant part of the transcript, this was on Wednesday, p.83, starting at line 3. It should  
12 begin, "The price control has a completely different way it works".

13 THE PRESIDENT: Yes, line 3.

14 MR. PICKFORD: Line 3, yes. Could you read that exchange to yourself, please, down to the  
15 next question from Mr. Saini and then your next answer.

16 A (After a pause) Yes.

17 Q You should have read down to, "That objective can be achieved with the obligation of fully  
18 allocated cost standard"?

19 A Yes.

20 Q I would like to remind you of the context. I would like you now, please, to take up bundle  
21 BT3, and turn, please, to para.6.107 and 108 on p.125. Could you read, please, to yourself  
22 those two paragraphs, 6.107 and 6.108.

23 A (After a pause) Yes.

24 Q Just so that you are clear what the context is here, if you turn back to p.122, you will see the  
25 sub-title, discussing a price control and PPCs.

26 A Yes.

27 Q The paragraphs that I referred you to, are they consistent, inconsistent or simply not relevant  
28 to the evidence that you gave to Mr. Saini?

29 A They are consistent. What I understand Ofcom is arguing here is that when they are looking  
30 at constraining the prices in this current context, there are two principal ways you could do  
31 this, cost orientation or a multi-year price control, and what Ofcom is saying is that under  
32 multi-year price control, the regulated company would have incentives to improve  
33 efficiencies to reduce costs, which you would not expect the company to have if it was  
34 under a cost orientation obligation.

1 Q Could you now go, please, to 159 in the same document. You will see that this is dealing  
2 with the remedies in the wholesale AISBO market, and could you turn to p.160, you were  
3 asked some questions by Mr. Thompson about Ofcom's aims when imposing regulation, but  
4 he did not actually take you to Ofcom's statement in relation to that. Could you please read  
5 under the sub-title, "Aims of regulation", paras.7.10 and 7.11.

6 A (After a pause) Yes.

7 Q Are those aims that you recognise as honest?

8 A They are.

9 Q Can you explain what, if anything, you draw from this passage about Ofcom's aims when it  
10 was imposing condition HH3.1?

11 A I conclude the first one is that they wanted to make sure that wholesale prices would not be  
12 set an excessive level, because that could lead to higher prices for consumers. Therefore,  
13 that would operate, I think, as Ofcom says, against the industry consumers. The second  
14 conclusion I would draw is that Ofcom also considered this to be attractive because it would  
15 imply or increase the likelihood of downstream competition between communication  
16 providers that would compete with BT's downstream arm and that was desirable.

17 Q You explained in answer to another question that you relied on evidence in the 2004  
18 statement on the issue of barriers to entry.

19 A Yes.

20 Q Can I take you, please, to p.397 of the same document.

21 A Yes.

22 Q Could you please read para.B4.41, "Assessment of market power on AISBO", and B4.42  
23 under the heading, "Likelihood of competition developing in the future".

24 A (After a pause) Yes.

25 Q Is this the type of thing you had in mind or was it something else?

26 A Precisely. That was the thing I had in mind.

27 Q Can you explain what, if anything, you draw from this passage as regards the imposition of  
28 condition HH3.1?

29 A That the likelihood of upstream entry, entry in this market to compete with BT, was quite  
30 low because, as the paragraph set out, there are significant barriers to entry for a new entrant  
31 and also it also sets out that the expectation was the position will not change over the next  
32 two to three years. So if one thinks about the dynamic efficiency criterion then I think what  
33 one could read into that is that promotion of downstream competition was quite desirable in  
34 terms of the balance of downstream competition versus upstream competition, when setting

1 wholesale prices, and therefore that would imply that it would be more desirable for  
2 wholesale prices to be lower as a result of the cost orientation obligation rather than higher.

3 Q You were also asked by Mr. Saini about the interpretation of para.7.63 in ----

4 A The same document?

5 Q 7.63, the same document. It is on p.149.

6 A Yes, I remember.

7 Q Some of these are also repeated in Core Bundle E but I have taken you to BT3 because a  
8 number of the parts we have gone to were not in it.

9 A Yes.

10 Q I do not believe that you ever gave your own view as to precisely what your interpretation  
11 was. You were asked various questions about, for instance, Ofcom's interpretation. For the  
12 purposes of the question that I would like to ask you, I would like to make clear the terms  
13 on which I am asking. So I would like you to put aside everything postdating 2004 and  
14 imagine you are answering the question in 2004. So you will have the benefit of what you  
15 know in 2004 but nothing else. On that assumption, as a professional economist, what  
16 would your interpretation be of para.7.63?

17 A Yes, I think there are two points in terms that Ofcom makes for choosing the cost  
18 orientation rather than price control. The first one is that the AISBO market is in a  
19 relatively early stage of development and I think what I would read into that is that because  
20 the market is at an early stage of development it was difficult to forecast costs into the  
21 future, because to forecast the costs into the future in order to set a price control it is  
22 necessary to also forecast the volumes in that market. And because typically price controls  
23 will last for three to four years, you have to forecast the average cost for up to three or four  
24 years from 2004. In other words, in 2004 in order to impose a price control Ofcom would  
25 have had to come to a view on what the average cost of the services would have been in  
26 2008. And I think that in the context of a new market, not just this one but any new market,  
27 it is a very challenging exercise. Therefore, given that, I would understand that it would be  
28 preferable to impose a cost orientation obligation because you are still interested to make  
29 sure that the prices would not be set at an excessive level. The second part of the  
30 explanation is that this is necessary to give time for the effects of the cost orientation  
31 obligation to impact on the competitiveness of the market and my view is that by not  
32 imposing a price control that would also allow the competitiveness of the market to develop,  
33 because if Ofcom had imposed a price control, because of the uncertainty I mentioned in  
34 terms of forecasting forward, there would be a good chance of setting prices at too low a

1 level. Now, that chance is symmetric. Ofcom could have set the prices at too high a level  
2 or it could have set the prices at the too low a level, but in terms of promoting efficient entry  
3 upstream, i.e. in the provision of AISBO services, if it was to get the price wrong in terms  
4 of forecasting it too low, then that could deter entry that would be efficient. Therefore, in  
5 my view, imposing the cost orientation obligation rather than a price control is also  
6 consistent with Ofcom achieving, allowing the competitiveness of the market to develop in  
7 some form.

8 Q You were taken to the 2009 Lease Lines Charge Control. I am not proposing to take you to  
9 it now. You were asked about how Ofcom would go about constructing a basket or  
10 grouping of services and whether it was good regulatory practice to consult on that  
11 grouping. Do you recall that?

12 A Yes.

13 Q This was in discussion with Mr. Saini.

14 THE PRESIDENT: Can we put BT3 away?

15 MR. PICKFORD: You can, Sir. Thank you. In that context you were then asked about the Sky  
16 and TalkTalk test and whether it would be good regulatory practice to consult on the  
17 grouping associated with that. The first question I would like to ask you is, do you know  
18 whether there were any significant services within the wholesale AISBO market, as defined  
19 in 2004, which you did not include in your WES, BES and main link grouping?

20 A No, I do not believe there are significant services I have excluded.

21 Q Would you have expected Ofcom to have consulted when it decided on the market  
22 definition for the wholesale AISBO market?

23 A In general, yes.

24 Q You explained in your evidence that you could be permitted to go outside the initial  
25 grouping of the products to demonstrate under-recovery elsewhere, where there are common  
26 costs in common with the other products that you are relying upon, and you said so long as  
27 that was not in markets where there are price controls or in competitive markets. Could  
28 you, please, therefore, explain what is the relevance of the initial grouping in your test and  
29 how important or otherwise is it to its ultimate application?

30 A The purpose of the initial grouping is there will be a set of services that are subject to cost  
31 orientation and those services will share fixed and common costs between them and they  
32 will also share fixed and common costs with other potential services. Those services are  
33 together because they are sold together, they are found to be in the same market, and  
34 therefore the grouping follows from that assessment. So in that sense that would support

1 the wider grouping. Then one needs to take a view as to whether you group all those  
2 services together, for example all WES, BES and main links, or whether you might group  
3 them more at the sub-group level. I explained that, this is explained in my report, I think in  
4 the current context the proper grouping was the wider grouping of services.

5 Q You also said you should not include competitive markets but I do not think you explained  
6 why. Could you explain to the Tribunal why you said you should not include competitive  
7 markets?

8 A Yes. The reason I said the competitive markets should not be included is because the under  
9 or over-recovery in competitive markets - I am saying that either way. In principle you  
10 could have over or under-recovery compared to fully allocated costs in competitive markets.  
11 The reason I am saying the competitive market should not be included are two-fold. The  
12 first one is that when BT produces the accounts it allocates common costs between all of its  
13 services, so that already of course they are allocated to competitive products and to  
14 regulated products. Therefore, in my view, you can propose to do a review as to whether  
15 the prices within the regulated products recover the costs or not. My view is the appropriate  
16 starting point would be on the basis of the cost that BT has already allocated to those  
17 products, so that is already a decision that has been taken. Because to do otherwise would  
18 provide an incentive to BT, or an additional incentive to BT, when it is actually producing  
19 those accounts, to try and load more costs into the regulated products and less cost into the  
20 competitive products. Now, the second reason is that I think the prices in competitive  
21 markets, that is the definition, they are determined by competition, not determined by BT,  
22 and therefore, in my view, you should not allow costs that effectively are the costs that BT  
23 incurs in the competitive markets, where the prices were below the fully allocated costs, and  
24 the recovery should not be allowed to be counted against an over-recovery in the regulated  
25 markets because I cannot see any reason why that would lead to any improvement in  
26 allocative efficiency. So just to go back and explain that a little bit more, the reason why we  
27 are saying that for a group of cost orientated services prices could be above fully allocated  
28 cost and still that would be consistent with cost orientation in relation to the context of this  
29 question, is because BT may have priced another set of services below fully allocated cost.  
30 As a result of that, that means that you would have lower demand for services for those  
31 products where BT priced above full allocated costs, and then you would have higher  
32 demand for services for those services where BT had priced below fully allocated cost. It is  
33 precisely that difference which means that overall you would see allocative efficiency had  
34 improved or could have improved as a result. Okay? So the reason we want to allow BT to



1 justify an over-recovery in a group of cost orientated services is precisely that. So it is not  
2 in the abstract. It is exactly because we are assuming that because the prices in another  
3 market were priced below fully allocated cost, and this led to an increase in demand, that  
4 increase in demand counterbalanced the reduction in demand from prices being above fully  
5 allocated cost in the cost orientated services. I do not see any reason for such a link  
6 between competitive services, products offered in competitive markets, and products in  
7 regulated markets because if you reduce prices from let's say DSAC for a group of regulated  
8 products, if you reduce them from that level to fully allocated cost there is no reason to  
9 expect price in competitive markets to move. Prices in competitive markets are determined  
10 by the conditions of competition in those markets. Okay? So if I reduce prices from DSAC  
11 to fully allocated cost I get an increase in demand as a result of that, and I do not get any  
12 reduction in demand anywhere else. So that, in my view, would lead to an improvement in  
13 allocative efficiency and that is the reason why competitive services should not be included.

14 Q You were asked by the President why Ofcom did not impose a price control in high  
15 bandwidth AISBO in 2009. Do you know whether Ofcom found SMP in high bandwidth  
16 AISBO in the 2008 market with the preceding imposition of the charge control?

17 A My understanding is it did not find SMP in that segment.

18 Q Do you know what approach Ofcom has adopted to the wholesale AISBO market in 2013?

19 A I am sorry, do I know?

20 Q Do you know what has happened since 2009 and what approach Ofcom has adopted now in  
21 2013?

22 A I am not fully -- in relation to this market or in relation to ----

23 Q In relation to the wholesale AISBO market in 2013. If you do not ----

24 A I think it is cost control again but I am not sure.

25 Q You discussed with Professor Mayer the cost standard relevance to an entry decision in the  
26 wholesale AISBO market and you said it was not DSAC but you did not say what it was.  
27 So what is it?

28 A I think Professor Mayer, my understanding of his question, was that whether BT could  
29 actually price, given the specific circumstances in this market, where there are significant  
30 economies of scale, could BT price above DSAC and still we would see no entry, because a  
31 potential entrant observing those prices, which would be above DSAC, would not  
32 necessarily enter because they would ask themselves, "If I was to enter this market what  
33 would be my likely returns?" And the answer to that question would be, "Well, what will  
34 happen to the prices after I enter?" I think Mr. Mayer's question was that if, as an entrant, I

1 believe, that the regulated company could reduce those prices potentially significantly after  
2 I enter, then my expected returns could be much lower compared to the prices that I  
3 observed pre-entry.

4 Q My question is simply what, if anything, is the relevant cost standard from an entry  
5 perspective? You said it was not DSAC.

6 A Okay. So my point is that you could price ----

7 Q If it is the same answer, that is fine.

8 A So ... if you could price all the way to DSAC or even higher than DSAC you would still see  
9 no entry. For me the relevant standard, if you want, would be as an entrant what would I  
10 expect my costs to be in order to be able to enter, and therefore I would need some  
11 guarantee that the prices could be at a level that would allow me to recover my costs if,  
12 under Ofcom's theory, I wanted to allow entry which would be allocatively efficient. In my  
13 view, if you set the price at FAC, that gives you a reasonable cost benchmark and it means  
14 that if a new entrant wants to come into the market, then they would have to be more  
15 efficient than BT in order to be able to compete in that market. Therefore, for me, using  
16 fully allocated costs as a standard to set the cost orientation would be consistent with  
17 promoting entry and promoting efficient new entry.

18 Q You were taken briefly by Mr. Thompson to Mr. Higo's first witness statement which is at  
19 CBC tab 8, in particular paras.25 to 29 which deal with the detrimental effect of BT's high  
20 prices. I put to you that all of those paragraphs only concern the levels of prices and not  
21 relative prices. Could you read to yourself, please, para.28. (Pause to read)

22 A Yes.

23 Q You agreed with Mr. Thompson that these all concerned only the levels of prices and not  
24 relative prices. Can you explain why you say that in relation to para.28, please? (Pause)

25 A Sorry, do you mind repeating your question?

26 Q My question is you agreed the proposition put to you by Mr. Thompson that all of these  
27 paragraphs, including para.28, only concern the issue of absolute prices and not relative  
28 prices. I just wanted to ask you if you could explain that, please, why you say that in  
29 relation to para.28.

30 A I was making a simple observation in relation to the response that the effects that were set  
31 out were resulting from the statement about BT's higher prices on Sky. I then, I think,  
32 explained that actually under the potential for aggregation, which is the proposal as I  
33 understand it from BT, that could also have an impact on the level of prices that Sky would  
34 face, so it's not just about the structure; it's not just that it would be changing the structure of

1 prices that would be having an impact on the overall payment. The point I made was that  
2 actually the amount that would be paid under an aggregation (if aggregation was possible)  
3 the amount would be higher. I think the implication is that depending on how the different  
4 communications providers, the different costs that they face, that increase could be different  
5 between different communications providers. So they could be affected in different ways.

6 Q You can put away that bundle, please, CBC and pick up instead bundle CBE, tab 12 p.494.  
7 This is the reason why we are all here, Condition HH3. That is the internal numbering, it is  
8 external numbering p.44 of that tab 12.

9 A Yes.

10 Q It was put to you that BT could never have understood that it was required to comply with  
11 your test on the basis of this condition. Is the aggregate CCA FAC approach that you have  
12 proposed, do you say in economic terms that that is the only means of satisfying this  
13 condition, or do you consider that there could be other means?

14 A I am saying that the CCA fully allocated cost is a way of satisfying the condition. There  
15 could potentially be other means, but the CCA fully allocated costs would be certainly a  
16 way of satisfying the condition.

17 Q In exchange with Mr. Harrison you said you had not attempted to calculate the actual  
18 overcharge, taking into account the occasions on which BT price below DSAC and you  
19 were only trying to illustrate the maximum potential over-recovery relative to FAC that is  
20 permitted by the DSAC test. I think later you said that Mr. Robinson had calculated the  
21 overcharge. Could I just take you, please, to CBD 17 para.2.8.

22 THE PRESIDENT: Is this something you need to put to Dr. Houpis? I think some of these  
23 figures have been corrected.

24 MR. PICKFORD: They have been corrected.

25 THE PRESIDENT: Is there any reason to put it to him? He says he has not calculated it, so I do  
26 not see why you need to put it to Dr. Houpis.

27 MR. PICKFORD: It was simply a point of clarification. I am very grateful. We do not need to  
28 deal with it.

29 Could you then put away bundle D and pick up bundle C again, tab 16, the second witness  
30 statement of Mr. Morawetz. Go please to para.15. You agreed with the proposition from  
31 Mr. Thompson that the first sentence of para.15 indicated that TalkTalk has acted in the  
32 wholesale Ethernet market.

33 A The second sentence, yes.

34 Q Sorry, the second sentence, I beg your pardon. The first and second together. Do you mean

1 the wholesale Ethernet market with which we are concerned in this case, the wholesale  
2 AISBO market?

3 A No.

4 Q You do not?

5 A No.

6 Q What market were you talking about?

7 A I presume when Mr. Morawetz says they operate in a competitive market, what they mean is  
8 the higher bandwidth market, because the AISBO market is not a competitive market. The  
9 lower bandwidth market is not a competitive market.

10 Q Do you have any first-hand factual knowledge about whether TalkTalk actually competes in  
11 the wholesale market?

12 A I do not.

13 Q You were asked about whether various issues were relevant in considering the implications  
14 for regulatory and contractual certainty of applying or disapplying clause 12.3 in the  
15 contract of the CPs. From an economic perspective I am going to ask you whether another  
16 factor is relevant. Is it relevant or not whether BT has SMP? The context for the questions  
17 was whether all of these factors were relevant or not to the economics implications of  
18 potentially overriding the contractual term.

19 A Yes, I would expect the fact that one of the parties that is signing the contract has significant  
20 market power to be relevant, because that would affect the likelihood that communication  
21 providers could turn to someone else if they couldn't sign a contract with the SMP provider.  
22 And being an SMP provider, knowing that the likelihood of the person you are negotiating  
23 with to go to someone else is very small (because that's the very consequence of being an  
24 SMP) I think gives you quite a lot of bargaining power, and I would expect it gives you a  
25 lot of bargaining power in the contract negotiations.

26 Q Thank you. Those are my questions in re-examination.

27 THE PRESIDENT: Thank you. We will take a ten minute break. We have a couple of questions  
28 for you, so you are not quite finished yet. We will come back at five past 12.

29 Adjourned for a short time

30 THE PRESIDENT: Can we just go back to some very basic points about what the regulator was  
31 trying to do. I think it is a given that the telecoms regulator wants to encourage efficiency  
32 and competitiveness. You are nodding, but you need to say "yes"?

33 A Yes.

34 Q And they will set an SMP condition with that broad objective in mind?

1 A Yes.

2 Q It would be a fair approach, and there are various kinds of efficiencies, and all the experts  
3 are agreed - they may not be commonplace for a lawyer, but I think they are commonplace  
4 for an economist - the three kinds of efficiency that you set out in your joint statement?

5 A Yes.

6 Q And that includes allocative efficiency and here lower wholesale prices will lead to lower  
7 prices in the downstream retail market and so Ofcom will want to prevent the wholesale  
8 prices of BT being too high, that would be a fair objective?

9 A That is correct.

10 Q They also wish to encourage dynamic efficiency, which here involves encouraging new  
11 investment by BT and also potential competitive entry in the upstream market, the  
12 wholesale market so far as possible. That would be also a fair objective?

13 A Yes, I wasn't sure if I heard correctly regarding efficient investment by BT, is that what you  
14 said, or encouraging investment by BT?

15 Q New investment by BT, but if you want to qualify that and say efficient investment by BT?

16 A I think in general my expectation would be the objective would be to encourage efficient  
17 investment, and within that to also, to the extent they can, encourage also innovation.

18 Q Yes, and competitive entry by ----

19 A And then also entry in the upstream market

20 Q Yes, and you referred in your evidence, it seems a long time ago now, to there being a trade-  
21 off sometimes between the various objectives, or one could say perhaps that there is a  
22 balance to be struck - I think this is right, is it not - if the cost orientation ceiling is too low  
23 then you might discourage efficient new investment by BT and discourage competitive  
24 entry?

25 A If the cost orientation ceiling is too low, then you could discourage efficient investment by  
26 BT and you could also potentially discourage efficient entry as well.

27 Q Yes. As I said, I think these are very basic points but I want to make sure I have understood  
28 it. So one goes back to this idea of a trade-off or balance to be struck between the goals of  
29 dynamic efficiency as justifying them and allocative efficiency, which is a fair way of  
30 putting it?

31 A That's correct.

32 Q Clearly, there can be wrong ways of trying to achieve that and, indeed, you say Ofcom have  
33 adopted the wrong way and you explain that in detail. But, would you agree there is no  
34 single right balance between dynamic and allocative efficiency, there is no one right

1 balance, it is a matter of regulatory judgment, whether you want to favour one or the other?

2 A Not in general. I think that is a question which has to be asked in a specific context. I do not  
3 think in general you can say there is no right balance. I think, depending on the context you  
4 can then come to a view as to whether there is a balance to be struck. Just to be clear, when  
5 we say "balance" we mean you give up a bit of one for the benefit of the other and my view  
6 is that there are circumstances where you can actually achieve both with one regulatory  
7 policy. There is not necessarily a trade-off.

8 Q I see. But, would it be fair to say you can choose to favour one more at the expense of the  
9 other in both directions?

10 A I think generally, as a matter of regulatory policy, could you come to a view after you have  
11 analysed markets etc. that you are prepared to favour one over the other. I think as a general  
12 principle that is possible, yes.

13 Q And on that general principle it would be a judgment to be formed as to where you want the  
14 balance to come out?

15 A That's correct.

16 Q Now, on this market you say, as I have just mentioned, Ofcom did it the wrong way and on  
17 dynamic efficiency you are very clear for the reasons you have explained that you consider  
18 allowing prices up to the level of DSAC is not necessary. Indeed, I think you go further,  
19 you say it is not appropriate in order to promote dynamic efficiency?

20 A That's correct.

21 Q Just to be quite clear, you were asked a question about this just before the short break by  
22 Mr. Pickford regarding what you say about FAC, but if I can take it from your reports, to  
23 make sure I have understood the point - they are in bundle D, and you have written a lot of  
24 reports for us, I think more than anybody else, but if we go to your fourth report at tab 11,  
25 and on p.5, para.2.2.1, you say:

26 "Efficient entry into the market for the provision of services that are offered by BT  
27 is promoted if entrants are able to offer the same services at costs no higher than  
28 BT's efficient costs, which, for the group of services that are subject to cost  
29 orientation, are in general at FAC, not DSAC."

30 Then again, further on at p.23, at para.3.38:

31 "Where dynamic efficiency considerations through promoting efficient entry in the  
32 provision of the AISBO services are important, an approach to cost orientation that  
33 reduces the risk of prices for such services being set below the costs of an efficient  
34 entrant would be justified."

1 Then a few lines down you talk about FAC, and you say:

2 "For this reason, the FAC metric is used commonly as a basis for setting access  
3 prices for a number of other wholesale services provided by BT, where dynamic  
4 efficiency considerations are also relevant."

5 So have I understood this correctly: what you are saying is that if prices are below FAC  
6 then that would discourage new entry upstream, and your point is there is no justification  
7 for the much higher ceiling of DSAC?

8 A That is correct. The only comment - I think you said "would discourage" or "could  
9 discourage". I would say it could discourage entry upstream, yes, efficient entry upstream.

10 Q Then just clarifying one thing for me, your FAC test which involves a grouping, because it  
11 is an aggregate across a grouping, I thought you had said earlier in your evidence in answer  
12 to Mr. Thompson that all BT's services that are subject to a cost orientation obligation, that  
13 that was the relevant ----

14 A Let me clarify the point. There are two, I think, related questions. The first one is - let me  
15 just put it in terms of what would happen in the future. I know it is a case about the past,  
16 but I think it will help answer the question. The first point is that there will be a group of  
17 services that are subject to cost orientation such as the WES, the BES, such as the AISBO  
18 services, and the FAC test, it will be required that the revenues from those services are no  
19 higher than the full allocated cost of the services. Let's say that's the BES, okay?  
20 Now, at the same time, I've said in the proposal that it should not be applied  
21 mechanistically. So, in principle, you could say, "Okay, for the BES, and we stop at that, if  
22 revenues are above fully allocated costs we will find a breach, and if they're below we  
23 don't". However, what I said is, no, it should be applied in a non-mechanistic way as DSAC  
24 is, and then I provided some explanations as to what non-mechanistic way actually means.  
25 In that context, one of the elements that would be part of assessing cost orientation in a non-  
26 mechanistic way would be to say that if prices for that group of services were higher than  
27 fully allocated costs then that could promote allocative efficiency, because it implies that  
28 because BT is trying to recover its fixed and common costs flexibly, it may be pricing  
29 another group of cost orientated services below fully allocated costs. If that was the case  
30 then the non-mechanistic approach would imply that BT would be able to go to Ofcom and  
31 say, "We charge more than fully allocated costs for this group of cost oriented services, but  
32 the reason we've done this is because we have under-recovered from cost oriented services,  
33 as a result of which demand for this group where we have set prices above fully allocated  
34 cost is lower, but demand for this other group of cost oriented services where we set prices

1 below fully allocated costs is higher. Therefore, within the non-mechanistic application,  
2 what I meant was that BT could have the opportunity in that context to argue that a recovery  
3 above fully allocated costs could potentially be justified if there was under-recovery in  
4 relation to other cost oriented services.

5 Q When I read 3.21 in your fourth report on p.16 where you set out the justification I did not  
6 see that one there.

7 A I understand that point, and the reason for that was, I think, firstly, that paragraph is within  
8 the overall context. I think consistently throughout Houpis 1 I have always said - I must  
9 have written this ten times, which says if you find that costs are above fully allocated costs  
10 and there is under-recovery elsewhere then that could be allowed. I think what the  
11 particular paragraph you refer to does is effectively make that operational. I accept that I  
12 use the term "services", I wasn't specific in the paragraph in terms of exactly which services,  
13 and I think that's because within the context of everything that I've said before, I think I was  
14 taking it that that would be the natural interpretation of that sentence.

15 Q Thank you, that is clear.

16 PROFESSOR MAYER: Dr. Houpis, if I could just pick up some points relating to your model,  
17 and I am referring to tab 8, which is your first report, para.2.7.2 on p.6, and you make the  
18 point that in terms of promotion of dynamic efficiency pricing in relation to FAC is  
19 appropriate and you say the use of DSAC alone would provide a higher return than required  
20 to achieve efficient investment. I just want to try and understand what you have in mind  
21 behind that. Perhaps we can go to p.8, and the diagram that you provide there to try and  
22 illustrate and understand what you have in mind. As I understand it, what you are saying is,  
23 "If we are thinking about efficient investment in relation to a group of services X and Y", as  
24 you have in that diagram, "together, then if we considered it in relation to DSAC of X and Y  
25 separately, we would be providing too much incentive because we would be recovering the  
26 common costs twice". Is that what you mean by "providing an excessive incentive to  
27 invest"?

28 A Yes, if I could say, in the specific context if these other services that the firm is offering and  
29 the regulator comes and says, "I consider", because in that context Ofcom would come and  
30 set a price control within this context so that the firm can recover its costs. In order to do  
31 that, the regulator has to take a view on what's the appropriate cost to capital.

32 Q Right.

33 A And if it does that then fully allocated costs, the fully allocated costs measure, will reflect  
34 the return which the regulator considers is appropriate for the regulated company to be able



1 to undertake efficient investments. There is a long discussion that goes on in order to set  
2 that cost of capital for BT, and ultimately Ofcom comes and says, "This is what is". In the  
3 current case it was 11.4 per cent in the period. Now, if you allow then the company to  
4 recover more than fully allocated costs then the returns would be higher than 11.4 per cent,  
5 and in that context I think the answer to your question is, yes, given that the regulator takes  
6 the view that 11.4 is sufficient to provide incentives to invest efficiently something higher  
7 than that would incentivise inefficient investment.

8 Q Let us assume that the cost of capital is 11.4 per cent, and now let us say that for some  
9 reason the regulator is interested or concerned about promoting investment and/or entry in  
10 relation to service X as a set of services and service Y as a set of services, and wishes to  
11 ensure that there is sufficient investment in relation to those sub-markets.

12 A Right.

13 Q In that case, if you are concerned about entry, is it not the case that you do actually have to  
14 apply a common cost to X alone to encourage entry into X and the common costs alone in  
15 relation to Y to encourage entry into Y?

16 A When you say - you have just got to stand back because the question in terms of  
17 encouraging entry in one part of the market to the other would be related to, as I said earlier,  
18 what prices that entrant would expect to collect afterwards.

19 Q Just leave that point aside for the moment, and let us assume that the prices do stay at the  
20 cost level. Is it the case then that one would have to set a price at a level that is consistent  
21 with the common costs being attributed to each of those markets individually?

22 A I don't think so. If I can put it in the specific context, there are significant economies of  
23 scope between the different services. In that context, what efficient entry should try and do  
24 is take advantage of the economies of scope, i.e. the production of those services together.  
25 So my expectation would be that if you were to say, "I am going to set the prices extremely  
26 high in some sub-segment", such that a new entrant in this sub-segment would be able to  
27 recover the whole of the fixed and common costs of those services, I think it would risk  
28 very inefficient entry in that context.

29 Q So you are saying that some of those costs may essentially be relevant to other part of the  
30 market as well from the point of view of entrants as well as the incumbent. To the extent  
31 that the economies of scale that the entrant can derive are not as great as those of the  
32 incumbent, would that not still mean that the price would, in some measure, have to be  
33 above the ----

34 A Well, I think this is an issue that comes into the discussion the Chairman asked me earlier. I

1 think, as a regulator you do face those issues generally. Where there is a company that has a  
2 particular position in the market then you have to take the view as to whether you need to do  
3 something to skew the balance to try and help a new entrant in order for them to be able to  
4 enter the market. I think, in general, you could try and see if that would be a relevant  
5 consideration. My view in the specific context is, given the barriers to entering this market,  
6 because we are having an abstract conversation, in the specific context of the AISBO  
7 market, where the sunk costs were so significant, by Ofcom's own admission, across the  
8 whole market, I do not see what would be the rationale to try and incentivise entry in the  
9 lower bandwidth market by trying to follow such a policy. As you can see, prices were not  
10 just set at DSAC, prices were set significantly above DSAC. BT set prices significantly  
11 above DSAC and no entry has occurred in the market. So I think one can have a theoretical  
12 discussion and say would that possibility arise, and I think theoretically it could arise. In  
13 the specific context I think the evidence, and there was a lot of discussion of theory, but  
14 there's a little evidence and this is a clear piece of evidence, these prices overall in the  
15 market over the period were DSAC roughly. If you look at the revenues between 2006 and  
16 2009, overall these were broadly consistent with DSAC, and if you look at individual  
17 services in some cases they were significantly above DSAC, as you know, otherwise we  
18 would not be here. And no entry has occurred in that part of the market. So I do not think  
19 that could be, although theoretically it could be possible, I do not think it is particularly  
20 relevant.

21 THE PRESIDENT: When you say no entry has occurred, I thought it was indeed put to you by  
22 Mr. Pickford that in high bandwidth AISBO markets, by the time of the 2008 and 2009  
23 assessment, BT no longer had significant market power, so entry had occurred?

24 A Correct. I think I said "lower bandwidth", so I am talking about the lower bandwidth part of  
25 the market, which is, as I said, meant 97% of the market, and I am specifically talking in  
26 this example that Professor Mayer asked me about, that is the part of the market where  
27 Ofcom found there are very significant barriers to entry in terms of sunk costs, and it found  
28 that the potential revenues would not justify entry. And that contrasts that part of the  
29 market with the higher bandwidth part of the market where Ofcom found that both the  
30 revenues were higher and the costs can be expected to be lower.

31 Q Where there has been entry?

32 A And that is where it has been, correct.

33 PROFESSOR MAYER: As we discussed earlier on, that might well reflect an anticipation that  
34 prices could be cut post-entry and thereby to deter an entrant coming into the market in the

1 first place. Is that not equally true even if prices are set in relation to FAC, that a potential  
2 entrant could be discouraged because it anticipates that higher prices can be cut to, shall we  
3 say, LRIC or DLRIC?

4 A I think ultimately, if you believe that the real effective cost floor is incremental cost or  
5 marginal cost and therefore you expect that prices could be cut all the way down to  
6 incremental or marginal cost, then I think for a potential new entrant what they would be  
7 thinking is that that would be the price that I would expect BT not to be able to go below  
8 without then facing predatory pricing type allegations. It is possible that BT could engage  
9 with quite aggressive pricing before necessarily pricing at incremental cost, so it is possible  
10 that a new entrant would think, "Actually there might be some room above that, BT would  
11 not reduce prices that low", and therefore in that sense FAC could provide a reasonable  
12 benchmark for efficient entry. But as a matter of principle, as a matter of theory, then one  
13 would expect BT to be able to price all the way down to incremental cost or marginal cost  
14 without -- Let me just try and rephrase this. I think BT could price down to that level with  
15 an expectation that it could face some competition issues if it priced very aggressively, but I  
16 think if it priced below the incremental cost then it could definitely be accused of deterring  
17 entry into the market, so that would be the floor for the pricing that an entrant would expect,  
18 assuming that the entrant obviously knows what the incremental costs are and so on.

19 Q If, within your relevant group of services, as you say, the advantage of bundling together a  
20 group of services is that it allows prices to be set above FAC in some components and  
21 below FAC in relation to others, where prices below FAC is it not the case, even within  
22 your terms, that that will discourage entry into those particular services?

23 A I think, if I understand your question, what we are facing here is different types of demand  
24 for different sub-segments and let's take the different bandwidths. So it is 100 bandwidth,  
25 1000, etc., and then the propensity, the willingness to pay for the high bandwidth is  
26 relatively higher, and therefore if you were to price overall at fully allocated cost you would  
27 expect higher prices for relatively higher bandwidth services. In my illustration I have a  
28 little example. I have not turned to it yet. I will come to it in a moment. You would expect  
29 prices for higher bandwidth services to be potentially higher than fully allocated cost, prices  
30 for lower bandwidth services to be relatively below the fully allocated costs, with overall  
31 revenues recovering fully allocated costs. Now, in that situation I think a new entrant would  
32 have to take a decision, "Would I go in and try and compete in the part of the market where  
33 prices are above fully allocated cost or the whole market?" My sense is a strategy which  
34 says I am going to go and compete only in that part and not the rest, I would expect that

1 probably to be self-defeating, unless there is some other constraint, because if prices go  
2 down in that part of the segment as a result of new entry then the incumbent would also be  
3 able to use those prices. It would just rebalance the prices. So ultimately what you would  
4 end up is with an incumbent which prices overall at fully allocated cost, and if the new  
5 entrant cannot match that, cannot match the fully allocated cost, it will not be able to  
6 compete with the incumbent. So I am not saying that such a strategy would be impossible  
7 or it might never happen, and indeed it may in certain circumstances, but I think in the  
8 longer term I would expect -- it is a bit like an arbitrage. You could do it for a period of  
9 time but ultimately I think if you wanted to be able to compete with the incumbent you  
10 would have to be able to offer the full range of services.

11 Q So, as I understand it, what you have in mind is in terms of providing dynamic efficiency,  
12 you are anticipating that a new competitor or a potential entrant would not precisely but  
13 approximately replicate the set of services that BT is currently providing, that is would  
14 probably enter a cross for something like the whole range of services. Is that right?

15 A Not necessarily. I can see a situation in a market, as it is the way it happened, where  
16 somebody would come at one end of the market and then BT would keep prices at that end  
17 of the market at a reasonable level to allow that new entrant to operate at that level with  
18 potentially higher costs than BT, and that could be an outcome. So I am not excluding that  
19 as a possibility. But I think what we need to ask ourselves is, is this the kind of entry that  
20 would deliver the kind of dynamic efficiency benefits we are talking about here? Okay. In  
21 my view, that kind of entry at the margin, where a new entrant effectively prices more or  
22 less at the same level as BT - in which case there does not seem to be any significant  
23 benefits from entry in terms of price - , and that new entrant knows that if it was trying to be  
24 more aggressive than BT, BT could just reduce prices down to the fully allocated costs or  
25 incremental costs in that market and that it would have difficulty following if it is not as  
26 efficient. I would imagine that that would also deter that new entrant from really trying to  
27 aggressively compete with BT. So, yes, entry could happen in some segment of the market  
28 but would not deliver the kind of benefits that would justify the kind of allocative  
29 inefficiencies that I have mentioned earlier. In my view, it would not and, as I say, in terms  
30 of the sub-1Gbps part of the market there is no evidence of such entry occurring. I know  
31 entry occurred in the above 1Gbps segment but, as I think I said yesterday, my understanding  
32 is that there was already entry in this segment of the market back in 2004. Not as much as  
33 in necessarily 2008 but there was entry already in 2004.

34 Q In terms of thinking about the relevance of evaluating charges in relation to FAC, even if

1 prices could be dropped as far as LRIC or DLRIC, are you still saying that there is a merit  
2 in looking at charges in relation to FAC even if you would not expect the dynamic  
3 efficiencies to be observed?

4 A I am sorry, do you mind just repeating that? I think I understand but just to be clear.

5 Q Even if it is the case that the dynamic efficiencies of entry do not take place because BT  
6 could drop its prices to deal with it, is there still a merit in looking at charges in relation to  
7 FAC? Does it answer an interesting set of economic questions?

8 A If the question is, in that scenario we discussed, would it be appropriate having an overall  
9 constraint of fully allocated cost even if, in that scenario, where some prices might be above  
10 fully allocated cost, the fact that a new entrant would know that if they entered that part of  
11 that market, it could just get taken away, would that still be desirable in terms of dynamic  
12 efficiency, I think I will come back to my earlier point which is, I think, if a new entrant was  
13 able to come in and compete with BT - in principle I am talking about - and be able to do  
14 that by charging prices on average below fully allocated cost, I think that would be  
15 desirable. That is a desirable outcome because it could lead to prices effectively falling on  
16 average and then, as a result of that, the kind of dynamic efficiency we talked about earlier  
17 would materialise. Both the prices falling and through more innovation or more  
18 competition, etc. So, in my view, that would still be desirable, bearing in mind we are  
19 comparing this to DSAC. We do not have something else, another benchmark in mind, you  
20 know, that is between an average constraint of fully allocated cost compared to another  
21 constraint at DSAC.

22 PROFESSOR MAYER: Thank you.

23 MR. HARRISON: Just on the practicalities of how your model would work, basically it is a zero  
24 sum game. Prices above FAC have got to equal prices below FAC, therefore any change  
25 has got to zero out as far as how your model works. Is that fair?

26 A It is about ... revenues but, yes, in broad terms if the revenue is above FAC.

27 Q Yes.

28 A Okay.

29 Q Factors influencing that calculation are not just prices. There are a range of other factors that  
30 will affect that relationship between external revenues and FAC. There is going to be  
31 volume, not only for the particular products but, in your examination of the groups, could be  
32 for any other groups that are cost orientated. Changes in volume could alter FAC on any  
33 products.

34 A That is so, yes.

1 Q Similarly new products coming in would immediately change the calculation as well  
2 because it would alter FAC?

3 A That is true for FAC, but also true for DSAC. I am trying to understand exactly what ----

4 Q No, no, no. What I am trying to get at is how your model works in application terms. I am  
5 just trying to understand how it would work in application terms. Given that there are all  
6 those variabilities that changes, any one of those changes, automatically means the prices  
7 need to be adjusted, how would that work in practice sort of *ex ante* in looking forward?

8 A I understand. I think maybe just backtrack for a second, there is an important point to  
9 clarify in terms of my test would work in a similar way as the DSAC test in terms of the  
10 application. So what happens, let's take a hypothetical, that the test is in place, then what I  
11 would expect BT to do is to look at the range of cost orientated services. It will have a view  
12 as to what the FAC of those services is and it will try and set a set of prices based on its best  
13 forecast of volumes, etc., for that. Okay? That is the *ex-ante*. Then demand happens,  
14 volumes happen, costs clarify, and then BT will see how the revenue is compared to FAC.  
15 Now, let's say that when volumes materialise, and as a result of that what happens is one  
16 group of cost orientated services shows that the revenues in relation to FAC are 10% higher,  
17 because of the kind of uncertainty you mention. Now, in principle communication  
18 providers could come and say, "There is a breach here. It is supposed to be at FAC and it is  
19 10% higher". What I would expect to happen is that BT, if that was the case, a case is  
20 brought, the appeal will go to Ofcom and say, "Hold on a second, we did our best. We  
21 forecasted our costs to the best of our ability. We forecast the volumes to the best of our  
22 ability and we set our prices on that basis". Now, we are not able to perfectly forecast  
23 volumes. I totally accept that. I totally accept there is uncertainty and I think, if it is a  
24 reasonable case for Ofcom on that. I do not see why Ofcom would apply another charge if  
25 revenues, in that example, were found to be above FAC, say, by 10%.

26 Q On that basis what we have is a situation, an assumption that you are making, that BT  
27 approaches this in trying to achieve its obligation and does not game play in that scenario.  
28 Does that not create an asymmetry in how it would work, because clearly if it went wrong  
29 and they went below FAC (a) there is a question of what that does to market efficiency, and  
30 I will not go back there, but, secondly, it would mean that they would have no mechanism  
31 for reclaiming that back again.

32 A OK, so the point is if, as a result of trying to meet their obligation, the outcome is that the  
33 revenue is below FAC, could that be detrimental? In my view, if you know and you expect  
34 that if your revenues are above that on average, you wouldn't be penalised; I don't see why

1 you should set your prices so that persistently, consistently over time your resulting revenue  
2 is below FAC. I'm not saying it's going to happen. Both things could happen. They set  
3 their revenues in one year; they are below FAC; the next year they are above. As long as I  
4 think the explanation is reasonable, and that's clear, then I don't see why that should  
5 happen.--

6 Q Yours would be over a period of time, in looking at what happens over a period of time as  
7 opposed to individual years?

8 A No, I think the test would apply in individual years, but when Ofcom comes to take a view,  
9 it would have to take into account, if there have been a number of years where this test has  
10 been running, there could be relevance of the period over which this happened. I think that  
11 would become a relevant factor. Would it actually in practice be binding? I don't know, but  
12 over time I would expect that if BT could show consistently that sometimes it was above,  
13 sometimes it was below and to the best of their ability it was a random event, then I think  
14 that will be useful information in terms of Ofcom coming to a view as to whether in a  
15 particular year, if for a particular group prices were above cost, that would be relevant in  
16 coming to a view as to whether there was a breach or not.

17 Q OK. Thank you.

18 THE PRESIDENT: Mr. Pickford, anything arising out of that?

19 MR. PICKFORD: No, sir.

20 THE PRESIDENT: Thank you very much, Dr. Houpis. You have been with us a long time. You  
21 are now released as a witness.

22 Witness withdrew

23 MR. PICKFORD: That concludes our economic evidence. Obviously we have an accounting  
24 expert.

25 THE PRESIDENT: Mr. Robinson, yes.

26 MR. READ: Sir, I will call Mr. Coulson, but while he is just making his way to the stand can I  
27 just mention one point before he takes the oath. As you know, on Monday evening we  
28 served his fourth expert's report and that was handed up to the Tribunal on Tuesday. That  
29 report followed your exchange with Mr. Saini on day 2 of the hearing, and in particular the  
30 issue about how it is going to be raised with Mr. Coulson. BT believes that having put it  
31 into a fourth report in the way that we have, it will save a considerable amount of time for  
32 the Tribunal to have it, and indeed for the other parties to, in short, know what Mr. Coulson  
33 is going to say before he actually says it.

34 BT also considers that the report simply replicates what Mr. Coulson's reply evidence would

1 have included had the matter been raised in the defence. No-one seems to be objecting to it,  
2 or no-one has raised an objection since Monday and therefore I would propose to ask Mr.  
3 Coulson to adopt that fourth report as his evidence.

4 MR. SAINI: I am content, sir, that the report goes in.

5 THE PRESIDENT: There is no objection so it can go in.

6 MR. DAVID COULSON, Affirmed

7 Examined by Mr. READ

8 Q Mr. Coulson, can I ask you to take core bundle D tab 14, to look at the document there, and  
9 to go p.38 and I ask whether that is your signature?

10 A Yes, it is.

11 Q Is there anything you want to add to that report?

12 A Yes, there is. There was one page missing from my CV in my first report.

13 Q I think that has been distributed to everybody. Subject to that point, do you adopt that  
14 report as your evidence in the case?

15 A I do.

16 Q Sir, I want to ask one very minor point of clarification.

17 THE PRESIDENT: I just wanted to say that the revised CV that we received is identical. I know  
18 a lot of adjustments have been made by Mr. Coulson to various things, but the further CV is  
19 identical to the initial CV. We could not detect any adjustments other than the typeface. If  
20 you want to add it as well. It was appendix A to your report, was it not, your CV?

21 A It was, yes.

22 MR. READ: It is possible, of course, that in the process of copying – anyway, the new CV is the  
23 one that you want to rely upon for the purposes of this report?

24 A Yes.

25 Q Can I ask one small point of clarification. Can I ask you to look at para.4.5 p.23 where you  
26 talk about your model being edited to be used to provide answers in a wide number of  
27 different scenarios or enquiries made of it. How easy would that be to achieve?

28 A Yes, it would be quite easy.

29 Q You say that the scenarios are not limited to the scenarios which you have set out in the  
30 results. How flexible will it be to be able to deal with different scenarios?

31 A Yes, the model was built to be flexible to take a variety of different scenarios. As I say, I  
32 think it would be relatively easy.

33 Q Thank you. Can I ask you to go to tab 15 in the bundle, and go on in that document to p.11.  
34 Unfortunately I can see that in my bundle in fact it has not been signed. I do not know



1           whether the copy there has been signed or not?

2   A    No, it has not.

3   Q    Could I ask you then to take BT32.

4   MR. SAINI: Sir, I am content if it saves time, for it to be accepted that that is his report.

5   THE PRESIDENT: If it is adopted, it is your report. There is a signed copy. This is your report?

6   A    Yes.

7   MR. READ: This is your report. Somewhere there is a signed version of it?

8   A    Yes.

9   Q    And do you accept that as your evidence?

10  A    I do, yes.

11  Q    If we go to divider 16 we see your third report there and at p.13 there is your signature.  
12       Again, do you adopt that as your evidence in this case?

13  A    Yes, I do.

14  Q    Finally, and I hope I have got this right, I think it should be at tab 19 in the same bundle,  
15       there should be a further report from yourself. I hope it has gone into tab 19 in the bundle,  
16       sir?

17  THE PRESIDENT: Yes.

18  MR. READ: That is your fourth report and again if one looks at p.12 one sees that that is your  
19       signature. Do you see that?

20  A    I don't think I've got it in my version.

21  THE PRESIDENT: You have not got it at all?

22  A    No, I don't believe I do.

23  Q    Perhaps you want to put it in. Can you insert it at tab 19.

24  A    Yes. (Handed)

25  MR. READ: You see your signature at p.12. That is your signature and do you adopt that report  
26       as your evidence as well?

27  A    Yes, I do.

28  Q    Finally, I just want to go to tab 2 of this bundle which is the joint statement that you entered  
29       into with Mr. Robinson and yourself.

30  A    Yes.

31  Q    One sees on the final page, p.10, yours and his signatures. If one goes back to p.7 one sees  
32       some revised calculations in para.3.3 and 3.4 set out the agreement that you have reached.  
33       Do you see that?

34  A    Yes, I do.

1 Q If you go over the page to 3.5 and 3.6 there are then a series of further figures which were  
2 produced.

3 A Yes.

4 Q Can you explain who produced those?

5 A They were produced by Mr. Robinson.

6 Q Did you, for the purposes of the joint statement, consider those particular figures?

7 A No, I did not.

8 Q Thank you. If you just like to wait there you will be asked some more questions.

9 Cross-examined by Mr. SAINI

10 Q Mr. Coulson, I would like to ask you some questions on behalf of Ofcom. I understand you  
11 are being called as an expert witness in the proceedings, but in fact you are also a witness  
12 that has some detailed factual knowledge concerning the dispute. Is that correct?

13 A That's correct.

14 Q Is that because you were employed by BT for certainly part of the time while Ofcom was  
15 considering the disputes?

16 A Yes, that's correct.

17 Q I just want you to help me, if you can, in relation to dates. It was not that clear from me  
18 from your CV. May we go, please, to your first report, divider 14 p.3 of 53 where you  
19 describe your qualifications and professional background. I am just wondering if you can  
20 help me with some dates. When did you join Ernst & Young?

21 A It was in June 2011.

22 Q June 2011. If I can just get the dates of the Final Determination and the Provisional  
23 Determination, we know that the Final Determination was 20<sup>th</sup> December 2012 and the  
24 Provisional Determination was 9<sup>th</sup> February 2012. Was it the case that while you were at  
25 Ernst & Young you were assisting BT in their dealings with Ofcom in relation to these  
26 disputes?

27 A Yes, that's correct.

28 Q If I can then seek some clarification of para.117, you say that before joining E&Y, which  
29 you have now said was June 2011, "I worked in the group regulatory finance team at BT for  
30 five years". So that was the five years immediately before joining Ernst & Young?

31 A Yes, that's correct.

32 Q Can you just explain to us what your particular title was, and in particular your relationship  
33 with Mr. Dolling, from whom the Tribunal has heard evidence?

34 A Yes, I had a number of different titles actually during my time at BT. So when I started my

1 title was Head of 21 cn and network costing. I then had the title of Head of Group Costing,  
2 and then I later had the title of Head of Regulatory Finance.

3 Q Your relationship with Mr. Dolling?

4 A Mr. Dolling joined the team whilst I was there. I can't remember the exact date, but Mr.  
5 Dolling joined the regulatory finance team, but at the time that he joined I was a direct  
6 report to him.

7 THE PRESIDENT: He was working under you?

8 A No, I was working for Mr. Dolling.

9 Q You were working for him?

10 A Yes.

11 MR. SAINI: He was above you in the hierarchy as it were?

12 A That's right, yes.

13 Q Would it be fair to say, then, if one looked at – going on in Appendix A in this particular tab  
14 to p.40 where you have given some further dates.

15 A Sorry, where?

16 Q Page 40, this is your more extended CV. You describe some particular roles. I think you  
17 have just repeated Head of Group Costing.

18 A Sorry?

19 Q Divider 14?

20 A Yes, mine seems to be slightly different to yours. My CV is right at the back, but I have got  
21 it now. That's fine.

22 Q It may be that I am wrong. Do you have your CV? It is p.40 of your report.

23 THE PRESIDENT: He has got the CV, I think. It is the same document.

24 A I have got my CV.

25 MR. SAINI: Does your page have Head of Group Costing in the middle?

26 A That's right, yes.

27 Q You say there that from December 2007 to 2008 you had a responsibility which included  
28 product costing and profitability for BT Group.

29 A That's right.

30 Q Then you have expanded upon that there a bit later. Would it be fair to say that in your time  
31 at BT you straddled two areas, the two areas being both regulatory finance and also costing  
32 of products?

33 A Yes, that would be fair, yes.

34 Q Would it also be fair to say, and perhaps we can turn back to p.3 of your ----

1 THE PRESIDENT: I am sorry, Mr. Saini. (To the witness): You straddled those areas at the same  
2 time, or over the course of your time at BT? You see the distinction?

3 A Generally speaking I would say they would have been in serial not parallel so I would have  
4 had some responsibilities for doing product costing at one time, and then another time I  
5 would have had responsibility for regulatory costing.

6 MR. SAINI: I think it is, first, product costing and then later on regulatory finance?

7 A Well, actually it is a bit more complicated than that.

8 Q Perhaps you can explain?

9 A Actually when I first joined BT, although I did join the regulatory finance team I spent  
10 about a year, I moved out almost immediately, after a few months, and I spent about a year  
11 on a one-off project that had nothing to do with regulatory finance - I think I refer to it in  
12 my CV here at the very end, where it says: "Transformation of BT's internal trading model".  
13 So I was asked to assist with a project that was outside of the regulatory arena and that took  
14 about a year.

15 Q I understand. I was then just going to take you back, please, to para. 1.17 on p.3. We have  
16 dealt with the issue of your role with regulatory finance.

17 A Sorry, which page?

18 Q Page 3, para. 1.17, your first report?

19 A Yes.

20 Q We have dealt with your role in group regulatory finance. We have described your role in  
21 the costing area, but you were also, it seems, involved - if one goes just over half way down  
22 - you say, after referring to leased line control and wholesale local access charge:  
23 "Prior to this, as Head of BT's Group Costing Function, I was responsible for BT's  
24 regulatory cost allocation models."  
25 So cost allocation was one of your special areas, is that right?

26 A Yes, it was an area that I'd spent quite a lot of time in.

27 Q If I can ask you another, more general, question, which is that you are aware that in this case  
28 there were SMP obligations, cost orientation obligations imposed on BT, are you not?

29 A I am, yes.

30 Q And you are aware that their regulatory finance team was the entity within BT that had to  
31 put together accounts, effectively, which showed how those cost orientation obligations  
32 were being fulfilled?

33 A That's right.

34 Q What was the dialogue between the regulatory finance team, of which you were, at one

1 point, head, and those people who were costing the products? In other words, was there  
2 ever a dialogue where the regulatory finance team would say: "It looks like DSAC has been  
3 exceeded in this past year, and that we ought to be concerned from a regulatory point of  
4 view about the future costing of our products"?

5 THE PRESIDENT: When you say "costing" do you mean pricing?

6 MR. SAINI: Pricing, I should say "pricing", "the future pricing of our products". Was there ever  
7 such a dialogue?

8 A My memory of the events at the time is that there was not such a dialogue. Let me explain a  
9 little bit more. When I first became involved in this area, I think it was only with hindsight  
10 really, and probably the advent of these various disputes, that it was remarkable, actually,  
11 looking back that there was not the focus on DSAC and the linkage between what the  
12 pricing teams were doing and the regulatory finance team, was actually quite absent.

13 Q So, just taking it in stages, it is a very frank answer, the regulatory finance team was aware  
14 of DSAC and you describe it in your statements?

15 A The regulatory finance team was responsible for producing DSAC so, yes, it was aware of  
16 it.

17 Q And the regulatory finance team was aware that DSAC was a measure, if not the only  
18 measure for cost orientation used by Ofcom?

19 A Well, actually, when I joined the team it was quite difficult for me to find anyone within the  
20 regulatory finance team that really could explain to me what the significance of DSAC was.  
21 I found a few people that could explain to me how DSAC could be generated and the  
22 models that they used to do that, but there did not seem to be an awful lot of intelligence  
23 around actually what this thing was for.

24 Q So the regulatory finance team was reporting DSAC but you are saying that your  
25 understanding at the time was that no one really knew why they were reporting DSAC?

26 A No, and I think there is probably another relevant factor here. I think it might have been  
27 before I joined but certainly it was either before or soon after I joined, the obligation for  
28 PwC to audit the DSAC numbers had fallen away, or had already fallen away - I don't  
29 exactly remember when. The regulatory audit was a very complex, long task which  
30 happens every year and the BT regulatory finance team take very seriously, and it uses a lot  
31 of resource at BT to actually go through the numbers. It was quite clear to me that if  
32 something was dropped from the audit it would definitely have much less of a profile, if you  
33 like, within the regulatory finance team. I think that that is probably what happened with  
34 DSAC.

1 Q Just going back for some clarity on your earlier answer, within BT's structures, what is the  
2 entity that decides on pricing, what is it called? Is there a name of it?

3 A It is pretty difficult to generalise, it doesn't really work like that.

4 Q Let us deal with Ethernet?

5 A Ethernet at the time, the key pricing decisions were being made by the pricing team within  
6 Openreach. I refer to them as the "pricing team" I'm not sure what the exact term was.

7 Q And is it your evidence based on your factual knowledge at the time, that there was no  
8 dialogue going on between regulatory finance and the pricing team as regards cost  
9 orientation?

10 A That's correct.

11 MR. SAINI: I am going to turn to another subject.

12 THE PRESIDENT: Would that be a suitable place to break? We will return at 2 o'clock. Are we  
13 all right for time, Mr. Saini?

14 MR. SAINI: I was not here yesterday when the estimates for Mr. Robinson were given. I think I  
15 will be another half hour at least with Mr. Coulson.

16 THE PRESIDENT: I think we were told about half an hour.

17 MR. SAINI: We will comfortably finish today then.

18 THE PRESIDENT: Yes, so be it. 2 o'clock.

19 (Adjourned for a short time)

20 MR. SAINI: Mr. Coulson, you described before the adjournment that there was group regulatory  
21 function, then a pricing function. From your knowledge, was there also a compliance  
22 function within BT that was making sure that BT's regulatory obligations were being  
23 complied with?

24 A Yes, that's my understanding, yes.

25 Q From your knowledge, was the group regulatory finance team reporting to the compliance  
26 function?

27 A No, not to my knowledge.

28 Q Can I ask you about the question of regulatory financial statements, as I understand it from  
29 your various reports you accept that regulatory financial statements are a very important  
30 source of information for communications providers - is that correct?

31 A Yes, I would, yes.

32 Q Would you accept that they provide the only visibility as far as communications providers  
33 are concerned into BT's compliance with cost orientation obligations?

34 A Well, I think certainly they provide the primary visibility. I don't know for sure, but I would

1 imagine that there are other routes - for example, through Ofcom.

2 Q Would you also agree with me that it is very important, unless there are compelling  
3 circumstances, that there should not be changes made to the regulatory financial statements?

4 A Yes, I think it's important that the regulatory financial statements are as accurate as possible.

5 Q You may have open still your first statement, which was divider 14, and I was focusing on  
6 para.1.17 at p.3. You may recall that, where you were describing your experience. I  
7 considered with you the regulatory finance and the costing function, but you also over half  
8 way down:

9 "Prior to this, as Head of BT's Group Costing Function, I was responsible for BT's  
10 regulatory cost allocation models."

11 Please help me if you can on this: you know that there is a dispute in this case about the  
12 allocation of, for example, connections and rentals - you are aware of that, are you not?

13 A I am.

14 Q So would it have been part of your role to develop models which would assist in deciding  
15 where particular costs would be allocated?

16 A Part of my role at that time was to make sure that the regulatory financial statements were  
17 created in accordance with Ofcom's annual consultation on the form and the contents of the  
18 accounts. For example, in one particular year where new services were being introduced,  
19 such as Ethernet services, Ofcom may well have asked BT to disaggregate or to further  
20 refine some of the products that were reported in the RFS, and part of my responsibility  
21 would have been to ensure that my team were able to do that if that's what Ofcom wished us  
22 to do.

23 Q So you would, for example, devise a methodology for deciding that particular costs, let us  
24 say electronic costs, should be allocated to connections of rentals?

25 A As you're probably aware, there are thousands of cost allocations that exist within the RFS.  
26 They don't all get reviewed and set up at the same time, it's much more of an evolutionary  
27 process. So, as new requirements came up, and one way of a new requirement may be a  
28 new service may be introduced, then certainly part of my team would have been responsible  
29 for understanding what that service was and then devising a cost allocation method for it.

30 Q Would you agree with me that there are two working principles that one can adopt when one  
31 is looking at cost allocation. First of all, when you decide to allocate a cost to a particular  
32 product or service, there must be some logical rule applied?

33 A Yes. What's the most common thing to do is to apply some sort of framework that you use  
34 as your benchmark and then you would apply your decisions according to that framework.

1 Q The second working rule I think in this case is that the decision as to where then to decide to  
2 allocate costs is for BT?

3 A No, not entirely. I remember, when I was a part of BT's regulatory finance team, having  
4 quite in-depth and detailed conversations with Ofcom, and in particular, as I think I  
5 mentioned earlier, I was invited when I first joined BT on 21CN products, which was BT's  
6 new network that they were rolling out at the time. So again, this is related to the fact that I  
7 was making earlier, the point I was making earlier, which is often when someone as senior  
8 as myself would be invited would be when new products and services were being  
9 introduced that were considered to be material. The point that I'm making is that at that  
10 time Ofcom were heavily involved in discussions with myself about exactly how the costs  
11 would be allocated. It was more of an information gathering exercise from Ofcom's point of  
12 view and explaining, but ultimately they then consult on those in the annual consultation  
13 document.

14 Q Would you agree that, as a general principle, the primary decision as to how to allocate  
15 costs is made by BT, and on occasions Ofcom has become involved in the process - would  
16 that be a fair summary?

17 A I think the emphasis is actually just exactly the wrong way round. I think that Ofcom,  
18 especially for the more material cost allocations, has become increasingly more active in BT  
19 regulatory financial statements over the last several years, and I think where I would say BT  
20 has most - is left on its own, if you like, for want of a better expression, mostly is probably  
21 the more immaterial items.

22 Q Could I ask for you to be provided with bundle B, which is the Determinations.  
23 THE PRESIDENT: Just before you do that, when you say "increasingly involved over the past  
24 several years", what sort of period?

25 A Primarily, I think, the period that I was last at BT, which when I left was the spring of 2011,  
26 so I think by then. Of course, that was following the PPC disputes. By then Ofcom were  
27 becoming more and more actively involved in BT's cost allocations. Having said that, as I  
28 said, for the big material decisions, as soon as I joined actually, which was in 2006, Ofcom  
29 were already deeply involved in discussion around 21CN for example.

30 MR. SAINI: I was going to ask you, please, to go to bundle B, which is the Determination  
31 bundle, p.328., and to table 13.37.

32 A Yes.

33 Q Can we take, just as an example, the very first item, the BES 100 rental, and if you look at  
34 the fourth entry, which is external revenue less external DSAC, one sees some quite



1 substantial figures there, 6.3, 8.6, 3.8, 0.2 - do you see that?

2 A Yes, I do.

3 Q That is the difference between external revenue and external DSAC?

4 A Yes.

5 Q As I understand your evidence, this would have been noticed within the regulatory finance  
6 team, but no one within the regulatory finance team would have communicated that to a  
7 compliance function or to the pricing function?

8 A Well, that's not really exactly what I said, so I'll clarify.

9 Q Please clarify?

10 A Clearly that would have been noted by the regulatory finance function who produced the  
11 results. I think what I was suggesting was that there wasn't some sort of automatic process  
12 whereby these numbers were communicated, but that doesn't preclude the fact that  
13 somehow there may have been some communication around these numbers. I, personally,  
14 wasn't involved in any such communication, so I'm not aware of it. Clearly, a company the  
15 size of BT, there are lots of people with lots of different responsibilities, and I'm sure that  
16 potentially some of them could have discussed these issues with each other. But, as I said,  
17 there was no specific inherent mechanism that I was aware of, or was involved with, that  
18 would have communicated those numbers to some sort of compliance function.

19 Q You had a very senior role. You were the head of regulatory finance, were you not?

20 A Yes, that's correct.

21 Q So if there had been any formal reporting system - in other words, if an alarm bell had rung  
22 - you would have known that there was a system requiring you to report it to the compliance  
23 function or to the pricing function?

24 A I think perhaps some more context might help with this. The line that you've alighted on is  
25 BES 100 rental. I think, certainly my memory from when I was at BT, was that this  
26 sensitivity to a DSAC on an individual product - i.e. a rental - was certainly not acute. I  
27 distinctly remember looking at markets in aggregate in the first instance. You'll probably  
28 appreciate that there are something like £15 billion worth of costs that need to be allocated  
29 across all of BT's products and services. Clearly the more and more granular these  
30 allocations become, the less meaningful they become in the abstract. I think, by the time  
31 you're getting down to individual bandwidths, individual services, the sensitivity would  
32 have been much less than, say, something much more aggregated.

33 Q So is it your evidence that these very substantial figures which, on their face, would ring  
34 alarm bells, did not ring alarm bells because as far as the regulatory finance function was

1 concerned, they were aggregating between connections and rentals and therefore there was  
2 not a problem?

3 A That would have been part of it. Certainly when I was at BT and particularly in the early  
4 few years where I was, as you say, the head of regulatory finance, there were various  
5 markets that were reported each year with different returns on capital employed, some of  
6 which were seemingly much higher than BT's cost of capital. Therefore, perhaps some of  
7 them would have been above the DSAC measure. The sensitivity around that wasn't there  
8 as far as I could see.

9 Q You are aware, are you not, and I think this becomes clear from the figures you have seen in  
10 this case, that even if one aggregates there is a very, very substantial level of overcharging,  
11 if that is the right word?

12 A Yes. Yes, and I think, as I said, we did look at ROCEs, as they're called, "return on capital  
13 employed", at the market level, but again I think with a product that is relatively new there  
14 may well have been the expectation that you would have needed to observe the ROCE over  
15 time before you reached the conclusion that it was excessive. Broadband was a good  
16 example of that. The broadband returns at the time that these numbers were coming up  
17 were relatively high, but it was also acknowledged that there had been a big upfront  
18 investment in broadband technology, years of where the ROCEs had been relatively low,  
19 and then, in the fullness of time, over the investment life of the products it may well have  
20 been that those returns looked reasonable.

21 Q If we just stick with these particular Ethernet services for the moment, and I would like you  
22 to distinguish if you can between what you think may have happened and what you know  
23 happened. As I have understood your last answer, your evidence is that it may be the case  
24 that BT took comfort from an aggregation or by looking at the overall ROCE figures? It  
25 may be the case but you do not definitely know that - is that the position?

26 A Well, what I do know is that certainly DSACs on individual services in individual years  
27 would not have rung alarm bells.

28 Q And that is within the regulatory finance department?

29 A Correct.

30 Q What would have rung an alarm bell?

31 A That's a difficult question to answer. Hypothetically speaking, I guess, well perhaps an  
32 intervention from another part of BT. You mentioned the compliance function that might  
33 have asked the regulatory finance function to explain some of these numbers and may have  
34 put them into the context that seemed to be missing, or it may have been that over ten years,

1 say, there was a number in excess of a certain ROCE over a persistent period of time, but  
2 it's difficult to answer in any more specific terms.

3 Q What I am confused by, Mr. Coulson, is what you say about the pricing function. You said  
4 the pricing function, as far as you were aware, you worked within that area for ----

5 A I did not work within pricing.

6 Q Sorry, you worked in the costing function?

7 A Yes.

8 Q The pricing function would have to know about price controls, would they not?

9 A Well, I think it would depend on which product they were pricing.

10 Q In this particular case we know that from 2008 onwards for low bandwidth a specific RPI  
11 minus X price control was imposed - you recall that, do you not?

12 A That was from 2008/09.

13 Q Yes, I am just taking an example.

14 A Yes.

15 Q So there would have to be some communication to the pricing function that, "Guys, when  
16 you price this product be aware that there is a specific price control there". Does that  
17 follow?

18 A Yes, that follows. Yes.

19 Q As I understand your evidence, there was no communication to the pricing function that in  
20 addition to price controls there is also a separate cost orientation obligation. Is that your  
21 evidence? There was no such communication?

22 A If you are talking specifically about Ethernet, obviously prior to 2008/9 there was not a  
23 charge control, so I think if there had been some communication around there being a cost  
24 orientation obligation I was not aware of it.

25 Q You are not aware of any such communication?

26 A No.

27 Q Can I ask you, please, to put that way. I want to ask you some more specific questions on  
28 three particular accounting issues. I will just tell you what they are before we come to each  
29 of them. There is an issue concerning provisioning costs, if you recall?

30 A Yes.

31 Q And within that there are two sub-limbs. One is the level of provisioning costs and the  
32 second limb is allocation. That is the first two, and the third area I want to ask you about is  
33 the transmission equipment costs.

34 A Okay.

1 Q If we could first of all deal with the last area, which is the transmission equipment costs, and  
2 I would like you, please, to be provided with the Draft Determination, which is in Bundle  
3 BT9, and if you can please go to p.127 of the Draft Determination. This Draft  
4 Determination was issued on 9<sup>th</sup> February 2012, by which time I think you had left BT, but  
5 were you still assisting BT in relation to their responses to these disputes? In February  
6 2012.

7 A So the draft ----

8 Q It has got 9<sup>th</sup> February 2012.

9 A Yes, I think I was. Yes.

10 Q So you were effectively performing a kind of consultancy function?

11 A Yes, that is right.

12 Q Were you essentially doing the same, wearing an Ernst & Young hat, as you were doing  
13 while you were at BT, as regards assisting Ofcom in resolving this dispute? Assisting BT in  
14 their dialogue with Ofcom?

15 A No, not directly. Some members of the team that I supervised effectively reviewed the  
16 Draft Determination.

17 Q You will recall from 12.60 to 12.66, here Ofcom is dealing with an issue which you  
18 described in your reports, which is Ofcom's desire to amend the timing mismatch between  
19 revenues and cost reporting in the RFS. You recall that, do you not?

20 A Yes, I do.

21 Q It is quite neatly summarised in terms very similar to your report at 12.60, which is that the  
22 revenues associated with this equipment are recognised in upfront connection charges but  
23 for accounting purposes the assets are capitalised. Ofcom had to come up with a way of  
24 dealing with that issue.

25 A Yes.

26 Q We see that at 12.60 we have the particular adjustment that Ofcom comes up with, but just  
27 looking immediately above that, at 12.65, if I may read that with you slowly:

28 "Consequently we have estimated that the cost of expensing the equipment in the P&L  
29 each year by apportioning BT's annual additions from the asset register on the same  
30 basis as depreciation and MCE in the RFS. We consider that this approach is a more  
31 appropriate basis on which to estimate the annual P&L expense".

32 You will see a footnote 318, if you go down the page, and the footnote refers to:

33 "BT's response of 28 March 2011 to follow up question 13 of 22 October section 191  
34 notice".

1 Do you recall that?

2 A I have not ----

3 Q Okay.

4 A I can see it here, yes.

5 Q You deal with some of these issues in your most recent statement, but what I have asked to  
6 be put together is a very short tab of documents which includes, in particular, this response  
7 of 28<sup>th</sup> March. I am going to hand this up to you. Some of this stuff is in the bundles and  
8 some of it is not, but for convenience I have just put it together in one tab.

9 A Yes.

10 Q I am not going to take you by any means to all of this but this is just really to refresh your  
11 memory. If I can take it in stages. So Ofcom needs to work out how ----

12 MR. READ: I wonder if my learned friend could just for me to get a copy?

13 MR. SAINI: Certainly.

14 THE PRESIDENT: Can we put this, for our purposes, in additional documents at Tab 33?

15 MR. SAINI: I am content with that, Sir, yes. So Ofcom needs to work out a way of making its  
16 adjustment and they ask various questions of BT in relation to how that adjustment can be  
17 made. If I can take you immediately, please, to p.43 of this little tab. This the email of 28<sup>th</sup>  
18 March 2011 sent by you to Mr. Causby of Ofcom, and I believe this is the response which is  
19 referred to in footnote 318, so please do take time to read it. The real issue I am interested  
20 in, Mr. Coulson, is on the second page, p.45. Ofcom have made a formal statutory request  
21 which is under question 13, and your response is in red, I hope. Do you see that?

22 A Hm mm.

23 Q What you have done is you have worked out for Ofcom, in the attached workbook,  
24 additions by service on the same date as depreciation and MCE in the RFS. Is that right?

25 A That is right, yes.

26 Q So would it be fair to say, Mr. Coulson, that the source of 12.66 in the Draft Determination,  
27 and the figures there have been redacted because they are confidential, was a response that  
28 you gave to BT -- I am sorry, that BT gave to Ofcom, you acting at that time for BT.

29 A Yes, that is correct.

30 Q Would you agree that it is perfectly clear, because you were the author of the figures, that  
31 the methodology that Ofcom wanted you to adopt was a methodology based on depreciation  
32 and MCE on the same basis as the RFS. Is that correct?

33 A Correct.

34 Q While we are in this bundle, and you will have left BT by this point, but if you could kind,

1 please, go to the back of the bundle, and I do not know if you knew about this, but at p.57,  
2 which is the last but one document ----

3 A I am sorry, which ----

4 Q Right at the end of this. It is in the loose pages, p.57.

5 A Yes.

6 Q This is on 9<sup>th</sup> February, which I believe is the same date as the Draft Determination.

7 A Yes.

8 Q There is an email sent by Paul Dean to Stuart Murray. Who was Stuart Murray?

9 A Stuart Murray is one of the lawyers at BT.

10 Q That includes an Ethernet model spreadsheet. Can I ask you, first of all, were you aware at  
11 the time, I know you are not copied in on this but you were at Ernst & Young by this stage,  
12 were you aware at the time that BT had been sent this model by Ofcom, at the time of the  
13 Draft Determination?

14 A The model attached to ----

15 Q Yes, there is an extensive model attached. I have essentially attached one page. Perhaps I  
16 can show you the page? If you can open it out. It is the very last spreadsheet, and if you  
17 look in the bottom left-hand corner, it says: "Provided by BT on 28<sup>th</sup> March 2011", and:  
18 "We asked BT to apportion the ... capital costs for services on the same basis as  
19 depreciation and MCE".

20 Do you see that? It is rather small, for which I apologise. Bottom left-hand corner, do you  
21 see that table and it has got some confidential figures?

22 A Yes.

23 Q So BT were using figures, were they not, for depreciation and a method of depreciation  
24 which you had provided to them on 28<sup>th</sup> March 2011?

25 THE PRESIDENT: That Ofcom were using.

26 MR. SAINI: I am sorry, Ofcom were using. A method which BT, acting by you, had provided on  
27 28<sup>th</sup> March 2011.

28 A Yes. I am sorry, I am just going to read the email.

29 Q Please take your time.

30 A Yes, thank you. (After a pause): Sorry, could you repeat the question?

31 Q BT, in the Draft Determination ----

32 THE PRESIDENT: Ofcom.

33 MR. SAINI: I am so sorry, Ofcom in the Draft Determination were using figures and a method  
34 which you had provided to them on 28<sup>th</sup> March 2011.

1 A Yes, to summarise, I think, so Ofcom had asked for the methodology using the RFS, which  
2 I provided, and I was not aware of ever seeing that so, as you said, I was not copied on it,  
3 but you say this is an extract from ----

4 Q It is an attachment to that email, you can take it from me.

5 A And it is an extract, it says here, from the model used.

6 Q Yes. The answer to my question is, if I can ask it again, if you would like me to?

7 A Please, yes.

8 Q Ofcom had used figures based on a model which BT had provided to Ofcom.

9 A I do not think BT provided a model. I think BT ----

10 Q A methodology, sorry.

11 A Well, I am not sure if they provided a methodology to resolve a dispute. What they  
12 provided was a series of numbers that were consistent with the RFS, which Ofcom then  
13 modelled in here, as far as I can tell, to make this adjustment.

14 Q So you are well aware that the basis for Ofcom's approach was the method used in the RFS?  
15 Is that fair to say?

16 A Clearly I was aware at the time that I provided the information, although I do not think I  
17 specifically pulled the information together myself, but clearly I was aware when I sent the  
18 email. But if you were to ask me was I aware subsequently, particularly after I had left BT,  
19 absolutely not and this is a vastly complicated model with lots of adjustments in it and lots  
20 and lots of data, and I do not think it would have -- Well, I certainly was not aware  
21 afterwards, particularly before the provisional or even after the provisional determination  
22 had come out, probably was not aware exactly, or had not remembered exactly, that these  
23 numbers were being used in that way.

24 Q But you knew how the RFS methodology works, did you not?

25 A I would have known when I provided the information, but I doubt whether it would have  
26 recalled it when the provisional determination came out.

27 Q If I can just, please, ask you to go within that loose tab to p.29? I just need to clear this up  
28 because it is a matter of dispute between Ofcom and BT, given the way that Mr. Read  
29 opened the case. If you go to p.29 there is an email again from you of 11<sup>th</sup> February 2011 to  
30 Mr. Causby of Ofcom, and you provide a response to various questions, and what I am  
31 interested in is p.31, which is your actual response but with a particular figure you see. Do  
32 you see that?

33 A Yes.

34 Q I am sorry, and some particular diagrams.

1 A Yes, I can see that.

2 Q There you have described the way in which, underneath those figures, the allocation of  
3 MCE and depreciation charges is undertaken in regulatory financial statements.

4 A Right, so I was a pretty senior member of the BT team, which I think we have already  
5 discussed. By this time I was working primarily with the Openreach business as opposed on  
6 the costing team side, and one of my key responsibilities was to respond to Ofcom's  
7 information requests. So, if you like, I was the conduit through which this information was  
8 flowing to Mr. Causby. So I sent emails in response to Mr. Causby's questions and I  
9 reviewed the data that I was given. The data was prepared by people who were in one of  
10 my sister teams, if you like, within the regulatory finance team, which was the costing.

11 Q My point, Mr. Coulson, is that there could have been no doubt in the mind of BT that  
12 Ofcom had used the same methodology as used by BT in its RFS?

13 A Yes, I think that probably another relevant factor is in the Provisional Determination quite  
14 rightly it says that the methodology used was consistent with the RFS. My memory of the  
15 Provisional Determination when I read it and subsequently is that the key reason it gives for  
16 explaining why it rejected BT's suggested methodology of using connection volumes and  
17 adopting instead something that was consistent with the RFS was that BT's methodology  
18 failed to take into account the unit cost differentials between different pieces of equipment.  
19 That comes through very loud and clear from the Draft Determination. What doesn't come  
20 through clearly is that the difference between the two methodologies is one uses rental  
21 volumes as opposed to connection volumes.

22 Q I understand that, Mr. Coulson. I am not, at the moment, debating with you which is the  
23 better methodology; I am just trying to deal with the factual issue, because it is said by BT,  
24 through Mr. Read, that despite the clarity (in our submission) of the Provisional  
25 Determination, BT was somehow left in the dark as to the particular methodology that  
26 Ofcom had adopted as regards these costs. As I understand your answer, BT was aware of  
27 the methodology, but you have a different complaint which is that there is actually a better  
28 methodology. Is that fair to say?

29 A My previous answer was relevant, because if Mr. Read had said that BT was in the dark, I  
30 think that is consistent with what I have just said, which is on reading the Provisional  
31 Determination it isn't obvious to the general reader at BT that what Ofcom have done is  
32 moved to a methodology that uses rental volumes. It's obvious that they have moved to a  
33 methodology to address the weighting of equipment issue differential, differential issue. It  
34 isn't obvious that they have moved to a methodology that relies on rental volumes. There's



1 a reference to the DAM, I think, or there might well be a logical thing might have been to  
2 have gone to the DAM if you didn't understand it, but it isn't particularly easy to find out  
3 how BT did this. You say, of course, that BT provided the data in the first place, but what  
4 I'm saying to you is there are experts within BT that would have understood this within the  
5 costing team, but by no means would every allocation in BT's regulatory accounts be  
6 forefront, front of everybody's mind, particularly the more senior people reviewing this data.

7 Q But with respect, Mr. Coulson, it is not all complicated. Look at the very page you have got  
8 open there, back at p.31 of that loose sheet. If I may ask you, this is your communication; it  
9 is not someone else's communication, this is your communication with Ofcom and you say,  
10 after the first paragraph which beings "The allocation of ...", please look at the second  
11 paragraph if I may read it: "The first step involves the allocation from COWs in ... to the  
12 high level sections: WES, BES and ..." It carries on saying:

13 "The allocation is performed on the basis of rental volumes times electronic costs.  
14 Rental volumes are used as a depreciation charge related to previous years'  
15 connection volumes and not just in-year volumes representing the RFS."

16 So what Ofcom did is that they used rental just as you have described it. They used rental  
17 volumes, did they not?

18 A That's correct, they used rental volumes, yes.

19 Q It is rental volumes in part, is it not?

20 A It's rental volumes in part, but it's rental volumes first.

21 Q Can I ask you to put that bundle away and clear your desk and now take out bundle B. I  
22 want to turn to .. provisioning costs. I want to consider the first limb of provisioning costs,  
23 which is the level of provisioning costs. If you can go to p.309, please, para.13.357. Could  
24 you read 13.357, please, to refresh your memory. (Pause to read) Tell me when you have  
25 finished it, please.

26 A Yes.

27 Q You will see that Ofcom there are saying that BT may well have a point, that it is possible  
28 that the provisioning cost component in 2006 and 2007 did not capture provisioning costs  
29 associated with Ethernet service, but they are saying that the evidence that they have does  
30 not allow them to reach a conclusion on this point. Do you understand that, do you not?

31 That is what they are saying there?

32 A Yes, I do.

33 Q Would it be fair to say that in your report, and in particular in your last report, the fourth  
34 report which was produced earlier this week, you have now provided further information

1 which explains where those provisioning costs happen to have been allocated?

2 A Yes, it certainly explains why the numbers in 2006/7 and 2007/8 appear to be much lower.

3 Q I think we are agreed on that. Is there any reason that you are aware of, given your intimate  
4 involvement in this dispute and the Determination process, why BT was not able at the time  
5 of the Provisional Determination to supply this evidence?

6 A My understanding was that actually BT had provided some information on this during the  
7 administrative phase. I think it's referred to in the September letter.

8 Q Have you not provided a lot more information, in particular you have provided information  
9 off the ... what is called the Aspire system?

10 A That's right.

11 Q What is the Aspire system?

12 A The Aspire system is the costing system which BT uses to generate the RFS.

13 Q So the material that you have now provided in your reports was always available to BT if  
14 someone had looked, is that correct?

15 A I wasn't involved in the creation of the September letter, but I imagine that the numbers that  
16 were provided, which were quite specific, would therefore have come from the Aspire  
17 system.

18 Q So you have no reason to believe that this information was not always available?

19 A I'm not sure to what extent it was available, but as I say, in the September letter, which was  
20 prior to the Final Determination, BT had clearly raised the issue that they thought the  
21 provisioning costs in 2006/7 and 2007/8 were low for Ethernet services.

22 Q And you would accept Ofcom were asking for some further evidence, were they not? They  
23 obviously were asking for evidence, but they concluded the evidence available did not  
24 enable them to reach a conclusion?

25 A Actually, at 13.358 just enough it says: "Therefore we do not consider that BT has provided  
26 us with sufficient evidence". I don't know to what extent Ofcom had asked BT to follow up  
27 after the September letter, but I think all I did really, when I started this exercise, was take  
28 the September letter (which was available to Ofcom), I reviewed it, I considered which  
29 pieces of information needed further explanation, and I asked BT to provide Aspire  
30 downloads to provide that information to me. It actually wasn't a very difficult job for BT  
31 to provide that.

32 Q Thank you, that is very clear. Can I ask you please to put that bundle away and go back to  
33 your fourth report which is at the back of bundle D in divider 18. This is the report you  
34 prepared earlier this week to deal with various points that we had made, Ofcom had made,

1 in oral opening and in skeleton arguments. One of the points you will be aware of – if you  
2 go to the body of your report please, p.6 of your fourth report. You very helpfully quote at  
3 p.6 para.3.3 parts of our skeleton argument.

4 A Yes.

5 Q You see at 3.3D we have raised the issue that it was unclear on the basis of your evidence  
6 whether the products where costs had been previously allocated had been the subject of  
7 previous regulatory decisions. You see that?

8 A Yes, I see that.

9 Q If one looks at appendix B of your report, p.14, could you just describe for me as a lay  
10 person, there are a lot of abbreviations on this, what this table is showing?

11 A Yes, so what this table shows is the allocation of two OUCs as BT calls them.

12 Q What are OUCs?

13 A Effectively organisation codes. So these are codes which are set up in order to capture  
14 specific types of costs within a business. In this case, these organisation codes capture two  
15 types of cost: service provisioning cost and service assurance cost. They capture them  
16 together, which is why we have to consider service assurance costs at the same time. So  
17 those two organisation codes are then in turn ultimately allocated through to services that  
18 BT provides. So where it says "product", that column refers to a product or a service code  
19 and the description is the description of that service. So in effect, what we have here is a  
20 view of how all of the service provisioning and service assurance costs were allocated to  
21 each of BT's services ... and then I think the tables are for other years.

22 Q To help me and the Tribunal, I am going to give you a very simple example to see if I can  
23 understand what is going on here. Let us take the first item, which is SL141 wholesale  
24 PSTN transfers. That is a product, is it?

25 A That's a product that sits within a different market.

26 Q So what happened is that you have discovered, for the purposes of the fourth report – you  
27 have done some investigations and you have discovered that some of the costs that should  
28 be allocated to Ethernet have been allocated to that service, is that right?

29 A That's what it appears, yes.

30 Q Do you know whether or not that is a regulated service? In other words, is it subject to  
31 charge control?

32 A Well, I don't know for sure, but I would imagine the fact that it's got PSTN, which relates to  
33 BT's copper services, that is part of the wholesale analogue services, which is a regulated  
34 market for provision of local access lines, copper access lines.

1 Q So there may well be a price control covering that particular product, would that be fair to  
2 say?

3 A Yes, absolutely.

4 Q So would it not be rather dangerous, Mr. Coulson, to allow BT to shift these costs over from  
5 this price controlled service into Ethernet, because when the price control for that particular  
6 service was being set, costs of that service would have been taken into account, would they?

7 A Well, what I have done here is identified an error. I think when errors are found, it is  
8 important to identify them and understand them. There is then a question about how you  
9 deal with that in the context of historic charge controls, which I have not considered, to be  
10 honest. But what I would say is that whilst the absolute amount of cost that belongs to  
11 another market doesn't change, clearly if you move £2 million from Ethernet and put £2  
12 million into copper access lines it is £2 million. But from a unit cost perspective I suppose  
13 it's important to remember that there are thousands of Ethernet services, and probably  
14 something like 25 million copper lines in the UK. So the absolute amount would be the  
15 same, but the unit cost would be much less significant in any of the copper access services  
16 than it would have appeared in the Ethernet.

17 Q I think you are making a quantitative point there, Mr. Coulson. I am not making a  
18 quantitative point; I just want to know whether or not you agree with me that if one allows  
19 costs from one price controlled service such as the first one, wholesale PSTN, to be shifted  
20 into Ethernet there could be an adverse impact as regards a regulatory decision that was  
21 made when the price control or PSTN was set?

22 A I don't really know what you mean by adverse impact.

23 Q It is very simple: that the price control for wholesale PSTN would have been configured on  
24 the basis that the costs of wholesale PSTN are X, and what you are doing now is that you  
25 are moving those costs over to Ethernet.

26 A As I said, I think you would need to consider the materiality of the market you are moving  
27 the costs from relative to the market you are moving it into. It would depend ----

28 Q So you would agree with me that, had you provided this information to Ofcom, during the  
29 administrative phase, these are all factors that Ofcom could have considered?

30 A Yes, that's right.

31 Q Can I ask you to go to the last issue, which is if you have open, please, bundle B in front of  
32 you, which was the Determination, which is the provisioning costs section. As I mentioned  
33 to you there are two issues on provisioning costs, there is the total provisioning costs issue,  
34 which we have just been looking at, and there is a separate point concerning allocation

1 provisioning costs just for the year 2008 and 2009?

2 A Yes.

3 Q You recall that?

4 A Yes.

5 Q If you could please go to p.309 and if you can read 13.359 and refresh your memory?

6 A (After a pause): Yes.

7 Q If I can stop you after the first two sentences of 13.359, as I understand the dispute appears  
8 to be that in the RFS £8.9 million of provisioning costs were allocated to rental, and  
9 essentially BT were saying that is an error, these should be allocated to connections. Is that  
10 essentially the nub of the dispute?

11 A Yes, that's right.

12 Q At 13.361 over the page Ofcom makes the point that first of all the decision as to how to  
13 allocate the costs each year was made by BT. That is clearly right, is it not - how to allocate  
14 in the RFS?

15 A Yes.

16 Q And they are making the point that it is not necessarily wrong to have allocated them for  
17 particular years under rentals and for other years under connections, that is their other point,  
18 is it not?

19 A Yes.

20 Q Would you agree with me that there must have been a good reason for BT in 2008 and 2009  
21 to allocate these costs to rental?

22 A No, I wouldn't agree. I cannot think of any good reason why they would have done that. In  
23 fact, all the evidence that I have seen suggests that this is something of an aberration and I  
24 can only assume that it was just an error that wasn't picked up at the time.

25 Q So you are saying it was an unreasoned decision by BT so far as you are aware, that  
26 someone just by accident allocated in that year these particular costs to rentals rather than  
27 connections?

28 A That is certainly what it looks like. My understanding had always been, and is, that these  
29 costs relate much more closely to connections rather than rentals. They are, by definition  
30 costs which are involved in the setting up of the new customer, which happen at the time  
31 that the connection is ordered, so it seems to me, as you say, this would have been an error  
32 that just wasn't spotted.

33 Q If you look at 13.363, please, on this same page, 310. Ofcom there observes:  
34 "We note that even if we had found that the evidence suggested that the

1 methodology for allocating the provisioning cost component in 2008/09 was  
2 obviously inappropriate or the allocation was in error, we would need to take into  
3 account the fact that BT allocated a large part of the cost to WLR products which  
4 were subject to regulatory decisions, such as the setting of charge controls.

5 What is your understanding of the point that Ofcom are making there?

6 A I think it is the same point that we were talking about earlier which is, by definition - I think  
7 Openreach is dominated by copper services, so any time you are moving costs around the  
8 chances are you are going to be affecting the copper services, which is referred to here as  
9 WLR. So Ofcom are simply making the point that we would need to take into account that  
10 if we move some costs from Ethernet there might be an implication for WLR.

11 Q So the same as the implication we discussed earlier in these provisioning costs, which is that  
12 regulatory decisions made for other charge controlled services may have been based on  
13 particular allocations which are now being changed. Would that be a fair summary?

14 A That would, and I think clearly what Ofcom would have needed to have done, when it  
15 looked at all of its adjustments, was to understand the potential impacts for making those  
16 adjustments and the impact of that on other regulated markets or other services that BT sold,  
17 although I don't think they made the same judgment when it came to 21CN products,  
18 because I think they made those adjustments and made no offsetting adjustment in any other  
19 part of BT's RFS. I think the other adjustments were all contained within Ethernet so they  
20 probably did not need to.

21 MR. SAINI: Thank you very much, Mr. Coulson.

22 Cross-examined by Mr. PICKFORD

23 Q Good afternoon, Mr. Coulson.

24 A Good afternoon.

25 Q It is correct, is it not, that BT reported FAC information for the purposes of its cost  
26 orientation compliance?

27 A That's my understanding, yes.

28 Q And that FAC information was audited?

29 A Yes, that's right.

30 Q Do you know whether BT used that information to help inform whether it was complying  
31 with its cost orientation obligation?

32 A I don't, no.

33 Q From what you said before I think it is fair to say, is it not, that BT approached its cost  
34 orientation obligation on an aggregated basis across a number of services?

1 A Yes, that's right.

2 Q An organisation prepares its management accounts with sufficient frequency to be able to  
3 supply it with the information that it needs to run its business properly, does it not?

4 A Yes.

5 Q I am not suggesting that this is the case from BT, but are you aware from your experience as  
6 a professional accountant that there are a few rare organisations, for example, some  
7 investment banks and very big retail organisations for whom up to date financial  
8 information is so important that they would compile their management accounts on a daily  
9 basis?

10 A I'm not aware of that, no.

11 Q BT obviously would be expected to prepare its management accounts with sufficient  
12 frequency to ensure that it had the information to comply with its various obligations,  
13 including its cost orientation obligations. That is right, is it not?

14 A Yes, BT produces the regulatory financial statements which are separate from its statutory  
15 financial statements in order to do that.

16 Q How frequently did BT compile its management accounts during the period in which you  
17 were in charge?

18 A I was not involved in the management accounting process at all. Could you explain,  
19 perhaps - are you drawing a distinction between statutory and management accounts?

20 Q Yes, I am asking about the management accounts for the purposes of running the business.  
21 It was on a monthly basis, was it not?

22 A That would've been on a monthly basis, yes.

23 Q And do you know whether they were compiled on a fully allocated cost basis?

24 A I do know that, and they were not.

25 Q Did they contain DSAC information?

26 A They did not.

27 Q Given that a cost orientation obligation requires prices to be set in a certain way relative to  
28 costs, you would expect any well managed organisation to ensure that there were systems in  
29 place to ensure liaison between its costing teams and its pricing teams and its compliance  
30 functions, would you not?

31 A I think it would depend obviously on what importance and what understanding of the  
32 regulations and the intent of the regulator was in order for it to make those assessments and  
33 put those controls in place.

34 MR. PICKFORD: Thank you, I have no further questions.

Re-examined by Mr. READ

1  
2 Q Mr. Coulson, you were asked about the question of BES 100 and taken the example, and the  
3 reporting levels, you were taken specifically to I think it was table 13.27 in the original  
4 Decision?

5 A Yes.

6 Q Can I ask you to take bundle B and turn to para. 9.221?

7 A Yes.

8 Q You see there that it says in terms:

9 "These are factors we considered in our Provisional Conclusions. For the purposes  
10 of resolving these Disputes we do not consider average charges compared to  
11 average DSAC across the whole period, as we suggested might be relevant in the  
12 2009 PPC Determinations. We believe our approach is appropriate given the  
13 importance placed by the CAT on the DSAC test and its findings in relation to  
14 treating charges above DSAC as 'intrinsically excessive'.

15 Going back to the date of that table, which I think was looking at 2006/2007, was that your  
16 understanding of how any test of cost orientation would be applied?

17 A I am sorry, when you say "was that"?

18 Q I am asking you to look at 9.221 where Ofcom set out quite clearly that they are not going to  
19 average over a period and they are going to regard treating charges above DSAC as  
20 intrinsically excessive?

21 A Yes.

22 Q What I am asking you is to put yourself back into what the position was in 2006/2007 when  
23 you were asked about the particular figures in those tables, and was that your understanding  
24 at the time as to how cost orientation would be approached?

25 A Yes. Certainly, at the time I considered that a level of aggregation would have been  
26 necessary in order to test cost orientation that would have been both across services and  
27 across years, and I think I mentioned earlier one of the reasons for that would have been  
28 when you have an extremely complicated cost allocation model with ever increasing  
29 requirements to go to ever increasing levels of detail clearly the lower the level of detail the  
30 less reliable the results become, and one way that you deal with that is aggregation.

31 Q So to return to the specific question I asked you, what is set out there in 9.221 was that your  
32 understanding in 2006 as the test that would be applied?

33 A Well, my understanding would have been that there would have been aggregation.

34 Q You were asked questions about pricing function and who would have known what. Can I



1 ask you to take BT16 and go to tab 5. This is a pricing paper OPAG 41/2006, do you see  
2 that?

3 A Yes.

4 Q Are you familiar with how BT was setting out its pricing papers?

5 A Not terribly, I am familiar that they have pricing papers, and they had a pricing group that  
6 reviewed them.

7 Q Can I ask you to go to p.10?

8 A Yes.

9 Q And I would ask you to look at the box half way down, where it says:  
10 "The following team members support the proposal and agree the proposal should  
11 move forward to OPG".

12 A Yes.

13 Q It has "Product Line, Product Finance, Regulatory Affairs, Openreach Pricing, Legal  
14 Business Services, Product/Cross Portfolio, Customer Services Operations." To what extent  
15 does this reflect your understanding at the time of how decisions would be taken in BT  
16 about specific prices?

17 A I recognise all of the functional areas. It represents the people that in my view had the  
18 responsibility for signing off pricing changes. I've never seen this before actually and I  
19 guess what is striking is there's no one from regulatory finance in there.

20 Q What about ----

21 THE PRESIDENT: Someone from regulatory affairs?

22 MR. READ: Yes.

23 A Yes, which would have been a separate function.

24 THE PRESIDENT: What is the distinction?

25 A Regulatory affairs are, within BT, typically the function that deals with regulatory policy.  
26 They don't have any responsibility for producing regulatory financial information.

27 MR. HARRISON: Can you give me an example of the type of policy things that they would  
28 decide upon?

29 A They would be discussing with Ofcom, for example, how Ofcom would be approaching a  
30 charge control, how Ofcom was going to manage the price control. They would largely be  
31 staffed with economists and they would be dealing with economics issues and talking to  
32 Ofcom about the way in which the market was defined, for example, and the implications of  
33 that.

34 THE PRESIDENT: Just before you leave that, when it says above that list, "The following team

1 members support proposal, agree with proposal, should move forward to OPG". OPG is  
2 what?

3 A I think that stands for Openreach Pricing Group, which I think is a collection of senior  
4 managers from Openreach who would ultimately sign the pricing paper off.

5 MR. READ: You were asked a question about how important it is that the RFS should not be  
6 changed, and you said, yes, it is important that the RFS are accurate. Can I ask you what  
7 happens when an error is discovered in the RFS?

8 A Well, typically what happens is that an investigation would be launched to understand  
9 whether, in fact, it is an error. Quite often, these things are not exactly clear cut. Once it  
10 would have been established that it was clear cut and that it was an error there would have  
11 been a team of people assigned to fixing it. Part of the process possibly would have  
12 included talking to PWC, the auditors, and if it was big enough discussing it with Ofcom.

13 Q What is overall aim that BT would be trying to achieve in going through that process?

14 A Well, you know, to make the accounts as accurate as possible.

15 Q In a situation where an error is discovered, how important or otherwise is it for the RFS to  
16 be restated?

17 A It's really important, especially if it's a material change, because clearly one of the key  
18 measures in the RFS is the year over year change between services, and I think you could  
19 ultimately, or potentially, having a misleading view if you were not to re-state the prior  
20 year.

21 Q Can I ask you to take bundle B9 again, and go to tab 19, which is the draft Determination,  
22 and you were taken, I think, to para.12.60, p.127, and I want to be clear about the sequence  
23 of what is going on in these paragraphs. Can you, first of all, from those paragraphs,  
24 describe what it was that BT was seeking to achieve?

25 A Do you mean what BT was seeking to achieve prior to the adjustment?

26 Q It says in terms at 12.62:

27 "For each year we [Ofcom] have removed the depreciation and asset charges and  
28 replaced them with an estimate of the cost of expensing the equipment in the P&L  
29 in the year of purchase."

30 A Yes.

31 Q Then 12.63:

32 ". In addition BT provided an estimate of the cost of expensing the transmission  
33 equipment in the P&L each year. It did this by taking the annual additions from  
34 the asset register and apportioning them between services based on the volume of

1 connections in each year."

2 Can you explain what BT was seeking to achieve?

3 A Yes, what BT was seeking to achieve in responding to Ofcom's issue that it had raised was  
4 to address the mismatch between the revenue that was recognised upfront and the costs that  
5 were recognised over several years. Obviously Ofcom and BT had discussed the fact that  
6 the way to do this was to remove the depreciation in the MCE cost from the service and  
7 instead replace it with the capital cost, and that way you could effectively match the cost of  
8 the equipment, revenue and cost in the same year.

9 Q Just so we are clear, this provisional Determination here post-dates the email that you were  
10 taken to earlier of 11<sup>th</sup> February 2011?

11 A Yes.

12 Q When BT had responded in the 11<sup>th</sup> February 2011 email, was it trying in any way to  
13 indicate what is set out in 12.63 there?

14 A Well, yes, I think what BT was trying to do was to provide Ofcom with the capital costs that  
15 would need to be replaced and put back so that the matching could be achieved.

16 Q We can see from para.12.64 that Ofcom reject that?

17 A Yes.

18 Q Then, and in that context, they then make the statement in 12.65 about how they are going  
19 to apportion them?

20 A Yes.

21 Q When you were being asked to look at the 11<sup>th</sup> February 2011 emails, what was the basis  
22 upon which the material set out in the annex being put forward? Do you want to have a  
23 look at it again. I think p.29 of that little bundle is the relevant email, and then p.31, if I  
24 have understood it correctly, is one of the attachments?

25 A Yes.

26 Q What I am trying to understand from this, given the sequences that we have just out, is was  
27 this answer in the context of what is said in para.12.63 of the provisional Determination,  
28 namely an apportionment involving the volume of connections in each year?

29 A Well, I think the chronology was that here in the draft Determination BT had provided the  
30 equipment split based on connections. Ofcom then came back and, as you say, rejected that.  
31 Ofcom then came back and asked BT to provide the proportion of depreciation in MCE. So  
32 clearly the question they asked then was on a different basis.

33 Q Thank you. Can I then ask you to go to annex B of your fourth report, which is at p.14, tab  
34 19 of bundle D, and you were asked specifically I think about the PSTN business

1 connections charge?

2 A Yes.

3 Q I think your answer was that that was probably effectively price capped?

4 A Yes, I think so.

5 Q The question that I would want to ask is: how significant or otherwise would the transfer of  
6 costs from the PSTN business connections elements to Ethernet be in your view?

7 A They wouldn't have been very significant. I don't know exactly, but, broadly speaking, the  
8 amount of cost collectively in the various copper based price controlled markets is  
9 something in the region of £3 to £4 billion, so clearly ----

10 Q £3 to £4 billion did you say?

11 A I said billion, yes.

12 Q Sorry, you were going to add something and I interrupted you?

13 A No, I was going to say, clearly, in the context of £3 to £4 billion, none of the amounts  
14 shown on here were particularly material.

15 Q I think you were, in your first report, if we can just go back to it, tab 14 of bundle D, if we  
16 turn to section 3, which is where you deal with it, and if we go to para.3.46, you say in  
17 terms there, and this is in response to the one specific matter that Ofcom had raised in its  
18 Decision, that:

19 "In any event, such Ethernet provisioning costs that were wrongly allocated to (and  
20 therefore spread across) other Ethernet Openreach products are unlikely to have  
21 had a significant impact on WLR products."

22 We know, in fact, from your subsequent report that the figure would be about £8 million - in  
23 fact, it was originally, I think, with BT's September 2012 letter that the spread would be a  
24 sum of £8 million, I think it would be, that would be removed from the WLR market.

25 A Yes.

26 Q How significant would a figure like that be in the context of those types of products?

27 A Well, in the context of the WLR market, it would have been clearly in excess of £1 billion,  
28 maybe £2 billion, I'm not sure exactly, but we were talking about billions as opposed to  
29 millions.

30 Q Can you think of any area from which provisioning costs might have been sucked away  
31 from in order to go on this adjustment into the Ethernet product, any other area where the  
32 effect might be significant?

33 A No. I think, from my third report, I ordered the impacts in terms of size, and I think all of  
34 the major impacts were on the major copper products. So WLR and LLU, and, as I said,

1 combined, those represented several billion pounds worth of cost. As I said earlier as well,  
2 Openreach products, regulated products, aren't dominated by the copper services. That's by  
3 far and away the largest part of the business.

4 Q So your assessment as to the significance of that transfer would be what?

5 A It would be insignificant.

6 MR. READ: Thank you, Mr. Coulson. Do you have any further questions, Sir?

7 MR. HARRISON: Just on that table, you were asked about p.328 of the Determination, Bundle  
8 B, p.328 of Bundle B.

9 A Of the Draft Determination.

10 Q No, not of the Draft Determination, of the Final Determination.

11 A Yes.

12 Q In response to Mr. Saini, who brought your attention to one product, if you aggregate all  
13 those products with BES and WES then in the first year external revenues exceed DSAC by  
14 31 million and FAC in the first year by 32 million. Now, you explained that at that point in  
15 time DSAC had dropped in significance because it had dropped out of the audit net,  
16 therefore you did not think it was of great concern. Is my understanding of that correct?

17 A Yes. Just to clarify, by the time I had joined BT it did not have much significance so I do  
18 not know. So using the word "dropped", that sounds plausible. I do not know whether it  
19 ever did, to be honest, but certainly by the time I got there it did not.

20 Q In the second year a similar problem arises and the size of numbers in the following year are  
21 of the order of 38 million exceeding DSAC and 52 million exceeding FAC. I am just trying  
22 to understand, would that not have been an alarm bell? This was the second year running  
23 this had occurred. Given the job of the regulatory finance side, and my understanding when  
24 Mr. Dolling gave his evidence was, "Hey, this is what your job was, to look at this", at that  
25 point in time would there not have been a sort of realisation that you could have  
26 overcharged and that a repayment would be due?

27 A I think there are probably two relevant considerations there. The first one is, I do not think  
28 that two years necessarily would have triggered those alarm bells that you refer to. The  
29 reason I say that is because I was aware at the same time of broadband market, which was  
30 also reported in the RFS, and I was aware that the broadband returns had been relatively  
31 high for at least two years, maybe more than two years. There was a general acceptance  
32 across the business that whilst this may look as though BT were making excess returns in  
33 those years, that BT had suffered losses prior to the beginning of the reporting obligations  
34 and when it had begun to provide the service, so there was an upfront investment which was

1 made prior to reporting. Reporting came along and the reporting happened to come along at  
2 the time that the returns were growing. That is not a coincidence. That is because at that  
3 time the broadband market was beginning to mature and typically when the market goes  
4 above a certain threshold in terms of its size of revenue Ofcom would ask BT to start  
5 reporting it. So in that context there were other benchmarks, if you like, to say that,  
6 "Actually you probably need to wait. This is a ... service. It is growing quite rapidly. We  
7 probably need to wait and see exactly how many more years of it it is going to go on before  
8 we start being concerned".

9 THE PRESIDENT: Did you have a cost orientation obligation in the broadband as well, can you  
10 remember?

11 A There was not a cost orientation obligation as far as I remember. There was a reporting  
12 obligation so that the numbers appeared in the RFS, and there was not a cost orientation.

13 MR. HARRISON: In the course of the last few days we have seen a letter that went in from Sky,  
14 I think it is, in January 2008, which I guess was having received the 2006/7 RFSs.

15 A Yes.

16 Q It came in and they basically said, "Looking at this, this looks wrong".

17 A Yes.

18 Q Would that type of query sort of hit your desk when that came in?

19 A No. I am sorry, the second thing I was going to say was that the regulatory finance team's  
20 primary function at the time that I was there was to keep score. It was to provide the  
21 financial information and, frankly, that is a very large and complicated job. The  
22 information that it produced would have been acted on by a whole variety of people, not just  
23 people within the senior leadership team of the regulatory reporting team. So those sorts of  
24 questions would not have come across my desk.

25 Q Logically would not have someone have come back to you and said, "Have you got the  
26 score right?"?

27 A Yes, that is possible. It is possible that someone could have come back and said, "What is  
28 the reason", or "Have you got it right and, if you have, what is the reason for this and is this  
29 going to be the same next year?"

30 Q Right, and you cannot recollect in this particular instance whether that actually occurred or  
31 not?

32 A No, I do not remember that letter that you were talking about.

33 Q Okay, fine. If I can, Mr. Harman yesterday on his report, which is in Bundle D. It was his  
34 first report. Which one was that?

1 THE PRESIDENT: Tab 6.

2 MR. HARRISON: Tab 6. If you go into Tab 6, I asked the question of Mr. Harman and he  
3 basically said that the figures, I think, came from you, when I asked him the question. If  
4 you turn to p.22 in Tab 6 of Bundle D.

5 THE PRESIDENT: The bundle in which your report is.

6 A Yes, what I have got is my report with the figures that I provided to him, which I think is  
7 the same.

8 MR. HARRISON: Yes. If you look at Table 2.1, and also then if you jump to p.7, you can see  
9 the actual figures that were reported on. It might help if you take p.7 out just to compare it  
10 with p.22, so you can just see the relativity of the two figures.

11 A Okay, yes. Yes, I have got p.7.

12 Q If you look at p.7 you can see in the "total" column the amounts per year and you can  
13 compare it with the ones in Table 2.1.

14 A I am sorry, can you tell me where Table 2.1 is?

15 Q Page 22.

16 A Yes.

17 Q When you look at the tables, in the early years the figures are very close.

18 A Yes.

19 Q Because both of them were over, if I can simplify it, DSAC and therefore aggregation was  
20 not going to make a difference.

21 A When you say "both of them", you mean rentals and connection?

22 Q BES and WES.

23 A Oh, BES and WES. Okay.

24 Q If you then go down, the big change occurs in 2008/2009 and again there is quite a  
25 substantial change in 2009/2010.

26 A Yes.

27 Q What were the drivers for that change? What caused that drop?

28 A Yes, so, from memory, WES rentals and BES rentals - I will generalise a bit here, if you  
29 bear with me - but WES and BES rentals more or less are over the DSAC throughout most  
30 of the appealed period up until about '10/11 when pretty much everything becomes  
31 compliant. So what you have got is rentals being non-compliant over all of that period, but  
32 what was happening is that connections were changing so, in particular, by I think '08/09  
33 BES connections had become compliant, I think as a result of price reductions, and when  
34 they became compliant they became very compliant in the sense that they went a fair bit

1 below the DSAC. In Mr. Harman's methodology he combines rentals and connections, so  
2 what we are seeing here is the effect of the BES connection being well below DSAC.

3 Q So the principal cause of it is price changes, not reallocation of costs?

4 A That is right. I think the only point at which the reallocation of costs becomes relevant is  
5 '10/11 when the electronics cost was moved by BT from ----

6 Q And in that year his methodology difference is quite small?

7 A Exactly.

8 Q Fine. Again, just to help my arithmetic, in the first year at '06/07 we can see actually his  
9 methodology is higher than Ofcom's. Just arithmetically, what would have caused that?

10 A The way the maths works is that Ofcom's method for creating the split by CPs was to first  
11 look at the amount of difference between DSAC and revenue for each service individually,  
12 so let's say connections and rentals separately, and then to split those amounts of excess  
13 between the CPs using the pro rata of the revenue for that particular service.

14 Q Oh, I see.

15 A My methodology combines rentals and connections and therefore performs the split using a  
16 combined pro rata, so effectively what you are seeing is slight differences in the mix  
17 between services.

18 Q I see, between CPs?

19 A Yes, between CPs.

20 Q Okay, fine. Thank you.

21 A The offset would have been other CPs that are not in this table.

22 MR. HARRISON: That is fine. Thank you very much.

23 THE PRESIDENT: We have no further questions. Thank you very much, Mr. Coulson. You can  
24 be released.

25 (The witness withdrew)

26 MR. PICKFORD: Sir, I believe the last witness for this afternoon is Mr. Robinson and I call Mr.  
27 Robinson, please.

28 Mr. THOMAS MARK ROBINSON, Affirmed

29 Examined by Mr. PICKFORD

30 MR. PICKFORD: Mr. Robinson, could you be provided, please, with Core Bundle D, and if you  
31 turn, please, to Tab 17. Do you have a document there entitled "Amended first expert report  
32 of Thomas Mark Robinson"?

33 A Yes, I do.

34 Q If you could turn, please, to p.45, is that your signature?



1 A It is.

2 Q Do you have any amendments you wish to make to this report?

3 A I believe there was a letter submitted to the Tribunal earlier this week relating to a couple of  
4 transcription errors in my calculations and it amended those errors.

5 Q I believe the letter that is being referred to, Sir, you should now have it in AD2 Tab 32.

6 THE PRESIDENT: Yes.

7 MR. PICKFORD: Perhaps if the witness could be provided with that, please?

8 A Yes.

9 Q Is this the letter that you are referring to?

10 A Yes, it is.

11 Q Subject to ----

12 THE PRESIDENT: Can you just help me on that, because I was not quite clear, Mr. Robinson?  
13 You go in your first report, on p.9, to Table 3.

14 A Yes.

15 Q And I understand, if you keep that letter, as it were, next to it, that the figure in table 3, the  
16 "total overcharge", you are amending from 233.5 to 232?

17 A Yes, that is correct.

18 Q That follows through, obviously into para.2.8. Then in the letter at point 3: "Aggregate  
19 FAC based overcharge including RAV adjustment in the dispute period", that corresponds,  
20 does it not, to your table 5?

21 A No, it does correspond to that table 5, but it's actually an amendment to the final table in the  
22 joint experts' report between myself and Mr. Coulson.

23 Q The total we have in table 5 of 240.5, should that be £233.9?

24 A £233.9 is the latest figure of a FAC based overcharge including RAV adjustment, yes.

25 Q So we amend that £240.5 to £233.9?

26 A There are methodological changes between table 5 in my amended first and the £233.9 in  
27 the letter, but the £233.9 does represent my latest figure for a FAC based overcharge  
28 including a RAV adjustment.

29 Q It has already been amended, as it were, once?

30 A It's been amended once, and subject to part of the joint statement between myself and Mr.  
31 Coulson, and then a further amendment based on the transcription error which is described  
32 in the letter.

33 Q Sorry, I think you have explained the £233.9 is now the figure we put in instead of £240.5?

34 A Yes.

1 Q That feeds through into some of the other tables later in the report?

2 A Indeed, yes.

3 Q Yes, thank you.

4 MR. PICKFORD: Thank you. Subject to the amendments that you just discussed with the  
5 President, do you adopt this witness statement to be your evidence in these proceedings?

6 A I do.

7 Q Can you then turnover please to tab 18 where you should have your second report. Turn to  
8 p.21. Is that your signature?

9 A Yes, it is.

10 Q Do you adopt this report as your evidence in these proceedings?

11 A I do.

12 Q Finally, just go to tab 2 of the same bundle.

13 A Got it, there is a second tab 2.

14 Q Yes, there is a tab 1.2 and then there should be a tab 2 which should contain the joint  
15 statement of yourself and Mr. Coulson?

16 A Yes, I've got that.

17 Q Could you turn, please, to p.10. Is that your signature?

18 A It is.

19 Q Again, subject to the point in the letter, do you adopt that as your evidence in these  
20 proceedings?

21 A I do, yes.

22 Q Thank you. Would you wait there, please?

23 Cross-examined by Mr. READ

24 Q Mr. Robinson, good afternoon. As you know, I am asking questions on behalf of BT. Can I  
25 just ask you to look at your first report which is at tab 17. Just so that we are clear about it,  
26 although we are calling this your first report, it is in fact your amended first report?

27 A It is indeed, yes.

28 Q The reason why it is amended is because following your first report you were asked a series  
29 of figures from Ofcom which you felt quite happy with, to include in this amended report,  
30 to update your information?

31 A Yes, at the time I did.

32 Q Subject to that, your first amended report is the same as your original first report?

33 A Subject to the additional information provided to me by Ofcom, yes.

34 Q Can we just explore, then, what you were asked to do in your first report. I think we can see

1 that most easily at para.1.3 p.4 where it sets out what you are instructed to do?

2 A Yes.

3 Q If we look at the first item on that which is "how much interest is payable on the  
4 overcharged amounts based on BT's cost of equity", that issue is parked because it is going  
5 off to another hearing if needs be.

6 A Item 5, yes.

7 Q Item 5, and so we do not need to consider that further.

8 A Yes.

9 Q The second item that we can look at is item 3 where you are specifically asked what is your  
10 view of Ofcom's exclusion of the 2009/2010 holding gains in the service costs in their Final  
11 Determination, and your conclusion on that was at para.6.12 p.36 of your report where you  
12 say that in your opinion mechanism 3 is a reasonable methodology. I will not go through all  
13 of the mechanisms that were involved, but you come up and say mechanism 3 is the right  
14 way of making this adjustment. It was Ofcom's mechanism 3 originally. You say in 6.14:

15 "Therefore, in my view, it is important that the Mechanism is employed so as to a)  
16 address the issue of inconsistent treatment of costs in 2009/10 and b) address any  
17 'genuine' holding gain incurred in that year."

18 That was that you said?

19 A Yes, I believe that's what it says, yes.

20 Q We know that that point is no longer pursued in this hearing?

21 A That is correct.

22 Q Does it mean that your views as set out in this report have changed?

23 A I think that there's a distinction to be made in terms of the points that I make in here are that  
24 it's desirable to have a matching P&L and balance sheet, i.e. that are compatible with each  
25 other. The points made by Ofcom in its Defence related to their issue with this adjustment,  
26 with this mechanism 3 adjustment, in so far as it pointed out in greater depth than they had  
27 done previously the difficulties that they may encounter in doing so. Furthermore, the fact  
28 that in doing so the changes to costs could be positive or could be negative; it's ambiguous  
29 which way they would go. So whilst I would still stand by what I've written here in terms  
30 of I believe it to be desirable that there is consistency between the P&L and balance sheet.  
31 In terms of materiality for the determination of these issues, it was appropriate to drop that  
32 ground of appeal, I feel. It was reasonable to drop that ground of appeal.

33 Q I do not want to spend any length of time on this, because obviously it is not an issue in the  
34 case, but just to unpick it, you are talking about it could be plus, it could be positive?

1 A That's what Ofcom says.

2 Q That is what Mr. Coulson said in his second report, was it not? He was the one who raised  
3 the question of the effect would actually turn out to be negative?

4 A For the 2009/10? Could you point me to the passage?

5 Q If you do not accept that, I do not want to take up time on this because it is not an issue in  
6 the case.

7 A I'm familiar with that statement in Mr. Coulson's second report.

8 Q What I am trying to unpick from you is whether you are saying that your conclusion is still  
9 right, but in fact it is immaterial in the effect it has; or whether you are saying it is still right,  
10 even though Ofcom has said something different in the defence?

11 A Sorry, which is the first one? Could you repeat that?

12 Q As I say, I think it would be wrong for me to spend a long time on a point that is not  
13 actually involved in this case. Anyway, whatever the position, that issue is no longer with  
14 us.

15 Can we now turn to item 2 on para.1.3. There you were asked:

16 "What effect does the inclusion of the Regulatory Asset Value (RAV) adjustment  
17 to costs have on the level of overcharge imposed by BT calculated in accordance  
18 with a) an aggregate FAC-based approach and b) the overcharge calculated by  
19 Ofcom?"

20 You see that?

21 A Yes, I do.

22 Q You were never asked, is that right, to consider your views on the appropriateness of the  
23 RAV adjustment at that stage?

24 A At that point, no.

25 Q I will come back to that, but can we just look at the figures. I want to just run through with  
26 you the figures as I understand them, and see if we can get some consensus on this. To  
27 assist in this I have actually set out a table which I think should cover all the various  
28 differences. (Handed) Sir, I produce this simply to try to cut things down a bit shorter rather  
29 than having to go through the documents. If we just look at the first entry, which is your  
30 first figure, the adjusted figures (because you have taken a shorter period to look at the  
31 dispute) on the Ofcom basis is £136.9 million, and we get that from your table 2. That is  
32 right?

33 A Yes, that covers the period from 2006/7 through to the end of July 2009/10.

34 Q Then your figure in your amended report, after you had had all the material you wanted

1 from Ofcom, was that the overcharge with the RAV adjustment on the DSAC basis (not  
2 getting on to the FAC basis) was £140.8 million?

3 A Yes.

4 Q In your first report. I have given an indication of one table, but I think in fact it crops up in  
5 a number of places, but perhaps it does not matter if you accept that that is the figure. So  
6 the increase in the overcharge – do you want to see the table? If you accept that is the  
7 figure I will not take you to the table.

8 A No, I accept that that's roughly right.

9 Q So the increase in the overcharge with the RAV adjustment in your first report is 3.9 million  
10 on what Ofcom has already produced, on Ofcom's figures?

11 A Yes.

12 Q Then in your second report – obviously the baseline figure for Ofcom is the same – but your  
13 figures for the overcharge with the RAV adjustment go up to 143.7 million?

14 A Yes.

15 Q Again, if you want to check that, I am quite happy for you to do so. I think it is in table 2 of  
16 your second report at p.33.

17 A Yes, I see that.

18 Q So you are happy that that is the correct figure I have used there?

19 A Yes, that is the figure that I used in my second report, yes.

20 Q I said p.33.

21 A Yes, I think p.10 of my second report.

22 Q Sorry, there is an error in that table, sir.

23 THE PRESIDENT: Is not there also an error, it is July 2009, is it not? The period is 2006 to July  
24 of the 2009/10 financial year.

25 A July 2009, yes.

26 Q So it should be 2009 throughout.

27 MR. READ: Perhaps we ought to look at table 2. Yes, sir, you are right. It is because I have  
28 tried to strip it down too much. It should have said July 2009/2010.

29 THE PRESIDENT: It is actually 2009, yes.

30 MR. READ: Sorry, sir. The increase then became 6.8 million?

31 A Yes, that's correct.

32 Q Mr. Coulson's figures in reply are set out in his second report, but we can see them in the  
33 joint statement. Perhaps we should look at the joint statement at tab 2 in that bundle. We  
34 see those on p.7, and we can see in para.3.3 that there is Mr. Coulson's figure for the

1 comparison with yours which is £139.3 million. That, you adjusted up slightly to (and I  
2 think there is a rounding issue here) £139.5, but the net effect, as we see in para.3.4 is that  
3 the total impact figure is £2.5 million. Do you agree with that?

4 A Yes.

5 Q So the net result of all of this is that you have had two figures that have been quite large,  
6 Mr. Coulson has come up with one figure, which was about £100,000+ off, and you  
7 effectively agreed £100,000 in excess of Mr. Coulson's calculations?

8 A That is correct, yes.

9 Q Can you go back to your second report, which is at tab 18. We see that at para. 1.6, which is  
10 on p.4?

11 A Yes.

12 Q You then set out that you are now instructed to consider:  
13 "whether the inclusion of the RAV adjustment may result in a more accurate view  
14 of costs".

15 A That's correct.

16 Q As you said earlier, that was not in your first report?

17 A It wasn't, I simply put some framing information in my first report. The second report  
18 addressed that direct question, as per my instructions.

19 Q At 1.9 we see there your conclusion, which may result in costs that differ from those which  
20 have actually been incurred had a consistent approach been applied. That is your  
21 conclusion in 1.9?

22 A That is my conclusion, yes.

23 Q Has that always been your view?

24 A On the RAV adjustment, yes.

25 Q Can I ask you to take bundle ST1-2, tab 9 - this is in fact an RGL Forensics Report dated  
26 23<sup>rd</sup> July 2010?

27 A Yes.

28 Q Which, in fact, was submitted with the dispute when it was put in. Were you the author of  
29 this report?

30 A No.

31 Q Did you have any involvement in it?

32 A I had involvement in it, yes.

33 Q Because if we look at para. 1.21 it says in terms:  
34 "We have then made a number of adjustments to the costs in the RFS to provide

1 more accurate calculations, based on the approach taken by Ofcom in its 2009  
2 Leased Line Charge Control and also its dispute determination on PPC charges,  
3 where appropriate."

4 Do you see that?

5 A Yes, I do.

6 Q That did not involve a RAV adjustment, did it?

7 A No, it didn't.

8 Q You see, what I am interested in is why, if the RAV adjustment is so inaccurate now was  
9 someone not saying that earlier on?

10 A Do you mean inaccurate or accurate?

11 Q Sorry, if making the RAV adjustment, which Ofcom has not done, if making it is so  
12 necessary in order to get an effective accurate view of the accounts, why was this not being  
13 picked up earlier?

14 A I can only go via my recollection of working on this report and I believe that at the time the  
15 principal consideration was to try to bring costs in line with those which were set out in the  
16 leased line charge control, which did not include a RAV adjustment at that point. If I go  
17 back to the genesis of considering whether a RAV adjustment should be included and where  
18 that decision might have been made, it would have been considerably later. The fact that a  
19 RAV adjustment gives a more accurate version of costs actually incurred I don't think is a  
20 particularly contentious point, it's just a point that was not made in 2010 but subsequently  
21 was made in the context of later documentation.

22 Q Can I ask you to take core bundle E? Can I ask you when you have that bundle to go to tab  
23 14? This is an extract from the Leased Line Charge Control?

24 A Yes.

25 Q If you go to p.37 do you see that?

26 A Yes.

27 Q One can see that just above para. 5.56, there is a heading: "We have not taken into account  
28 the RAV for pre-97 access copper and duct"?

29 A Yes.

30 Q So you see that Ofcom there have set out in a number of paragraphs why it is that they say  
31 the RAV adjustment should not be taken into account?

32 A I think there is a distinction to make here. From my recollection of this document, although  
33 it may not be 100 per cent accurate, the principal reason that Ofcom did not apply a RAV  
34 adjustment on AISBO services in this leased line charge control was because they felt that

1 Ethernet services being a newer technology were less likely to make use of 97 ducts, which  
2 is also what it says on para.5.56. That's somewhat debatable and to showcase the  
3 'debatability' of that it is worth pointing out that in the more recent charge control Ofcom  
4 have adopted a RAV adjustment on AISBO services on Ethernet services.

5 Q I just want to go back a stage, because we can see this from, in fact, some of the subsequent  
6 paragraphs, which I think you have already identified, which is that Ofcom did make the  
7 RAV adjustment for other types of product, did it not?

8 A In particular in this document they made the RAV adjustment for TISBO services.

9 Q Yes. So therefore in 2009 it was clear that Ofcom was applying a RAV adjustment in  
10 certain respects, and again I put the question why is it in 2010 that no one thinks it is  
11 inappropriate to adopt Ofcom's stance of excluding the RAV adjustment in respect of  
12 AISBO?

13 A I would have to say that I do not recollect why a RAV adjustment was not adjusted at that  
14 point in 2010, I simply do not recall why the author of the document opted to leave it out.

15 Q Can you look at para. 5.60 in the leased line charge control?

16 A Yes.

17 Q You can see that Ofcom sets out a number of reasons and one that I think you have already  
18 alluded to, namely:

19 "Most future investment is likely to be in new fibre services. Unlike TI services, it  
20 is likely that there will be a significant amount of future investment by Openreach  
21 and potentially other CPs in infrastructure used to provide Ethernet services. It is  
22 important for us to set the correct pricing signals (by setting prices which reflect  
23 the replacement cost of the assets) to encourage efficient future investment in this  
24 area."

25 Now, you are not in a position, are you, to second guess whether that was right for Ofcom to  
26 say that was the policy or not?

27 A I am sorry, could you rephrase the question?

28 Q Yes. You see what they are saying in that third bullet point of para. 5.60? If you want a  
29 chance to read it to yourself then do so?

30 A (After a pause): Okay.

31 Q So they are saying, in terms, that they want to set the correct pricing signals to encourage  
32 efficient future investment. That is a regulatory decision, is it not?

33 A That's what they say in that paragraph.

34 Q Are you suggesting that that decision by Ofcom was wrong?



1 A I am not sure whether to say that they are wrong. However, what I would say is that I don't  
2 think that that has any bearing on my statement in my report where I say that a RAV  
3 adjustment gives a more accurate version of costs. I think that this is clearly a policy type  
4 issue raised in order to encourage efficient future investment, so I do not think it is  
5 diametrically opposed to what I have written.

6 Q Yes, I know it is. I am putting to you that this is not just an accounting exercise that has to  
7 be done here, there is policy - regulatory policy - involved in it, and I think you were  
8 accepting that?

9 A I accept that there are various issues that Ofcom has to take into account when they are  
10 making any adjustment. I would say that accurate costs are very high up on that list, but I  
11 accept your proposal to a certain extent in terms of there are other considerations to be  
12 made.

13 Q Let us leave that subject and put that bundle away. Can we now go back to your first report  
14 which is in tab 17 in bundle D?

15 A Yes.

16 Q And can we then go back to the paragraph we were looking at previously, which is para.  
17 1.3?

18 A Yes.

19 Q And the other two items that are on that instruction list, namely items 1 and 4 ----

20 A Yes.

21 Q -- effectively relate to what is known as the FAC test?

22 A Yes.

23 Q Can I ask you to go to para. 2.22 which I think is on p.12?

24 A Yes.

25 Q You set out there the methodology you have used to actually allocate the various  
26 overcharges?

27 A Yes, I do.

28 Q Alleged overcharges. Now that is not your methodology is it, let us be clear about that?

29 A No, it is not, no. It's an implementation of the methodology set out by Mr. Houpis in his  
30 first report, I believe.

31 Q Can we just explore how this methodology actually works in practice, because I want you to  
32 go to table 34, which is on p.42 of your first report?

33 A Yes.

34 Q This is the total overcharge using a FAC based aggregated approach allocated to service,

1 including the RAV adjustment?

2 A Yes.

3 Q And if we can just look at one figure, can you look at BES 1000 rental, do you see that?

4 A Yes.

5 Q If you look at the second row down on your table ----

6 A Table 32 is this?

7 Q Sorry, table 34. Just to be clear, look at p.41 first?

8 A Yes.

9 Q And so we are clear about this you are talking under subsection "(iii) Total overcharge" do  
10 you see that?

11 A Yes, table 34 "BES 1000".

12 Q Yes, and so we are looking at the total overcharge that the two-stage methodology ends up  
13 with for the various products?

14 A Yes.

15 Q This includes the RAV adjustment, and we see that if we look at BES 1000 rental - do you  
16 see that?

17 A Yes.

18 Q The second row down, if we look just at 2007 and 2008, it comes to a figure of £34.3  
19 million, does it not?

20 A Yes.

21 Q Can you go back in your report now, keeping that figure in mind of £34.3 million, to table  
22 15, which I think should be on p.20.

23 A Yes.

24 Q Which is the adjusted total external revenues for the Ethernet services for 2006 to 2007 to  
25 July 2009 - yes?

26 A Yes, sorry, which table?

27 Q Table 15.

28 A That's all the way through 2009/10, it doesn't go to July 2009.

29 Q Yes.

30 A It goes to March 2010.

31 Q So this is the revenues that are actually earned by BT in that particular year from other CPs -  
32 yes?

33 A Yes.

34 Q Can we look at the BES 1000 rental. According to your table BT earned from CPs

1 £26.6 million - do you see that?

2 A Yes.

3 Q Your table with the FAC adjustment that we have looked at in table 34 suggests that there  
4 should be a repayment of £34.3 million?

5 A It does, yes.

6 Q Which means that BT is being required not just to repay everything that it earned in  
7 revenue, but to repay more than that?

8 A For that specific service, that is what it implies. However, I think that it's important to make  
9 the distinction and look at this as it was intended to be looked at, i.e. on an aggregate basis  
10 in terms of how much in total should be paid back from BT to CPs. This is a methodology  
11 for allocating a FAC based overcharge into the services to facilitate payments from BT to  
12 CPs.

13 Q You are instructed, are you not, by Sky and TalkTalk?

14 A I am instructed by Herbert Smith.

15 Q Yes, but effectively the people ----

16 A Sky and TalkTalk are their clients, yes.

17 Q BES 1000 rental - they are the biggest consumers of BES 1000 rental?

18 A Is that right?

19 Q Did you know that?

20 A I didn't know it off the top of my head, no.

21 Q So, in fact, for them this methodology works substantially in their favour, does it not, if it  
22 ends up with a result like that?

23 A In that particular year for that particular service, that's what that would imply.

24 THE PRESIDENT: I did not follow your answer when you accepted that your tables show that  
25 the overcharge is greater than the revenue. You say it is supposed to be considered in the  
26 end on an aggregated basis. How do you get to an overcharge calculation that is greater  
27 than the revenue in the first place?

28 A I think the methodology set out by George and then implemented by me, the purpose of it is  
29 to carve up the £232 million by service in order that - there's a two-sided approach to it,  
30 which I think George has been through over the past couple of days - Dr. Houpis has been  
31 through over the past couple of days. It is a way of carving up the £232 million, it's by no  
32 means the only way of allocating it to services.

33 Q You can carve up a figure in lots of ways.

34 A I think the point of the matter is that overall, if you look at these calculations, BT have

1 overcharged above FAC by a large amount. Then there is a question to be had about how  
2 that gets allocated into services. This is simply one way of doing that calculation. To be  
3 honest with you, it's an odd item in the table.

4 Q You know, I think, that different CPs take different products to different extents.

5 A I am aware of that, yes.

6 Q So the way you carve it ----

7 A Matters.

8 Q -- has quite an effect. It matters. It has got to be a way that makes sense, has it not?

9 A Yes, it does, Sir. I think the point is Dr. Houpis has come up with a methodology which has  
10 the benefit of having higher repayments for services which are in greater breach of their cost  
11 orientation obligation with regards to FAC - i.e. how much their revenue is above FAC? So  
12 there is a benefit to the methodology in terms of the services which are most in breach  
13 attract the most repayments. This is something of a quirk in the calculation which I  
14 appreciate entirely.

15 PROFESSOR MAYER: Can I ask whether or not this raised any concerns in your or Dr. Houpis's  
16 minds about the methodology and whether or not it needed some further consideration?

17 A It's not something that I have discussed with Dr. Houpis, and no, it's not something that's  
18 occurred to me until today.

19 MR. HARRISON: So it could be an error in the numbers?

20 A I don't think it's an error in the numbers. I think it's a quirk of the facts that those particular  
21 services are the ones that are most in breach of ----

22 Q How can you end up giving back more than your revenue? That is the question that has  
23 been put: let us say I was only buying that one service in that year, and I was the one who  
24 paid whatever it is ----

25 A You get more back than you actually paid out, yes.

26 Q -- £36 million, and I got more than I actually paid. How can that, on any sort of quirk, be  
27 right? If you have just looked at it for the first time then it would be better to say that it  
28 could be an error in the numbers.

29 A I don't think it's an error in as much as it - the best way to explain it is that I've got a round  
30 number at the bottom that I'm allocating into services based on the extent to which they  
31 priced above FAC. It just so happens that BES 1000 services are so high in terms of the  
32 FAC price margin that they attract more of this overcharge than they actually caused in the  
33 first place. It is not an error in the calculation, but it's a potential weakness in the  
34 methodology.

1 THE PRESIDENT: It could be, depending on the amounts, and one sees the same, I think, in  
2 2008/09, does one not, where the amount that was paid to BT was £28.2 million by the CPs  
3 who consumed that service, and your table 34 involves a repayment to them, or calculation,  
4 that they have overpaid by £33.4 million. Does this not suggest to you as an accountant that  
5 there is something inappropriate the way the methodology worked?

6 A It strikes me that in particular the second stage of this test, in terms of the allocation part of  
7 it, could be further refined in order to take these issues into consideration and have a more -  
8 numbers which make more sense vis-à-vis the revenue overcharge comparison.

9 Q Do you agree that this, as it stands, cannot be a sensible way?

10 A I agree that there are oddities to it, yes. I agree.

11 MR. READ: Finally, Mr. Robinson, you have already mentioned, if we go back in your first  
12 report to p.9, and table 5, the table 5 overcharge figure of £240.5 million that you set out  
13 there is wrong?

14 A Yes. It's since been updated with more accurate information and a more accurate  
15 methodology, yes.

16 Q It has been updated because someone made an error in the figures, did they not?

17 A Yes.

18 Q Because someone transcribed the wrong figures into the calculations that produced that  
19 table, table 5?

20 A That's correct, yes.

21 Q On main link?

22 A Yes.

23 Q Can I ask you to the joint ----

24 THE PRESIDENT: Before you leave that, the correction that is being made by the recent letter  
25 changes the ----

26 MR. READ: If you are about to go to the joint statement, Sir, that is where I am going.

27 THE PRESIDENT: No, I am not. That does not change the figures in table 15, does it?

28 A Of?

29 Q Of your amended first report?

30 A The correction that I've made would change them, but only by £1.5 million in 2007/08.

31 Q That is the revenue, is it not?

32 A Yes, it is, yes.

33 Q They do not change?

34 A No, the revenues were the item that was transposed incorrectly. The costs have remained

1 the same. So it is the £41.9 figure that you can see at the bottom of the second column  
2 along, it should have been changed to £40.4.

3 Q I see.

4 MR. READ: The consequence of that is that it does not affect the figures we have been looking at  
5 higher up, because it is focused on main link?

6 A We've been looking at the FAC based overcharge, which obviously in that year would be  
7 reduced in total by £1.5 million, because that's the adjustment. So the figures that you were  
8 pointing to in - which table was it, the allocation table ----

9 Q Just look at table 15 first. This is revenues - right?

10 A Yes.

11 Q And if you look at main link rental, you accept that the figure at the bottom there, and that is  
12 not confidential, £41.9 million, comes down to £40.4 million - correct?

13 A Correct.

14 Q That does not, therefore, affect the two figures at the top of the table next to BES 1000  
15 rental for 2007 and 2008. Those figures are not changed - table 15?

16 A On table 15, no, they're not. However, the overcharge - we've been discussing thus far the  
17 table relating to how the overcharge would be allocated into services - yes. The point is that  
18 we're reducing the FAC based overcharge in that year by £1.5 million. So that subtracted  
19 £1.5 million would have to be allocated into the ----

20 Q When we get to table ----

21 THE PRESIDENT: Let me see if I can short-cut this. It might slightly reduce the figure in  
22 2007/08, but it would clearly still be over revenue?

23 A Yes.

24 Q So the point remains, that figure of £34.3 might need adjustment.

25 MR. READ: Just to complete that, of course it would not affect the position for 2008/09, would  
26 it, because the figure you have adjusted is in 2007/08?

27 A No, it wouldn't, no.

28 Q Can we just move back to where we looking at in table 5. We know what the adjustment is  
29 there. Can I then take you to the joint statement, which is in tab 2 in that bundle, and go to  
30 p.8. We see at 3.5 in the statement your figures that you have produced as a result of the  
31 RAV adjustment that has been agreed with Mr. Coulson? He has not checked these figures,  
32 has he?

33 A Which line are you referring to, or are you referring to the whole table? He hasn't checked  
34 the table as far as I'm aware.

1 Q No, exactly, but what I am suggesting is that actually these are your calculations that flow  
2 through from what you agreed with Mr. Coulson in para.3.3 and 3.4?

3 A That's correct, yes.

4 Q The point is this: these figures now are incorrect, are they not, because they need to be  
5 reworked as a result of the adjustment that we have just seen to your first report?

6 A The letter, you mean?

7 Q Yes, the letter?

8 A The lined marked "External revenue in 2007/08", the £142.7 million should come down by  
9 £1.5 million.

10 Q Just wait a moment there. You are looking at table 3.5, are you?

11 A I'm looking at table 3 on p.8.

12 Q You are talking about the line with external revenue - is that right?

13 A That's correct.

14 Q And you are looking at 2007/08, the figure of £142.7 million?

15 A That's correct, yes.

16 Q You are saying that that has to adjust down slightly?

17 A Yes.

18 THE PRESIDENT: What is the new figure?

19 A 141.2.

20 MR. READ: It is right that Mr. Coulson has not checked any of these figures because he was not  
21 instructed to?

22 A I do not know exactly Mr. Coulson's instructions but I will take that.

23 Q At the joint expert meeting he was not agreeing those figures, was he, because that was not  
24 part of his brief?

25 A Yes.

26 MR. READ: Thank you, Mr. Robinson, if you would just like to wait there.

27 THE PRESIDENT: Mr. Pickford, any re-examination?

28 MR. PICKFORD: Yes, just very briefly.

29 Re-examined by Mr. PICKFORD

30 MR. PICKFORD: Mr. Robinson, if you could go back, please, to the RGL Forensic's report that  
31 you were taken to in ST1 Volume 2, Tab 9?

32 A Yes.

33 Q You were taken by Mr. Read to a paragraph entitled "Limitation of Analysis". It was put to  
34 you why RGL were not making a RAV adjustment, if it was allegedly an obvious thing to

1 do or an appropriate thing to do. Could you clarify for me, please, what the scope of RGL's  
2 instructions were in preparing this report, as far as you can recall?

3 A We were asked to examine whether there was any evidence that BT had breached its cost  
4 orientation obligation. Beyond that I would not remember the details.

5 Q Do you recall whether you were asked to take a view on whether there were adjustments  
6 that should be made that differed or were in addition to those set out in the 2009 Lease  
7 Lines Charge Control or the PPC dispute determination?

8 A I do not recall exactly but I would assume not.

9 THE PRESIDENT: Were your instructions as set out in para.1.1.2? Does that accurately  
10 describe the scope of what RGL was asked to do?

11 A Yes, that is it in a nutshell.

12 Q So you were asked whether there is evidence that BT has failed to comply with the  
13 obligations and, if so, what amount BT should repay?

14 A Yes.

15 MR. PICKFORD: I have no further questions. Thank you.

16 THE PRESIDENT: We have no more questions, Mr. Robinson. You are released.

17 (The witness withdrew)

18 MR. PICKFORD: I am grateful. That brings to an end to TalkTalk's and Sky's evidence.

19 THE PRESIDENT: I think we will resume next Thursday with Mr. Myers' evidence for BT. We  
20 have had a note, and I think you may have had it as well, from the transcribers that there is  
21 some delay in producing a transcript for today because their internet and telephone line has  
22 gone down. They say that they hope the situation will be resolved by BT soon! So perhaps,  
23 Mr. Read, Mr. Thompson, and those behind you, can use their good offices to restore that  
24 situation for our general benefit. We will resume at 10.30.

25 MR. PICKFORD: Sir, I just had a couple of minor points, if I may, before we go.

26 THE PRESIDENT: Yes.

27 MR. PICKFORD: The first was a housekeeping point in relation to confidentiality. I was asked  
28 to indicate whether the figures in Table 1.3 were confidential. The totals, that is the bottom  
29 row in the right-hand column, are not confidential to my clients and so we are happy to have  
30 those. I think it was just those total figures that the Tribunal were concerned with. That is  
31 in Bundle B.

32 THE PRESIDENT: I remember it, yes. You said there were a couple of housekeeping points?

33 MR. PICKFORD: Yes, that was the first one. The second one is that in order to assist and  
34 hopefully make much quicker my cross-examination of Mr. Myers next week, I have



1 prepared some calculations that are based on numbers in the report. So in order to give him  
2 an opportunity to see them and, indeed, if he wishes to, discuss them with Ofcom  
3 beforehand, I would like, if I may, to hand that up now so that he is not taken by surprise by  
4 any of those calculations. They are all based on numbers that are in the report.

5 THE PRESIDENT: Yes, that is very helpful and appropriate.

6 MR. PICKFORD: Then, finally, the third point was to apologise for an oversight earlier on in the  
7 week when I think I certainly was very preoccupied with my cross-examination of Dr.  
8 Maldoom, but I think we may have failed to offer our formal congratulations from the Bar  
9 on your appointment as President from Tuesday of this week. So if I could offer those  
10 congratulations.

11 THE PRESIDENT: Thank you very much. On that note, we shall adjourn until next Thursday at  
12 10.30.

13 (Adjourned until 10.30am on Thursday, 14<sup>th</sup> November 2013)