IN THE COMPETITION APPEAL TRIBUNAL

Victoria House,
Bloomsbury Place,
London WC1A 2EB

5 February 2008

Before:
VIVIEN ROSE
(Chairman)

ANDREW BAIN OBE
ADAM SCOTT TD

Sitting as a Tribunal in England and Wales

BETWEEN:

1083/3/3/07

HUTCHISON 3G UK LIMITED
("**H3G")**

and

OFFICE OF COMMUNICATIONS ("**OFCOM**")

AND

1089/3/3/07

T-MOBILE UK LIMITED ("**T-MOBILE**")

and

OFFICE OF COMMUNICATIONS

AND

1090/3/3/07

BRITISH TELECOMMUNICATIONS PLC ("**BT**")
and

OFFICE OF COMMUNICATIONS

AND

1091/3/3/07

HUTCHISON 3G UK LIMITED ("**H3G**")
and

OFFICE OF COMMUNICATIONS

AND

1092/3/3/07

CABLE & WIRELESS UK & OTHERS ("**CABLE & WIRELESS**")
and

OFFICE OF COMMUNICATIONS

HEARING DAY EIGHT

APPEARANCES

Miss Dinah Rose QC and Mr. Brian Kennelly (instructed by Baker & McKenzie) appeared for H3G.

Mr. David Anderson QC, Mr. Graham Read QC, Miss Anneli Howard, and Miss Sarah Lee (instructed by BT Legal) appeared for BT.

Mr. Jon Turner QC and Meredith Pickford (instructed by Regulatory Counsel, T-Mobile) appeared for T-Mobile.

Mr. Matthew Cook (instructed by Olswang) appeared for Cable & Wireless.

Miss Elizabeth McKnight and Mr. Stephen Wisking (Partners, Herbert Smith) appeared for Vodafone.

Miss Marie Demetriou (instructed by Field Fisher Waterhouse) appeared for Orange.

Miss Kelyn Bacon (instructed by SJ Berwin) appeared for O2.

Mr. Peter Roth QC, Mr. Josh Holmes and Mr. Ben Lask (instructed by the Office of Communications) appeared for OFCOM.

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THE CHAIRMAN: Good morning everybody. Mr. Roth, unless there is somebody else who wants to speak – Mr. Turner?

MR. TURNER: Very briefly, a few matters left over from yesterday. The first in relation to the Tribunal's proposed course of action in relation to judgments following my remarks at the close of proceedings yesterday, I confirm that we have no objection at all to the Tribunal's proposed course. We only wanted to lay down the marker, and the Tribunal will have this well in mind, that the outcome of the hearing now may have some impact on the trial of the non-core issues. Having said that, we would be the last people to suggest that the Tribunal should hurry a judgment out in order to save any costs that may arise in relation to the non-core issues, and we are therefore content with the Tribunal's proposed course.

The second point: madam chairman, you raised with me at the opening of my submissions yesterday a point that I said I would check in relation to Mr. Miller's witness statement. With madam chairman's eagle eye you had, of course, spotted that one of the post-pay tariffs referred to by Mr. Miller, the flex 35 tariff, one of the three that were mentioned, was indeed below the level of the wholesale charges of other operators as well as H3G, whereas we were making an H3G point in that paragraph.

In relation to that, if I may, I will make one or two points. First, H3G of course still remains the out-lyer by a considerable margin. Secondly, in our submission this points up a more fundamental difficulty with the gains from trade test as a whole very starkly, which is, as the Tribunal knows we and the Altnets say once one goes down the road of assessing impacts, gains and losses of people affected by your decisions, you should do it properly and that you should therefore look at the impacts on the transit customers as well, and that when you are assessing the impact on those affected at a particular point in time – stage 1 of the gains from trade test – look at the retail tariff now and compare it with the proposed wholesale rate, that is inherently unsatisfactory – a point which Ofcom themselves have essentially recognised which is why they then modify their gains from trade tests by moving to the pass-through stage 2 assumption, and you have our submissions on that, the pass through stage 2 is both meaningless and itself has distorting effects.

Just as a reference for what I have just said, in para.57C of our skeleton we have referred to the Ofcom defence at para.133.1 Ofcom itself has stated clearly the reasonableness of the charge should not depend solely on BT's downstream pricing decisions, which is why you move on to pass-through. Madam, that is all I wanted to say about that.

The other point that you raised, and I do not know whether this is an appropriate point or not to deal with it, was the point that you through out to the parties about SIA, and the

approach that the Tribunal might want to take in relation to clause 12(3)(1), and the analysis of that.

THE CHAIRMAN: Well, why do we not deal with that this afternoon, Mr. Turner.

MR. TURNER: Madam, I am obliged.

THE CHAIRMAN: Mr. Roth.

MR. ROTH: Thank you, madam. Can I say straight away that Ofcom also has no objection to the Tribunal's proposed course.

THE CHAIRMAN: Well I am assuming that as no one has contacted us that everyone is content with that course.

MR. ROTH: There seem to be nods all 'round. I was dealing yesterday with the question of whether it is appropriate for Ofcom to look at a blended rate and assess the disputed charge on that basis, and I now turn to how Ofcom assessed the reasonableness of the disputed charges in the BT determination, and emphasise that Ofcom did so in terms of the End-to-End Obligation, because that is what introduced the reasonableness requirement, and so Ofcom asked the question: "Is it reasonable to require BT to purchase interconnection at the charge at issue?" They approached the answer to that question and the criterion of reasonableness in the context of the purpose of the End-to-End Obligation imposed under Article 5(1) of the Access Directive, or I suppose more precisely imposed under the domestic enactment of that provision which is sections 45, 73 and 74 of the 2003 Act.

So one comes to the gains from trade test. Madam, I rather lost track of the pejorative adjectives and epithets that were applied by counsel to this test, so may I explain its logic. It has two quite distinct stages. There is a central gains from trade test, and then there is the pass-through issue; whether one says they are two parts of the same test or two successive tests – you will recall Mr. Keyworth says there are prevailing prices' gains from trade test and a variable prices' gains from trade test, I think that is really a question of semantics. At this point I would like to trace first the basic test or, if you like, stage 1, before any question of pass-through.

BT is under an obligation to purchase interconnection on reasonable terms. The purpose of that obligation is to require BT, who otherwise might be able not to interconnect, or at least threaten not to interconnect with a particular mobile network operator to ensure they do interconnect, but it is not an unbounded obligation as it would not be right to force BT to purchase interconnection with an MNO if they were financially worse off from doing so. But so long as BT is no worse off from being forced to interconnect than if it did not interconnect, i.e. so long as BT is purchasing interconnection at a charge that covers their

break even cost for the calls, then it is reasonable to require BT to do so; that is the underlying logic. So one is looking at reasonableness only in terms of whether BT should be required to interconnect at that price – the regulatory obligation involved. We say that is a principled approach, and on this point in the rather shifting alliances between the various network operators, we appear from the submissions yesterday by Miss Dinah Rose, to be supported by H3G in saying that that is the right approach to take, whether it is reasonable for BT to be purchasing interconnection – no, she is shaking her head, so we did not! (Laughter)

MISS ROSE: That is certainly not our position, as I think the Tribunal knows.

THE CHAIRMAN: I think you are on your own on this point, Mr. Roth! (Laughter)

MR. ROTH: I am on my own, well I have a few friends behind me who follow on … (Laughter) … in some of the operators. Well the point is this, it may be that the price demanded by the MNO is a high price, since the MNO has SMP. It may not be a cost based price. It may be higher than some notional competitive price – whatever that might be. But, if that is so, that is the result of exercise of market power by the MNO, and the most appropriate way for the regulator to address the exercise of market power is by SMP conditions. In adopting that approach to Ofcom's powers under the framework in the present case we say is in accordance with the Article 8 objectives since here first contemporaneously with the referral of the disputes Ofcom was in the course of a market review of these MNO charges that, indeed, by the time of the determinations had already lead to the imposition of SMP price control on a forward going basis, but covered the full blended rate. Secondly, because that price control had "kicked in" – to put it colloquially – on 1st April 2007 these charges were only retrospective. Thirdly, it had no adverse effect on end users for the same reason; and fourthly, to use dispute resolution as a means of controlling the 3G element of the blended rate in a period covered by the recently extended previous SMP regime would be inconsistent, and therefore an unreasonable measure in terms of Article 8(1) and discourage investment in terms of Article 8(2).

MR. SCOTT: Mr. Roth, just on the factual matrix there, as we understand it BT did not shift its tariffs. Are we right in thinking that nobody else shifted their tariffs, or is there a suggestion that there may have been tariff shifts amongst the Altnets?

MR. ROTH: There is no evidence of any shift in tariffs.

THE CHAIRMAN: Oh, I think there is. Mr. Cook.

MR. COOK: There is indeed evidence of a shift in tariffs and you will find that in Mr. Harding's witness statement. That was our recollection.

THE CHAIRMAN: Sorry, could you repeat that?

MR. COOK: There is witness evidence from Mr. Harding that Cable & Wireless did indeed shift its tariffs in a pre-emptive way.

THE CHAIRMAN: Is that its own transit tariff, or its retail tariff?

MR. COOK: My instructions are that it is both.

MR. ROTH: Madam, I will come back to that, if I may. I think the evidence is that there was some increase in prices because the proposals from the MNOs to Cable & Wireless for the MNOs to increase their MCT charges to Cable & Wireless. But, that was not as a result of these tariffs in dispute, which were the disputes that Ofcom was determining. That is in Mr. Harding's statement at para. 5.4.

THE CHAIRMAN: So, you say that the OCCNs that the MNOs sent to Cable & Wireless were not referred to you under s.185.

MR. ROTH: That is right. They were not part of the disputes before Ofcom.

There were many submissions - written and oral - that one cannot fail the gains from trade test. Well, that is clearly not correct for what I call the basic test - or, Step 1. One sees that if one goes to the determination at Bundle B, Tab 4, p.58. I think all the figures here are confidential. I will direct you to the place in the table and not refer to any figures. But, if you look at Table 7.3, which is headed significantly 'Results of the gains from trade test on all traffic to each MNO', you can see in the first line -- Well, the second line is the disputed charge. The first line is the prevailing charge. The third row is the break-even charge. You can see that the four 2G/3G MNO proposed prices pass this test. As for H3G, you will recall H3G has two disputes referred to Ofcom. There is first of all that BT sought to reduce H3G's current charge - a proposal that H3G refused; secondly, H3G, for its part, sought to increase its current charge - a proposal that BT refused. Both of those disputes were passed. So, the first one - the proposal by BT to reduce - relates to the current prevailing H3G/blender charge, the figure you have in the top left box. That is below the break-even charge in the third row. I am sorry - it is slightly inconvenient to have to address it in that coded way, but I hope you can follow ----

THE CHAIRMAN: If you are going to be saying anything more about this, it might be convenient actually to ask those who are not within the confidentiality ring to leave?

MR. ROTH: I think I can do it without. I think it is probably preferable, as a matter of public policy to do so if we can. If it comes to a point, Madam Chairman, where you feel that it is difficult, then perhaps we may have to take that course. But, I hope so far it is clear.

One can see, therefore, the conclusion reached on that basis in para. 7.7 which is not confidential.

> "Therefore the gain from trade analysis shows that BT earned a profit on an incremental basis in respect of Orange, Vodafone, and H3G's current termination charges and the termination charges proposed by 02 and T-Mobile, even in the absence of pass-through. In such circumstances, Ofcom does not need to consider whether or not BT could have passed through any of these price increases to its customers as BT was already obtaining a gain from trade. Therefore the finding that BT obtained a historic gain from trade provides evidence that these charges are reasonable in the context of the End-to-End Obligation".

Pausing there, for those charges we say this is an acceptable approach. No issue of pass-through arises. BT can pay those charges without being forced to make a loss by granting this interconnection. Picking up, Madam Chairman, your question from the start of yesterday -- how BT funds that payment we say is not relevant to the regulator.

THE CHAIRMAN: Even if it funds it by putting up prospective charges to end users?

MR. ROTH: That would be relevant, yes. Absolutely. But, for the reasons I sought to explain yesterday (a) there is no evidence that it did; and, (b) as a matter of principle, as it is not regulated in its retail charge, it would presume to be charging its retail customers the profit maximising price. These are purely historic now. It is retrospective. If it was prospective, yes. Absolutely. Because then it would be passed through. To future retail customers it would be of great concern. It would not come into the gains from trade test, but it would be of concern because of Article 8. You would not just stop with the gains from trade test. You will say, "Okay. It passes gains from trade, but does it have an adverse effect on end users?" Yes, it does - therefore, it should not be accepted in dispute resolution. But, here, because that was not an issue, because it is retrospective, it was not necessary to go on to that stage.

MR. SCOTT: If we take your point that BT's tariffs are already at a profit-maximising point, then if these prices are not cost-related, what is going on effectively is a shift from fixed network operations to mobile network operations in terms of thinking of economic efficiency overall, because what you are effectively saying to us is that you are not applying an efficiency test to this - you are applying a gains from trade test to it.

Now, what is clear is that cash ends up being in one place and not in another. So, the question then is: Is that right both in terms of equity and in terms of the obligation not to favour one form of electronic communications over the other.

MR. ROTH: Certainly there is a transfer of rent, as it were, for that period from the mobile operator to the fixed operator. It does not distort efficient allocation in terms of consumer choice because it does not ----

MR. SCOTT: I am not talking of the primary level of consumer choice. I am talking about the second level of consumer choice as a consequence, for example, of there being less money available for the new generation networks on the fixed side than is available for the development of the mobile networks. There must be some sort of rationalisation going on there because there is a clearly a shift of funds from one to the other. Now, you may say that the effect on consumers is a secondary effect - but, there must be an economic and radio-spectrum efficiency point in there somewhere.

MR. ROTH: The investments that they make will be made, if they are profitable, on a forward-looking basis, and if the investments are profitable to make, they will make them. It is not suggested that they are then lacking in capital to make them -- or that BT is then lacking in capital to make its investments on a forward basis given the nature and size of these companies. So, there is no reason to think that this shift is actually going to distort their investment decisions. There is no suggestion of that in any of the voluminous evidence. With great respect, it would not be rational to assume that effect.

PROFESSOR BAIN: Mr. Roth, you suggested that BT would already be at the proper maximising price, and so they would not change it when the costs went up. Now, these are incremental costs going up. According to my economic theory, if you change marginal cost, you change the proper maximising price. Is that not your economic theory?

MR. ROTH: Well, if it is a sunk cost -- if it is a poorly sunk cost ----

PROFESSOR BAIN: It is an incremental cost. It is not a sunk cost. You are putting up the margin cost of termination. That is a marginal cost. That will affect the profit maximising price. It ought to affect the prices that are charged. That is why, in general, you assume there will be an element of pass-through.

MR. ROTH: Sir, with respect, that is absolutely right on a forward-going basis if the marginal cost went up, the incremental cost went up. It would put up their prices on pass-through. Here this is being decided in July 2007 relating to calls made in the period up to April 2007, not the cost of ----

PROFESSOR BAIN: I agree that retrospectively it will not put up the price. Could I take a second point ----

MR. ROTH: That was the point. If it were forward ongoing, absolutely, that would have that effect. It is because of the particular situation here.

PROFESSOR BAIN: Of course at the time it was referred to Ofcom it still referred to a forward looking period?

MR. ROTH: At the time it was referred, but they did not put up the price in anticipation of that, and by the time decided it was not.

PROFESSOR BAIN: We will come to that later perhaps, but could I just make another point about this: you are looking here at the incremental cost and incremental revenue, which is fine if you are looking just at the margin of the business. In fact, there is a lot of business going on here. Normally business would expect to be covering some of its fixed costs from that margin. If you remove that element of profit then while you may say on the marginal minute it will still be profitable, so far as the business as a whole is concerned, if you are taking out a large chunk it may turn it from profit to loss, or to a significant reduction of profit. So, in fact, the conclusion about it being marginally profitable does not feed through into saying it will be profitable, because you have got to look at the business as a whole. You cannot simply focus on the margin when you are actually dealing with intra-marginal business as well as marginal business.

MR. ROTH: Sir, I think, if I have understood it, and forgive me if I have not, what one is doing with the break-even is asking what BT charged its retail customers under its then existing prices. Taking out the element that is related to BT's retail network and originating costs and any recovery of fixed costs they may have built into that, which they probably did, seeing what is then left and then saying, with what is left how much MCT charge could be paid without causing BT to make a loss. One has already taken out that element which will be the element in BT's charges to its customers that covers its allocation of fixed costs, network costs, and so on. I do not know if I have understood the question.

PROFESSOR BAIN: In order to make that argument you have to be assuming that BT was earning economic rents. What this is doing is eliminating part of the economic rent that they were earning. If they were economic rents I wonder if Ofcom was doing its job in regulating BT.

MR. ROTH: Ofcom was not regulating BT's retail price at this time at all. They were free from price regulation, the retail level. That had been removed a while ago.

PROFESSOR BAIN: Does that mean that Ofcom had assumed from the market it was effectively competitive so the scope for earning economic rents was not very great?

MR. ROTH: I will need to take instructions as to what happened with removal of retail price control. (After a pause) To explain the position, Ofcom still holds that BT has SMP in the retail market, but Ofcom concluded, when examining that market, that it was moving to an

increasingly competitive position and therefore decided in July 2006 that it would be disproportionate to retain price control on BT's retail prices. How that was all worked out in that statement, that I do not know and cannot assist on. That is the position and was one thing that was not appealed.

THE CHAIRMAN: You were saying that it was not correct to say that you half fail the first stage of the test.

MR. ROTH: Thank you, and I was pointing to 7.7 showing that everything passed but the proposed H3G increase as shown by the bottom left box in the table at 7.3. That failed. We say, therefore, before you get to pass-through that is an acceptable approach and I was seeking to address your questions on that.

Then BT did also apply the same principle in looking at the position of the terminating mobile network operator and asked, "Will they also obtain a gain from trade?" They altered that shortly in para.7.12, which refers back to para.6.15, and basically what they said (I will not read them out) is that no MNO has alleged in response to the draft determination – and indeed I can add no MNO alleges here that as a terminating operator the disputed charge for termination on its own network, so as a terminating operator – that it would have involved trading at a loss from the BT charge. It is a different position on transit.

Then I come to the pass-through point. It is only when one introduces the pass-through or the second stage that the argument that this is a test that one cannot fail arises. That applies, as I have sought to explain, the whole issue of pass-through, only regarding the H3G proposed price increase. The proposal I think was actually mentioned by H3G in open court in the SMP appeal, but just to be safe I will not mention it here. That fails the basic gains from trade test as you see from para.7.8. Analysis shows that BT, in the absence of pass-through, would not be profitable in providing fixed to mobile calls to H3G on the basis of charges proposed by H3G in November 2006. For that particular charge Ofcom noted that BT had not increased its prices in anticipation of the charge. It did not pass it through. That is para.7.9.

So Ofcom proceeds to ask the question, "Would BT have been able to pass it through to its customers?" and concludes that it could have done so and therefore it is reasonable for the purpose of the End-to-End Obligation – that is para.7.10 and 7.11.

I fully accept, madam, that this pass-through extension to the basic gains for trade test has serious weaknesses, as a matter of principle, in that it does not operate as an effective constraint. It is an obvious point that has been emphasised in various witness statements

and oral submissions, a very high charge from an MNO could still be passed through and you get to the point that it chokes off all traffic.

What I say in the context of this appeal, and purely in the context of this appeal, is that the gains from trade and then pass-through is used only on the question of the reasonableness under the E2E obligation. It is just addressing the question of reasonableness in terms of the obligation.

Secondly, if the pass-through of a charge were likely to have a significant impact on traffic volume, such that it would reduce consumers' willingness to make these calls, then a charge at that level would not meet the specific objective in Article 5(1) of the Access Directive, or promoting the maximum benefit for end users (Article 5(1) refers specifically to end-users) and that would be very relevant in a case where the charge was prospective, and so that would have to be taken into account. But on this actual proposed H3G charge none of the extensive evidence from BT suggests that at this level, if it had been passed through, it would have impacted on the volume of traffic. But at higher levels of charge where it would impact on the volume that would indeed be a very relevant factor to which Ofcom would have to have regard – not within the narrow confines of reasonableness but in the determination because then they could say that that is not a charge that we can uphold or set, because it is contrary to the Article 5(1) specific objective.

PROFESSOR BAIN: Does Ofcom regard the effect on the consumer surplus as opposed to the volume as irrelevant?

MR. ROTH: Forgive me. (After a pause) Yes, I was just making sure that I had understood the question – with some help. The answer is: absolutely yes. Indeed, it was my next point, although I had not put it in those terms. The volume point is one point, namely, they would be concerned about volume, but secondly, yes, they would be concerned about just price – even if no effect on volume and that was the point I will come back to and pick up here. Even if the dispute were about a prospective charge that would be passed through to the end-users, even if it would not affect volume, and even if it would meet gains from trade, it would not meet the specific objective of maximum benefit to end-users because of its effect on price to consumers.

PROFESSOR BAIN: You seem really to be saying, Mr. Roth, that if BT, as a counter factual, had in fact put up their prices in the same way as Cable & Wireless did, then Ofcom would have been bound to adopt a totally different analysis taking account of the effect on consumers?

MR. ROTH: They would have had to take that very much into account, and considered it on that basis, absolutely. Where it would have led in the counterfactual hypothesis, that I do not know, it would depend on the circumstances, but absolutely because they would then have had to consider, yes, it passes gains from trade, it would still do that. But, with respect, sir, that is a totally different analysis, they would say: "Yes, it might be reasonable for BT under end-to-end, but it does not meet Article 5(1) or indeed the wider Article 8 objectives, and therefore for that reason we cannot uphold it", and it would depend, I suppose on how much, and reasonable, and so on. But yes, it would have to be applied as a separate stage.

PROFESSOR BAIN: If BT were to put up their prices as a matter of course to protect their position, this would automatically improve their chances of winning their case?

MR. ROTH: In anticipation?

PROFESSOR BAIN: Because Ofcom would then take account of the detriment to consumers.

MR. ROTH: That would follow, I see that is right.

PROFESSOR BAIN: So the procedure you are adopting is a rather odd result that it makes it a no brainer in the future for BT to put up their prices, whenever they are faced with a charge of this kind, to protect their position. If they win they will get a windfall gain because there is no way they will ever be able to repay the consumers; whereas if they lose, they do not lose out because they have already recovered the funds from the consumers to meet the liability that will arise. Is that in the public interest?

MR. ROTH: Again, forgive me. (After a pause) If one ignored pass-through one could also have a problem, I think, on the hypothesis you are putting to me. It is difficult to escape a position where BT could influence the outcome, which is I think your point which I am summarising, as it were.

PROFESSOR BAIN: The point I tried to make is that it seems to me that the analysis being adopted by Ofcom in this case provides an incentive for BT to influence the outcome in a way that may not be in the ultimate interest of consumers.

MR. ROTH: And all I can say in answer to that, sir, is that if this test was applied here in the way it was, in the particular circumstances of this case, where that was not an issue, and it is not being set out by Ofcom as the way and the test, and the way you use it, for every case – and one can see that from the determination pending before Ofcom, which is the 0870 numbers' dispute, which is prospective, where BT is again subject to an interconnection obligation to those 0870 numbers. In the draft determination, I will not take you to it, but for your note the reference is bundle F4, p.441, but there no pass-through step is proposed, and the gains from trade test that is proposed there for BT for interconnection is qualified in a different

way, in part precisely to guard against the risk that otherwise it could lead to an increase in prices for consumers. So the test is subject to qualifications, and we are not saying this is the litmus test for interconnection dispute determination, it is not at all, and it is tailored to this case because clearly, if used in this way, in similar situations, but where the facts, what actually happens, and the prospective effect is different it would have seriously adverse consequences, as you have rather graphically pointed out, sir.

Therefore, we do say that although this particular charge (H3G charge) passed stage 2 of the gains from trade test on the basis of pass-through, it does not mean that in a prospective case it would have been upheld as their other considerations become very powerful and the test indeed might need qualification. Moreover, again in this case, when it came to the remedy, as BT had not in fact passed through the charge to its customers and could not do so it was thought retrospectively to any customers, in the draft determination Ofcom considered that it was not appropriate to require BT to pay more than the break even charge without pass-through, that is to say the figure we have in table 7.3, bottom left. That is what was proposed as the remedy in the draft determination.

Reverting to the chairman's question, this was not a consideration as to how BT can fund the payment, it was simply following through the logic that underpinned the gains from trade test; they should not be required to pay more than that since otherwise they would have purchased in a situation where purchased at a loss.

Indeed, we say that BT could not be criticised for not having anticipated the position because this is the first time Ofcom has been asked to resolve a dispute as to end-to-end and that is discussed in the determination (paras. 4.110 to 4.112). If matters had stopped there and that proposal in the draft had been followed through to the final determination then this whole issue would have been academic because payment would have been ordered only to the figure in table 7.3.

What happened – I will take it quickly because I think you know this – in response to the draft determination H3G suggested that in fact under the SIA BT could recover retrospectively from its transit customers. Ofcom asked BT about this, BT responded that it did have the right to recover, and the quotation in the determination is from a BT response, had the right to recover from originating operators with retrospective effect, as regards this disputed charge (para.6.58 to 6.59). BT's response, when Ofcom went back to them saying that H3G had said this to us – "is that right?" and whether it is right or not is a question for this afternoon. But on the basis that it was right Ofcom then modifies the proposed remedy, by a somewhat complicated process, which is explained in detail in the appendix to our

defence, and it is rather easier to follow in writing (D3, tab 8,appendix B to Ofcom's defence, pp 203 to 205, paras.18 to 25) Summarising it quickly, essentially what Ofcom did was to refer the figures from BT separately; BT's break-even charge for calls by BT's retail customers (BT originating traffic) clearly it could not recover the charge retrospectively from consumers, no question of that. That led to the separate break-even charge that you find in table 7.2, above the table we are just looking at. Therefore that meant that the remedy for BT originated traffic should be at that level, they should pay H3G at that figure and then that left the question "What do you do about the transit traffic?" Although on the basis of the retrospective right to recover BT logically could be required to pay the full amount of the charge and pass it on, and recover it, as it were, recapture it, recoup it from its transit customers, adopting that course would have led transit customers to pay more than BT's retail operations, and that would not be fair to transit customers who compete with the BT retail operation if BT reclaiming from them a higher rate of MCT than BT was having to pay on its own retail operation (para.8.13 of the determination).

> "Ofcom considers that such an approach [as explained above] is a proportionate resolution of the dispute between the parties in that it does not require BT incur a loss on its own traffic and also takes into account that BT can recover the higher charge from its transit customers. Ofcom also notes that available evidence supports the view that H3G avoids a loss of the determined termination charge. Ofcom considers it is appropriate and fair in the circumstances of this dispute for BT to make the same per minute payments to H3G in respect of both BT originated and transit traffic, Ofcom considers both BT and BT's transit customers (if BT chooses to recover the costs of the increase from its transit customers) should be charged at the same rate for H3G's termination service and it would be unfair to require BT's transit customers to pay a higher termination charge for the period",

so the same level of charge will all be BT traffic. That I to avoid a distortion between BT retail and transit customers, taking their interests into account. We also noted in footnote 86, a rather long footnote, that those transit customers, so far as Ofcom could see, should not be bearing a loss as a result. We note that while the Altnets – alternative fixed operators – say of course the reclaim of the charge affects them financially because they cannot reclaim it retrospectively from their customers, they do not allege in evidence from Mr. Harding and Mr. Granberg, the two witnesses, that the result is that they have had to purchase at a loss. Mr. Cook said, in his submissions on this point, the result is that Ofcom

is taking money, or producing a situation where BT, by reclaiming, takes money from his client's top line – I think he probably meant "bottom line", but the reference is transcript day six, p.80 lines 14 to 15.

As, madam chairman, you then pointed out to Mr. Cook, all this only arises if BT can in fact recover from transit customers, and we come to that this afternoon. If Ofcom in fact had to go further and consider the position of transit customers in detail that would have been a huge exercise to undertake within the confines of dispute resolution. BT has approximately 180 transit customers (Mr. Amos, para. 11, Bundle D1, Tab 4, p.116). We say it is just impracticable for Ofcom to have considered the financial impact on each of those. Some, in turn, will act as transit customers for their own wholesale customers. As Mr. Read said in opening BT's appeal, you can have quite a long line in transit operations (Day 6, p.18, line 26). Now, depending upon how you resolve the SIA point, this may all be academic. I do not want to labour this little corner too much. If BT cannot recover from its transit customers, then clearly the determination would have to be revised to go back to the figure proposed in the original draft determination.

THE CHAIRMAN: Is it Ofcom's position that the question, "Can it or can it not?" is determined simply by looking at the terms of the contract, or do you say it is relevant to take into account whether, because of what was said by Mr. Annette to other people, they are in some way estopped from relying on the terms of the contract, or something like that? As far as your investigation was concerned, was it purely a contractual matter?

MR. ROTH: We approached it as purely a contractual matter, and we say it is just unrealistic in the terms of dispute resolution, if Ofcom has to look at this, to go beyond that. They just could not do that. It might vary between customer and customer, and so on.

THE CHAIRMAN: The fact of the matter is between BT and its ----

MR. ROTH: Yes, that is right. All we would say is that if BT are entitled in law to reclaim retrospectively, then it seemed appropriate for Ofcom to take that into account in setting the remedy. We do note that they have apparently recovered quite a significant part of the charge paid on account of transit traffic - not just H3G, but the other MNOs' charges (Mr. Amos at para. 38 of Bundle D1, Tab 4, p.123). We say that it cannot be for Ofcom to determine, in setting a remedy, whether BT will seek recovery; how successful they will be, and so on.

Coming back to the basic point, we accept that the pass-through step does have these obvious weaknesses that have been pointed out. Obviously, one way of resolving that (if the tribunal reach that conclusion) would be to say, "Well, no, you should stop in this case at

the basic gains from trade test", in which case the particular H3G charge -- that charge cannot be upheld and what is permitted goes down to the figure in Table 7.3 at the bottom left.

The only other precise approach put forward is that one should, instead, use some sort of cost based charge - either the charge from the 3G control and the MCT statement, or, as Mr. Turner suggested yesterday, you extrapolate the glide path back for a previous year. That will give you, where you do that, a precise figure. But, to do that would involve regulation of the terminating MNO. Clearly it would be bringing forward the SMP price control for a point in the year before the market review statement applies. We say that should not be done through dispute resolution. I will explain in a moment how that accords with our submissions earlier in the SMP appeal.

Before that, may I just refer briefly to the issue of benchmarking which is used, and was suggested, by some of the appellants? The real problem about benchmarking is that it does not actually fix a precise charge. It can be used - whether it is a one-way test or a two-way test - as a check against the use of other criteria that are employed to derive a precise figure. It is one thing to say - as some have said - that Ofcom should have based the charges under the determinations on the cost based charges from the MCT statement -- or Mr. Turner's alternative, put forward for the first time yesterday which we say is wrong in principle. But, if you do not do that, then even benchmarking against the first year of the MCT statement (and we set out that comparison in our defence, you will recall, and Mr. Cook, in his skeleton argument, adjusted the figures to take account one year inflation) -- Indeed, that shows the proposed H3G charges are very high and out of line. But, it does not actually tell you how to get then to the correct figure. That is the problem that Ofcom primarily had to address.

THE CHAIRMAN: Does it have to address that? Or, can it just say: BT was right to reject this OCCN? I suppose you would then say: "Well, the next day they would put in an OCCN of 15.6 pence", or 14.6 pence, or whatever. Where, I suppose, you are requested to actually fix a sum rather than just say, "BT was right to reject it"----

MR. ROTH: Yes. It would be delightful for Ofcom if we could just say, "No. This OCCN is no good. Go away and think again". But, I think the parties, in bringing the dispute, were saying, "You say it's this. We say it's that. You should determine". Then Professor Bain raised the point, "Well, maybe Ofcom might think of going outside what the two parties said". But, I think just to say, "This proposal doesn't look right to us. Go away" would not be what we are being asked to do.

PROFESSOR BAIN: You did seem to be saying a moment ago, Mr. Roth, that the benchmarking showed that the H3G figure was well out of line, and you seemed to go on from that to say, "Well, that left us with the problem. We didn't know what to do about it". So, what we did about it, of course, was just to accept the H3G figure as slightly amended to bring it down to meet your gains from trade test. If it was well out of line, were you not really obliged to do a bit more than that? I mean, it may be difficult to find some way, but you cannot just say, "Well, it's very difficult. So, we are not going to do anything about it".

MR. ROTH: If this had an impact going forward, yes. In the situation where we had already completed the MCT review and set a charge from 1st April, Ofcom considered, "No" for that period given the limited effect.

PROFESSOR BAIN: So, although it is well out of line, it is still fair and reasonable?

MR. ROTH: Well, it was reasonable because the basic test is whether it is reasonable from the point of view of BT's interconnection obligation because they will not make a loss, and because we are not asking the question, "Is this a fair and reasonable charge?" That is not the question as between the parties. We are just asking the question, "Is it reasonable for BT to be required to interconnect at that charge on the test that if they are not going to make a loss, then it is"?

PROFESSOR BAIN: But, if the benchmarking exercise is to do anything useful, it must alert you to problems. You said a moment ago that it did alert you to a problem. It said that the H3G charge was well out of line. It alerts you to a problem, but you take no action. What use is that benchmarking exercise?

MR. ROTH: The use in the first place was that it gave comfort and reassurance on the other charges.

PROFESSOR BAIN: I understand that that is what you are saying. But, what about the H3G one? It alerted you to a problem. You took no action.

MR. ROTH: Yes. Well, it was not, of course, relied in supporting charges, but, no, we did not then seek to come up with a further test to deal with that. We took the approach that the logic of the basic test is that it does not -- I think you have got our submission on the point. I see entirely what you are saying, sir - that that particular charge is, of course, the one that is the focus of the problem that was caused. The others, both on Step 1 - gains from trade and benchmarking - are okay. But, we did proceed to deal with the H3G charge in the price controls that were then set. We knew by the time of the determination that we already had. I appreciate you say that that does not deal with it under the determination for that period. That is correct. I do not think I can take that further.

PROFESSOR BAIN: Thank you.

MR. ROTH: Madam, can I move on to deal with Article 10 of the Treaty? A separate head. You will recall that the argument here again concerns specifically, I think, the H3G charge. As I understand it, that was the focus of it. What he said, you will recall, is that this charge is so high ----

MR. COOK: Can I just clarify? This is not a point that solely concerns H3G by any means. As you will know, our point is that the blended rates conceal - and Ofcom should properly have been aware that they concealed - excessively high charges by everybody for 3G. H3G is exposed simply because it does not have truly blended charges .We say that all of the 3G rates were excessive, and that was something that Article 10 applies to all of them

MR. ROTH: Thank you. That is very helpful clarification. I can deal with that shortly in just a moment.

If I deal first with the blended charge, and then with the point that Mr. Cook has just clarified -- I am sorry. I had not understood it clearly. The blended charge is the charge that BT is being asked to pay by H3G. On that I think it is said that that charge, just looked at as a price to BT before you think about anything underlying it, is so high that it appears to be significantly above the competitive level and therefore excessive in terms of Article 82; that Ofcom cannot approve a charge, or set a charge, which involves an undertaking breaching competition law, since that would flout the duties of Ofcom under Article 10 of the treaty. I think that is the point, as I understood it. Mr. Cook quoted my submission in the SMP appeal where I say, "Well, the proposal by Hutchison to introduce that price was a demonstration of the exploitation of market power", and he said, "Well, there you are. Mr. Roth has said it himself". That was very much the H3G charge there which was being referred to.

Of course, Ofcom is subject to Article 10 of the treaty. If this would lead to a breach of Article 82 by the MNO introducing, or levying, that charge, the point would be a valid one. But, we submit that as a matter of law, on the facts of this case, it does not, and cannot, give rise to a breach of Article 82. The reason for that is explained in the reasoning of the Court of Appeal in the *AtTheRaces* case. I emphasise that it is part of that long judgment which has nothing do to with the nature of the product - which is very special - or, indeed, the level of the charge. The court was addressing the proper interpretation of excessive pricing as a violation of competition law. Can I ask you to turn to *AtTheRaces* which is Bundle H2, Tab 14? It is a long judgment in a case of, if I may say, quite horrendous complex facts. You may possible, Madam Chairman, wish to note that it is reported at [2007] UK

Competition Law Reports, p.308. But, we have here the Westlaw transcript. If one goes in the judgment to p.17 in the print-out in a section that is headed "The Principal Legal Provisions", the court says in paras.100-101, and this is the judgment of the court:

> "The overall context of Art.82 and s.18 …"

– that is the Chapter II prohibition in the Competition Act –

> "… is important: to prevent distortion of competition and to safeguard the interests of customers. As Jacobs A.G. said in *Bronner v. Mediaprint*:
> '… it is important not to lose sight of the fact that the principal purpose of Article [82] is to prevent distortion of competition – and in particular to safeguard the interests of consumers – rather than to protect the position of particular competitors. It may therefore, for example, be unsatisfactory, in a case in which a competitor demands access to a raw material in order to be able to compete with the dominant undertaking on a downstream market in a final product, to focus solely on the latter's upstream market power and conclude its conduct in reserving to itself the downstream market is automatically an abuse. Such conduct will not have an adverse impact on customers unless the dominant undertaking's final product is sufficiently insulated from competition to give it market power.'
> In *Aberdeen Journals (No.2)* Sir Christopher Bellamy, the President of the Competition Appeal Tribunal, said:
> '… the question whether a certain pricing practice by a dominant undertaking is to be regarded as abusive for the purposes of Chapter II is a matter to be looked at in the round, taking particularly into account, (i) whether the dominant undertaking has had "recourse to methods different from those which condition normal competition in products or services on the basis of the transactions of commercial operators …" and (ii) whether such conduct has the effect of weakening or distorting competition in the relevant market, having regard to the special responsibility of a dominant firm not to impair genuine undistorted competition.'"

Then on the facing page under the heading, "Excessive/unfair pricing", the court in para.114 quotes from *United Brands*, the well known *dicta* as to unfair pricing and says in para.115:

> "Although it would be wrong to read this passage too literally, it must, in our judgment, be read and applied with care. We make the following points …"

It is the fourth point in para.119 that is the important one for our purposes here:

> "Fourthly, it has to be borne in mind that, as stated in *Bronner*, the law on abuse of dominant position is about distortion of competition and safeguarding the interests

of consumers in the relevant market. It is not a law against suppliers making 'excessive profits' by selling their products to other producers at prices yielding more than a reasonable return on the cost of production, i.e. at more than what the judge described as the 'competitive price level'. Still less is it a law under which the courts can regulate prices by fixing the fair price for a product on the application of the purchaser who complains that he is being overcharged for an essential facility by the sole supplier of it."

That is the enunciation of the principle, and one can see how it is then applied in this case. There were a whole host of issues in this case. This was just one of them. If you go on in the judgment to para.215 on p.29, which is the section of the judgment where the court gives its conclusions on excessive pricing, as you see from the facing page, and again there were a lot of issues as to whether the price actually was excessive, and so on, given the nature of the product. They go on in 215:

"This said, we accept that there is moral force in ATR's position …"

I should have explained, ATR were the buyer, BHB were the seller.

"… ATR adds value (in the form of pictures of the races) to the pre-race data and has the task of collecting overseas bookmakers' payments. It is taking all the risks and, as the judge found, will have to absorb most or all of the costs, while BHB seeks to take half of what they make. This may be thought to be unfair, but it cannot alone make it an abuse of Bib's dominant position. As Jacobs A.G. said in *Bronner* (cited above), the principal object of Art.82 of the Treaty is the protection of consumers, in this case the punters, not of business competitors. In our judgment, this is correct, even if it is the competitors and not the consumers who are alleging abuse of dominant position. We need to look beyond ATR's immediate interests to the market served by ATR. There is little, if any, evidence that competition in the market is being distorted by the demands made by BHB upon ATR."

There was then discussion of a hypothetical case of a monopoly wholesale supplier, and I think I can go on to para.217:

"We appreciate that this theoretical answer leaves the realistic possibility of a monopoly supplier not quite killing the goose that lays the golden eggs, but coming close to throttling her. We do not exclude the possibility that this could be held to be abusive, not least because of its potential impact on the consumer. But Art.82, as we said earlier, is not a general provision for the regulation of prices. It seeks to

prevent the abuse of dominant market positions with the object of protecting and promoting competition. The evidence and findings here do not show ATR's competitiveness to have been, or to be at risk of being, materially compromised by the terms of the arrangements with or specified by BHB."

That was one of the various reasons why the found no abuse.

MR. SCOTT: Just sticking with this, if you look at para.218, the criticism of the judge is:

"For all the above reasons we conclude that, in holding that the economic value of the pre-race data was the cost of compilation plus a reasonable return, the judge took too narrow a view of the economic value in Article 82."

Yes? Here we are in a rather different situation because, as we have established earlier on, the economic value here, we are looking at an ordinary voice call termination to which 3G is adding no value – in other words, we are not talking about a product in the sense that *Attheraces* is talking about a very specific sort of product, with a very different sort of economic value to a voice call. Are you suggesting that we can read straight across from the facts here and the criticism of the judge here into an ordinary bog standard voice termination?

MR. ROTH: There were two quite distinct issues – there were more than two – two relevant ones for this purpose in *Attheraces*. One was that the judge had got economic value of the product wrong. That turned on the nature of the product, what is meant by economic value. We do not rely on that, that is of no relevance here. That is summed up in that paragraph. The other issue, or another issue, was that the judge had found abuse simply because he concluded that the price was materially above the notional competitive value and said, "Excessive, therefore violates Article 82", and that was wrong because Article 82 is not simply seeking to control excessive prices. There is only an infringement (and that is *Bronner*) if it harms the interests of consumers and produces a distortion of competition. That is the separate point, and it is a wider point that we rely on. The first point, as you identified, sir, is of no relevance in this case.

MR. SCOTT: Thank you.

THE CHAIRMAN: So this takes you back then to the particular circumstances of this case where the high price was not actually passed on to consumers, and hence there was no consumer detriment in the same way as it is said here. So it is a sort of *GlaxoSmithKline* point as well, that because competition law is looking at protecting consumers, there may be exceptional circumstances in which conduct which is generally thought of as being an infringement is

not actually an infringement because there is no impact on end users, only an impact on someone within the chain.

MR. ROTH: That is right, madam. I think one has to go a little bit further at one point, but also one has to say no material effect on competition. The fact that the purchaser has to pay a price, which seems a high price, to the seller and the fact that the seller, like BHB, can demand that price because it is a monopolist, that does not mean that Article 82 is infringed. You have to consider (a) any adverse impact on consumers, does it have a material effect on competition – I have got to come to that, Professor Bain's ----

PROFESSOR BAIN: You are about to come to whether it has a material effect on competition.

MR. ROTH: Because that also clearly is an element. Here, as regards consumers, I think you have got the point, the requirement that BT pay retrospectively to H3G. Even if the charge were appreciably above the competitive level it does not have any impact on consumers. Of course it costs BT money just as in this case the charge from BHB to Attheraces cost Attheraces a lot of money, but that was just a transfer from one to the other and it does not impact forward.

As regards the effect on the competitiveness of BT, who are the payer, the evidence is put that the MNO charges have an effect on BT vis-à-vis its transit customers because of its reclaiming of the charge from the transit customers, that it is asking them to pay and it is an attempt to recoup. The evidence that is given on that is entirely general. It is not linked specifically to the level of the H3G charge, it is because BT has sought to recover, it seems, all or a large part of all these charges from the MNOs from its transit customers. T-Mobile, we heard, have been asked, subject to that, for example.

So it has not just restricted to the figures in the BT witness statement to simply the result of H3G. I appreciate that Mr. Cook puts his point more widely and says it is the other charges as well. So I have to come to that.

PROFESSOR BAIN: I was just going to follow that up. Are you saying that the loss of revenue, net cost, BT handed to each of the Altnets and any other MNOs that were affected by this, you are saying that has no appreciable effect on competition?

MR. ROTH: Simply the fact that there is a transfer of revenue, no, does not, just as the transfer of revenue from Attheraces to BHB which left Attheraces with less money to compete with its competitors, that is not treated as an adverse effect on competition.

PROFESSOR BAIN: So if you take £3 million off a company that does not affect its ability to compete – an unexpected £3 million?

THE CHAIRMAN: Not sufficiently directly to give rise to ----

MR. ROTH: To distort competition. You need evidence of what actually it is going to do to that coming to the market.

PROFESSOR BAIN: You would not, as a matter of theory, expect it to distort competition?

MR. ROTH: It would depend on the size of the company. Mr. Cook made clear a moment ago, when I mis-stated his position, for which I apologise, that the point is made not just only as regards H3G where it is most striking, but also, and from which he used my quotation from the earlier case, as regards all the MNO charges because he says the underlying 3G element is high. With respect, the answer to that is simple. When one is considering whether there is an abuse of dominance or indeed excessive pricing for the purpose of Article 82 the focus is on the price that the purchaser is being asked to pay and whether that price is appreciably above the competitive level. If that price is not appreciably above the competitive level the fact that some element that goes to make up that price might have been calculated at a very high figure is irrelevant. You do not start unpacking the price that has been charged to the customer and say, "Let us look at each of the ingredients put in it and see whether there is a high profit margin or this or that". What you look at is the price the customer is being asked to pay, and is that appreciably above the notional competitive price. That is the test. So that point just does not arise.

MR. READ: Madam, can I just interject at this point to say one thing. We do not necessarily accept everything Mr. Roth says about the characterisation of our evidence. I am not going to take up time going through it at this point, but we will be picking it up in reply, so I would not want the absence of me saying anything now to be assumed that we necessarily accept the submissions that Mr. Roth has been making about the effect of our evidence is correct.

THE CHAIRMAN: Thank you, Mr. Read.

MR. ROTH: Madam, finally I come to the question of cross-over with the SMP appeal. Miss Dinah Rose yesterday towards the end of her brief submissions, which I have to say said very little about her own client's position as to what MCT rate should have determined in the various H3G disputes, which it is actually the appeal at this stage that is before you. The position that H3G take in their notice of appeal is a somewhat complicated one on that, and harks back to their position in the SMP case. It is at bundle D1, tab 1, bundle page 29, and a lot is said about Ofcom failing to take account of the wider impact on the market, which leads to the conclusion in para.9.4:

> "Ofcom's approach … is therefore founded on an incomplete and inadequate understanding of competitive interaction in the mobile market, and is

consequently contributing to an important, welfare-reducing distortion of prices – off-net versus on-net price differentials …

9.5 For, *inter alia* the reasons stated above, alter entrants and smaller operators, in particular H3G, make a loss and effectively subsidise …"

and so on. Then at the end of that paragraph:

" As part of its dispute resolution powers, Ofcom should have investigated this critical issue or at least discussed it further with H3G before dismissing it. It failed to do so.

9.6 H3G also submits Ofcom could and should have taken these market dynamics into consideration in its assessment of the disputed 3G MCT rates."

They basically say that either we should have fixed rates at zero pence per minute, which:

" …would address the distortions to competition caused by the current substantial net outpayments that H3G has to make to its competitors. Another way of achieving this would have been for Ofcom to resolve the disputes so as to set asymmetric MCT rates."

Those are the two alternatives that are there being put forward for all the reasons that are being discussed above. We say that would be wholly inappropriate in the context of dispute resolution and I think their position is that is what should have been done for H3G, but asymmetric rates – unless it is zero pence per minute – that would, I suppose, come within Professor Bain's question of "… well, go outside what the immediate parties have said to you and take a different solution for regulatory grounds." I think for the others it is said it would be a cost-based rate using what is in the 3G MCT statement.

Miss Rose really directed her submissions, in attacking Ofcom's position rather than seeking to support the notice of appeal, and said our position here is very odd in the determinations given what we say in the SMP appeal. You may recall she said that she awaits to hear from me how we reconcile them. I do not want to disappoint her, the answer is very simple: you will recall that in the SMP appeal I said that I will explain in this appeal what Ofcom says is the proper approach to take in the determinations, and I parked it rather than going into it there. Well I have sought to do that and explain what we say is the right approach, and say that Ofcom should not be fixing a cost-based MCT on the MNOs. Whether by direct application of the MCT statement for an earlier period, or by Mr. Turner's extrapolated glide path that one should use the gains from trade test, and that the focus is on the reasonableness from the perspective of BT. If Ofcom is correct in that, and if that is the way that dispute resolution is properly applied in this regulatory context, then it

does not operate so as to control the significant market power of MNOs, as Professor Bain's questioning of me graphically brought out, so it does not prevent SMP.

But, if Ofcom is wrong on this and if, on the contrary, the dispute resolution powers should be used to set a cost based charge or otherwise in a manner that precludes exercise of significant market power by the mobile operators, or H3G in particular, then indeed it would be regulating the mobile network operators' charges and so that form of regulation falls to be disregarded in determining whether or not H3G has significant market power for the purpose of Article 16 of the Framework Directive on the proper interpretation of the Tribunal's 2005 judgment, and to avoid circularity.

THE CHAIRMAN: That is the modified Greenfield?

MR. ROTH: Indeed, and para.138(b). I refer to our defence in the SMP appeal, paras. 89 to 90 and 97.3, and para. 16 of our skeleton argument, where we put it in that alternative way, saying that if our approach is correct then it has to be another approach that does control SMP to disregard it, and so it is entirely consistent.

Would you give me just a moment? (After a pause) I was just checking with my clients, subject to any further questions, those conclude my submissions.

PROFESSOR BAIN: Mr. Roth, I would like just to ask you a little bit more about the use of costs as a basis for a separate termination rate dispute. Is it Ofcom's position that even if they were to take some account of costs, that would not necessarily imply that they had to determine the rate solely on the basis of costs? I am thinking of the linkage between this appeal and the SMP appeal. Ofcom's position at the moment is that they do not have to take account of costs.

MR. ROTH: Yes.

PROFESSOR BAIN: But if they did take some account of costs would that, in Ofcom's view, be the same as determining on the basis of costs?

MR. ROTH: May I just take instructions? (After a pause) The answer is "no", it would not. The problem Ofcom had was what criteria would be sufficiently precise as to how to do it? That is the difficulty that is presented. In general terms, fine, as it were, but how do you develop precise criteria that enables one to do it in a way that enables you to come up with a precise price?

PROFESSOR BAIN: Well I understand that it may be difficult, but thank you for the answer.

THE CHAIRMAN: Thank you very much, Mr. Roth. Perhaps we will take a break for five minutes before we move to the interveners.

(Short break)

MISS DEMETRIOU: Madam, Mr. Wisking, for Vodafone, and I have tried, insofar as possible to liaise in an effort to reduce repetition. As is clear from Orange's statement of intervention, it supports Ofcom in respect of all the core TRD issues with the exception of the SIA claw-back issue in respect of which it supports the Altnets. So, what I am going to do in the space of time I have available is to confine my oral submissions to the question of Ofcom's dispute resolution powers. But, I should make clear that we adopt Ofcom's submissions in respect of all issues other that SIA and claw-back.

In short, Orange submits that Ofcom was not obliged to set cost based charges for MCC in resolving the BT and MNO disputes. On the contrary, we say such a determination would have been entirely inappropriate as it would have amounted to the retrospective imposition on the MNOs of the most draconian form of regulation permitted by the CRF, and that in circumstances where Ofcom had decided in its last market review not to regulate 3G MCT, and in its contemporaneous market review to regulate such prices with prospective effects from 1st April, 2007l as, indeed, we say was appropriate.

We say that for those reasons, in short summary, the consequence of the appellant's arguments is not to advance the CRF, but to undermine its proper application. I would like to break down my submissions into three parts. The first deals with the purpose of a dispute resolution procedure. The second deals with the Article 8 of the Framework Directive arguments. Thirdly, and finally, I would like to briefly touch upon the end-to-end connectivity obligation.

I will start with the purpose of the dispute resolution procedure. We say that the purpose is quite clear - insofar as the dispute procedure arises under Article 5(4) of the Access Directive, it is to ensure access and interconnection, and insofar as it arises under the Framework Directive, it is to resolve disputes arising in connection with obligations arising under that directive or the specific directives between undertakings.

In other words, the purpose of dispute resolution is to resolve deadlock between two undertakings where such deadlock either threatens interconnection or access, or where it concerns a regulatory obligation. The purpose of the procedure is, conversely, not to address market conditions in general, and not to address SMP. That is subject to a separate procedure with particular substantive and procedural requirements. Madam, the tribunal will be well aware of what those requirements are, but, in short summary, a market analysis is required to determine whether the market is effectively competitive (Article 16 of the Framework Directive). If it is effectively competitive, then the NRA cannot impose price controls (Article 16(3)). If the market is not effectively competitive, then the NRA must

identify undertakings with SMP. There are then fairly detailed consultation requirements and co-operation requirements (co-operation with the Commission) laid down by Articles 6 and 7 of the Framework Directive. Then, finally, once all of that has been gone through, Article 13(1) of the Access Directive provides that the NRA has a discretion to impose price control on an undertaking with SMP, but only where a market analysis indicates that a lack of effective competition means that the operator concerned might sustain prices at an excessively high level, or apply a price squeeze to the detriment of end users.

We say that observation of these requirements are of the utmost importance, particularly where the imposition of cost based price controls are contemplated given the draconian nature of such controls. I think this is the only provision that I am going to ask the tribunal to turn up because you are well familiar with the directives by now. If you could just turn to Recital 20 to the Access Directive at H1, Tab 4. Recital 20 summarises the position under the CRF, and says that

> "Price control may be necessary when market analysis in a particular market reveals inefficient competition".

So, the first point is that it is not necessarily required, even when there is inefficient competition. Then it says,

> "The regulatory intervention may be relatively light [and it gives an example] or much heavier, such as an obligation that prices are cost-oriented to provide full justification for those prices where competition is not sufficiently strong to prevent excessive pricing".

So, you see there that not only is there a discretion not to impose price control - even if the market is not effectively competitively - but if the NRA decides to impose a price control there is a range. What is being contemplated by the appellants in this case is the most extreme form of price control - in other words, cost based price control.

We say that given the very draconian nature of that price control, safeguards -- the procedural and substantive requirements laid down by the legislation must be strictly observed before they are imposed.

PROFESSOR BAIN: What do you say that the word 'reasonable' is meant to mean in Recital 20? The obligation that prices are 'reasonable' ----

MISS DEMETRIOU: The reference to 'reasonable' is a reference to Directive 97.33

PROFESSOR BAIN: Absolutely, but one of the questions before us is: What does 'reasonable' mean?

MISS DEMETRIOU: That is right. We say that 'reasonable' in this context has to be adjudicated depending on the context. We say that in this context Ofcom was quite right to focus on the end-to-end connectivity obligation which included a requirement of reasonableness which we say Ofcom had a margin of discretion as to how it assessed reasonableness. But, what 'reasonableness' does not mean is cost based price control because we say that that is inconsistent with the purpose of the dispute resolution procedure. So, 'reasonable' can depend on context, but in this context it does not mean the imposition of cost based price control.

THE CHAIRMAN: You do not accept that there is anything in between those two positions, taking cost into account, but not quite as 'orally' (if I can put it like that) as one would in a thorough SMP review.

MISS DEMETRIOU: Madam, in the circumstances of this case we say that that would have been inappropriate for the reasons which Ofcom gave in its determinations. I am slightly foreshadowing what I was going to come on to say, but -- It had expressly determined that for the period in question cost based price control was inappropriate. Now, there may, in theory, be other circumstances in which it might be, depending on the factual circumstances, appropriate to take costs into account. But, that is not this case.

We say that the dispute resolution procedure - looking at its purpose and the way it operates - is manifestly ill-suited to addressing SMP and to imposing cost based price controls. We say that is so, given especially (a) its short duration (and I will not labour that point because the tribunal has it well in mind); (b) the absence of any meaningful consultation requirements; and (c) its focus on a dispute between two undertakings rather than assessment of the market as a whole.

If I can just illustrate that a little further by reference to the facts of Orange's own case -- Now, the tribunal will have well in mind from the Orange preliminary issues ----

THE CHAIRMAN: Some of us will. The two wing members were of course different for the Orange preliminary issue, as these wing members remind me from time to time.

MISS DEMETRIOU: That has not gone unnoticed from my perspective. I am not assuming too much knowledge. I can just summarise the short point I want to make in this way: BT, of course, initially agreed in Orange's case agreed Orange's blended rate. It had commercial reasons for doing so. Perhaps I could ask the tribunal - and this is the last document I will ask you to turn up - to turn up the Orange judgment in Bundle H2 at Tab 21, p.10 para. 24 on p.10. That is an excerpt from the witness statement filed on behalf of BT - Mr. Colin Annette's witness statement. He explained there why, in the first place, BT accepted

Orange's charge and then why it changed its mind. You will see from the first of the paragraphs quoted that BT accepted Orange's charge because it was in commercial negotiations with Orange over a completely separate and very substantial project. BT was therefore inclined, in all the circumstances, not unnecessarily to rock the boat with Orange. There were also other commercial reasons why BT thought it might, in all the circumstances, be appropriate to accept the rates. However, the second major factor was that only Vodafone and Orange had so far sought a price rise. So, the tribunal will see there that there are a number of commercial reasons that BT referred to for it having accepted Orange's blended rate.

It does not take much of a stretch of one's imagination to see that BT may, for similar commercial reasons, have opted -- decided not to issue its own counter-OCCN, but to continue paying Orange's blended rate. If it had decided to carry on paying Orange's blended rate, then one would have been in a position where, for example, T-Mobile's dispute with BT would have been referred to Ofcom, but BT would have continued paying Orange's blended rates.

Now, if, in those circumstances, Ofcom was required to resolve the dispute between BT and T-Mobile by setting a cost based price on T-Mobile, then one would have ended up with asymmetric regulation on Orange and T-Mobile with absolutely no substantive justification for that kind of asymmetric regulation. I just make the point to illustrate that the dispute resolution procedure, which is dependent -- which focuses on a dispute between two undertakings, and is dependent on the commercial backdrop -- So, in particular, whether or not BT is commercially motivated to object to a price and refer a dispute -- can lead, because of the nature of that procedure, to unacceptable results if Ofcom is required, in dealing with the disputes before it, to impose cost based price regulation on the MNOs whose disputes happen to come before it. We say that is just an illustration -- It may be hypothetical, but it is not too far removed from the facts of Orange's case.

THE CHAIRMAN: Could that not work the other way as well? In any situation where the purchaser refers one dispute but not another, you may end up with different prices because one dispute is resolved by the regulator and one is not. Could it not also work that if T-Mobile in your circumstance had decided to set a cost based price, and that was accepted by BT, and Orange had decided not to set a cost based price, set a much higher price, say, and that had been referred, and if the regulator then applies the gains from trade test and approves that, you would then be in an asymmetric situation.

MISS DEMETRIOU: Madam, with respect to your first point, I would say that it is a different matter to impose. It is true that if the market is left to its own devices you may have different prices charged by different operators. In resolving it, if a dispute between BT and one operator is referred, then we say of course Ofcom has to resolve that dispute between them and that may result in a different price to a price that another operator is charging. So to that extent different prices are being charged. That is different to saying that Ofcom should asymmetrically regulate one MNO as compared to another.

We say that the dispute resolution process, because it focuses on bilateral relationships is ill-suited to the imposition of regulation on the MNOs. That is really the long and short of the point.

MR. SCOTT: Am I right in saying that if Ofcom concluded as a result of a dispute which related to one or more of the MNOs that an unsatisfactory situation had arisen they could then take action under the first part of Article 5.4?

MISS DEMETRIOU: The first part of Article 5.4?

THE CHAIRMAN: That is s.105.

MR. SCOTT: That is the part which says intervene on its own initiative where justified.

MISS DEMETRIOU: We say that if it wants to intervene to impose price controls because of SMP, because of ineffective competition in the market ----

MR. SCOTT: That point I understand. Ofcom has to resolve a dispute that comes before it.

MISS DEMETRIOU: Yes.

MR. SCOTT: In the second part of 5.4 the dispute comes before it because of the parties.

MISS DEMETRIOU: Yes.

MR. SCOTT: So Ofcom does not have a choice, but it does have a choice in relation to the first part of 5.4, and because of its awareness of what is going on in this arena it would know if a distortion had resulted from a decision it had taken in relation to some but not all MNOs.

MISS DEMETRIOU: So the point that you are putting to me is that Ofcom has the power to correct a distortion through this mechanism?

MR. SCOTT: Yes.

MISS DEMETRIOU: I can see in theory that it would have a power to correct the distortion, but we say this really is not the right process for doing it. If Ofcom sees that there is a problem generally in the market with uncompetitive prices then the way forward is to address it through the SMP provisions which are directed at addressing precisely that problem. We see that it would be rather unsatisfactory and cumbersome if Ofcom had to correct distortions in the market arising from its resolution of a particular dispute by exercising its

Article 5.4 powers to intervene at its own initiative in the relationships of the other MNOs and BT. That is a rather cumbersome way of achieving regulation in the market when there is a perfectly straightforward mechanism which had various substantive and procedural safeguards specifically designed for achieving that result. That is not really what the purpose of the first paragraph of Article 5.4 is. We say that that is the most obvious purpose of that provision. It is to intervene, for example, where there is no dispute between the parties but Ofcom sees that there is an absence of interconnection between particular operators and that is having a negative impact.

Just to summarise on this point about the purpose of the dispute resolution procedure, of course we do not say that it follows from my submissions that Ofcom has no power when resolving a dispute to set a price for an undertaking that has SMP, because that is plain from the first H3G judgment. What we do say is that its purpose in setting a price is to resolve a bilateral dispute and to prevent deadlock, and it is not to address SMP. That in turn has substantive consequences for the way it approaches the dispute.

The second issue that I wanted to address is Article 8 of the Framework Directive. This, on analysis, turns out to be the main plank of the appellants' arguments. They say that in not setting a cost based MCT price Ofcom failed to give effect to the objectives of the CRF as contained in Article 8. What we say to that is that this argument really assumes what it sets out to prove, because it assumes that the Article 8 objectives would only have been fulfilled by the imposition of cost based price control on the MNOs. We say that assumption is wrong, and it is wrong for a number of reasons.

First of all, as the tribunal is aware, Ofcom had already taken a positive decision in its 2004 statement not to regulate 3G call termination during the period covered by these precise disputes. We say that it gave a number of reasons for taking that decision and the tribunal has already been taken to those reasons in the 2004 statement. Those reasons are perfectly consistent with Article 8. In fact, Ofcom specifically directed its mind to the Article 8 questions and decided that it would be disproportionate to regulate 3G charges. We say, how can it be inconsistent with Article 8 to give effect to that decision in these disputes? We say it cannot.

Then we say, secondly, the appellants' submissions ignore the context of Article 8, which include, firstly, a starting point of light touch proportionate regulation and the NRA should only intervene to resolve a dispute where commercial negotiation fails. We have already seen Recitals 5, 6 and 20 of the Access Directive make that point. Secondly, there are the substantive and procedural safeguards which apply, and I have already addressed those.

Thirdly, Article 8 itself and the implementation of Article 8 in the domestic legislation also requires NRAs to act proportionately, consistently and transparently. We say that these requirements would not have been fulfilled if Ofcom had imposed retrospective cost based price controls on the MNOs after it had positively reviewed the situation and decided not to impose price controls on 3G calls until April 2007. It had consulted on that very point and everybody had put in their responses to the consultation. So we say that it would have been completely contrary to the principles of proportionality and consistency and transparency to then backtrack and retrospectively do what it said it was not going to do.

I can illustrate that quite briefly by reference to the facts of the Orange case because the dispute between BT and Orange arose in July 2006, BT having agreed on 3rd July to Orange's rate and then disputed it later in the same month. At that time what we had in place in terms of Ofcom's statements were that it had in its 2004 statement expressly decided not to regulate 3G call termination. A year earlier, so in the summer of 2005, it had expressly recognised that the MNOs could set blended rates, so it had flagged that up. Then in its consultations ----

THE CHAIRMAN: In the summer of 2005, the blended rates, which consultation was that?

MISS DEMETRIOU: That is the preliminary consultation which is at F1, p.303. The position is summarised at para.1.11, p.306 of F1.

THE CHAIRMAN: Thank you.

MISS DEMETRIOU: Then we see in the September 2006 consultation, which is before the dispute between BT and Orange was actually referred to Ofcom, Ofcom was consulting on the possibility of imposing charge controls with effect from 1st April 2007. That was the understanding of all the players in the market.

THE CHAIRMAN: Was it saying that it expected that between September 2006 and April 2007 it expected that the market was going to change in some way to make it appropriate to impose regulation as from April, or was it saying that as at September 2006 its assessment of the market was that the market had changed and was different, and that was going to convince it to apply regulation from 1st April?

MISS DEMETRIOU: We say it certainly had not reached any concluded view, and that was the very purpose of the consultation, but Ofcom had of course recognised that the market was changing and that the considerations which led it not to impose 3G price control back in 2004, that those considerations had developed and that the market was changing. We do not say that it had reached any concluded view in September 2006. Indeed, that would have been inappropriate because it would have rendered the whole consultation irrelevant. This

was the purpose of consultation. So Ofcom had its preliminary view but it was consulting to see whether, in fact, it would be appropriate to regulate on a forward looking basis.

MR. SCOTT: You say that the fact that in September 2006 the E2E statement comes out is neither here nor there?

MISS DEMETRIOU: It is relevant to the substantive manner in which Ofcom determine the dispute, because obviously that was a regulatory obligation in place which Ofcom had to look at in order to resolve the dispute before it. So it is certainly relevant to that extent. I do not know if that is the question you are asking.

MR. SCOTT: What has been argued is that that produces an obligation which then activates part of the common regulatory framework and its UK manifestation. I think your argument is that it does not make any difference that that changes in September 2006.

MISS DEMETRIOU: No, it only makes a difference to the substantive approach employed by Ofcom once it comes to determine the dispute. So what principles does it apply in determining the dispute between these two parties? Then, because this regulatory obligation is in play, Ofcom has to look at it. That is why, we say, it correctly focused on the question of reasonableness.

Just to deal very quickly with one or two of the specific arguments made on Article 8 by the MNOs, Mr. Cook argued that Ofcom had been too MNO-centric in approaching the dispute, and that a proportionate Article 8 compliant approach would have set the lowest possible price which would still ensure interconnection. We say, in short, that that ignores the starting point which is commercial negotiation. That is again illustrated by the facts of Orange's case, which is that commercial negotiation had actually taken the parties quite a long way. As we have seen, BT freely, for a number of commercial reasons, initially accepted Orange's rates. We say that that is precisely the type of commercial negotiation that the CRF seeks to encourage, and it is only when that breaks down that the dispute resolution powers require Ofcom to step in. It would be entirely disproportionate to step into a commercial dispute in circumstances where in Orange's case BT had actually accepted the rate and then imposed cost based price control on the MNOs. We say that is the flaw in that argument and that goes back to the purpose of the dispute resolution powers.

MR. SCOTT: Sorry to interrupt you again, but Ofcom's decision is predicated against the fact that there was not harm to consumers, but in the situation that you are suggesting there could have been because had BT accepted a high Orange rate ahead of anything else happening it would have been inclined to consider putting up its charges to reflect that higher rate.

MISS DEMETRIOU: It did accept it for a while. There is no evidence that it did put up its prices for the brief time in which it accepted it.

MR. SCOTT: The brief time is the important point there, because of course the next statement comes in. In the abstract, thinking about what you are saying, there could have been an impact on consumers had that managed to stay in place and not been overtaken by other events.

MISS DEMETRIOU: We would say that is unlikely, given what actually happened in this case which is that the higher rates were paid by BT over the period of time whilst the disputes were being considered and they did not put up their prices to consumers and we say that is not what happened in this case, and Ofcom had to consider what actually happened in this case which is that there was not a detriment to consumers.

Just turning to Mr. Turner's arguments. He recognises in Ofcom's favour that the dispute resolution procedure is inadequate for a full market analysis, and therefore he based his argument on the fact that Ofcom had already done the work required in the context of the MCT review (transcript day 7, p.11, lines 19 et seq) When madam chairman asked Mr. Turner whether Ofcom would have been under the same obligation to impose a cost base price, even if they had not been undertaking an SMP review, he said "not in the same way". First of all we say that is unsatisfactory in terms of giving guidance to Ofcom as to precisely what its requirements are, but secondly and fundamentally, we say that that is tantamount to arguing that the question whether Article 8 substantively requires the imposition of a cost based price turns on the existence and timing of a market review, and we say that cannot be right, so either Article 8 substantively requires the imposition of a cost based price or it does not.

THE CHAIRMAN: Well does Ofcom not also say that the coincidence of it affects the substantive test because it is the coincidence of the market review imposing a price as from 1st April that means that this charge is considered retrospectively only.

MISS DEMETRIOU: Madam, that is right, but Mr. Turner's point is that retrospectively Ofcom should have essentially imposed the price controls that it did on 1st April retrospectively. I am making the point that his submission is fairly limited in ambit because he is presumably not saying that Article 8, as a matter of substance – because it refers to the promotion of competition etc – requires whenever a dispute comes before Ofcom for it to resolve it by ensuring that the prices are perfectly competitive. He is not saying that because he recognises in Ofcom's favour, that that is unworkable, given the limitations of the dispute resolution procedure. That seemed to be very close to what Miss Rose was saying in the

context of the SMP appeal, because it seems to me logically that for the purposes of demonstrating that H3G has no SMP really she needs to show that every time a dispute comes before Ofcom, Ofcom will resolve it by setting a cost based price. I am simply pointing out that there is a divergence between the positions of the appellants in this respect, and that Mr. Turner certainly does not go so far as to say that, and neither do BT or the Altnets.

Finally, we say that Mr. Read responded to Professor Bain's question concerning the ambit of the particular dispute in hand, and the Tribunal will recall this question as to where the two undertakings concerned are arguing about price within a particular range does Ofcom have the power to go below that? Mr. Read said he doubted that it would be open to Ofcom to fix price below the range of the dispute between the parties (transcript day 6, p.60 lines 20-22). We say how is that consistent with BT's Article 8 argument? Because if Article 8 requires the imposition of a cost based price then surely it requires it, it cannot depend on the ambit of the particular disputes in any particular case, because that is a matter of chance.

Those are the short points I wanted to make on the arguments of the appellant, and I will just end very briefly by reference to the End-to-End Obligation. Mr. Read again stated in terms that BT is not arguing that the End-to-End Obligation is unlawful, and he said that the actual wording of the End-to-End Obligation with the reasonableness proviso is perfectly adequate to secure the CRF objectives (transcript day 6, p.31, lines 23-30) and we agree with that. But, he then went on to say that Ofcom misconstrued the End-to-End Obligation because they had focussed on "the bare functionality of the requirement on BT to purchase interconnection as divorced from the price on which the interconnection was offered. We say that that is wrong, Ofcom did focus on the price that BT was required to pay, but it did so by properly applying the End-to-End Obligation which provides that BT should only be required to interconnect at a reasonable price.

We say that the consequence of the appellant's arguments on the other hand is in effect to rewrite the End-to-End Obligation, so as to replace the word "reasonable" with "cost-based price", and that mis-applying the End-to-End Obligation we say. Mr. Wisking, I know is going to make slightly more detailed submissions on the End-to-End Obligation and I agree in anticipation with his submissions. (Laughter).

In conclusion we say that the imposition of a cost-based price control on Orange would have been wholly inappropriate and unfair, and in particular we say that that is so given the factual circumstances of Orange's case, whereby BT had recently accepted Orange's rate in the context of a commercial negotiation. Secondly, there was no relevant regulatory

obligation on Orange in play. Thirdly, Ofcom had taken a positive decision not to regulate Orange's 3G rates before April 2007. Fourthly, that was a considered decision following a market review and a decision which Ofcom kept under review; and finally, the prices imposed on Orange with effect from April 2007 were imposed prospectively, as is appropriate, and were subject to a glide path in order to mitigate their impact. So the imposition of retrospective price controls, in respect of calls terminated before April 2007 would have been entirely inconsistent with that decision.

Unless there is anything further, madam, those are my submissions.

THE CHAIRMAN: Thank you very much, Miss Demetriou. Mr. Wisking?

MR. WISKING: Unfortunately going last means that most of the things I wanted to say have been canvassed one way or another. I have a note which I am just circulating which sets out the points that I want to make, and should mean that we should be finished before lunch. I am in the unusual position of an MNO that is actually supporting Ofcom's determination that its charges were reasonable.

Our position is – from our statement of intervention in respect of the core issues – that with the exception of the SIA claw back issue Vodafone supports Ofcom, and as such I adopt the submissions Mr. Roth made this morning and yesterday with the exception of that one issue.

We also rely upon paras. 32 to 36 of our statement of intervention in respect of the non-price control matters which were elaborated in submissions in the MCT hearing, and we adopt Miss Demetriou's submissions made just now.

What I would like to do is to deal with three issues: first, really to reiterate the points previously made about the correct construction of the E2E Obligation. Secondly, covering the same ground as Miss Demetriou, to explain why in our view we think that Ofcom took the correct approach in not seeking to resolve these disputes by the use of cost-based charges; and thirdly, just to come back to some aspects of the determinations.

As a preliminary point I was going to make the point which Mr. Roth covered extensively, that these disputes are essentially historic; they relate to the period up to 31st March, so I do not need to say any more about that.

On the question of the construction of the E2E Obligation, our position is that on its proper construction it requires BT to purchase interconnection at any higher price which a terminating operator may request subject to an upper bound beyond which the price would be unreasonable.

We have previously submitted that that construction is supported by a number of factors which are set out in the note at p.2 that in essence the specific purpose of the E2E

Obligation, the fact that the E2E Obligation itself contains no reference to cost-reflective or competitive prices, or price setting methodologies along those lines, when obviously Ofcom could have done so had it thought it proportionate to secure interconnection.

Thirdly, and it is a point that Mr. Roth made yesterday, the deregulatory purpose of the Directives, so that operators without SMP are free to charge what they like, and obviously not all operators interconnecting with BT will necessarily have SMP. As Miss Demetriou has said, and I will come back to this, where there is SMP there is a specific regime within the Communications' Framework with its own procedure and protections for the imposition or modification of cost-based or price control conditions.

In addition, to interpret "reasonable" as requiring cost-reflective pricing would be tantamount to converting the E2E obligation into a price control on the MNOs, which Ofcom in its own consultation thought was disproportionate.

Finally, the overall regulatory framework, which again Mr. Roth referred to, is this idea that Ofcom has quite properly, within the Regulatory Framework, a regulatory toolkit which it can deploy in combination to achieve its objectives under the Directives. It does not need to use a hammer to knock in every single nail; it can use other tools.

One point that has emerged is whether because this interpretation is founded on the purpose of the E2E obligation, which is to secure interconnection, whether that is still relevant given that in this case ----

THE CHAIRMAN: Well is that the purpose, or could one say that the purpose is to secure interconnection at a price which has the effects that are required by Article 8 in sections 3 and 4? I wonder whether it is a semantic difference or a real difference. The purpose of the E2E obligation is not just to ensure interconnection, it is to ensure interconnection at a reasonable price, is it not?

MR. WISKING: It is to ensure interconnection at a price which can be up to the reasonable price, which can be effectively rapidly dealt with in the context of dispute resolution.

THE CHAIRMAN: So the upper bound that you referred to a moment ago, how does one arrive at that through the gains from trade test?

MR. WISKING: Well it comes down to this question of what is reasonable? What we say is reasonable could well be above the competitive price, it could well be above the cost-reflective price, because the primary purpose of the obligation is to secure interconnection in a way that can be rapidly dealt with in a dispute resolution context not, as I will come to, where you have to effectively force into the dispute resolution process an SMP-type review

in order to arrive at what would be a reasonable price assessed by reference to some cost-based measure.

PROFESSOR BAIN: Mr. Wisking, do you say that "reasonable" could also be below the cost- reflective price?

MR. WISKING: I am trying to envisage a circumstance where that would be the case.

PROFESSOR BAIN: A small MNO wishing to connect, if there was no obligation there BT could say "yes, we will connect at a very low price"? The E2E Obligation obviously weakens or eliminates their power to do that, but could a reasonable price be somewhere below the cost-reflective price?

MR. WISKING: That would raise wider policy questions as to whether it would be appropriate.

PROFESSOR BAIN: Could it perhaps – thinking historically – be a 2G price at a time that 3G costs were greater than 2G prices? Would that automatically be unreasonable?

MR. WISKING: I cannot exclude the possibility it would not be, but I think it would be very unusual for prices below cost to be reasonable. In any event, we say that notwithstanding the fact that in this case there was no threatened hiatus in interconnection, our interpretation of the end-to-end connectivity obligation still holds good, and that is because first of all it should be interpreted according to its original purpose and the paradigm case which it was intended to deal with. Secondly, it still remains the case that you want this higher level reasonable price as a basis for resolving disputes rapidly because, as we have seen from some of the issues that have been raised in this case by the Altnets, there is a very real problem if disputes go on for a long time; if you have people in a situation where they are acquiring services in circumstances where they do not actually know what they are going to cost, and then they had the problems in dealing with the adjustment that comes subsequently. So, even where there is no physical interconnection problem there is still a problem in the sense that you need to quickly come to a solution, and that is why it is appropriate to have this higher reasonable bound, rather than cost based charges.

MR. SCOTT: Is that true even if you have to hand cost based information, and so you do not have to conduct a separate exercise within the period?

MR. WISKING: We would still say for reasons that I would come to that that would not be an appropriate approach adopting Miss Demetriou's submissions about the proper approach to the regulatory framework.

The next heading is that we say that Ofcom was correct not to seek to resolve this dispute by setting cost-reflective or competitive prices. In part, that submission is based on the specific circumstances of this case; in part based upon construction of the regulatory

framework. The first point is that we say, as Mr. Roth has already submitted, that Ofcom was not obliged to pursue all of its duties through dispute resolution - it has other regulatory tools available to it. In this particular case, as we know, and as has been said, as of 1st April charge controls were applied on 2G and 3G termination.

The second point is that the regulatory framework, as Miss Demetriou has already said, contemplates that these type of price control conditions - and the words in italics at para. 9 of my note are actually taken from Article 13 -

> *'Conditions relating to cost recovery and price controls including obligations for cost orientation of prices and obligations concerning cost accounting systems'*

Are intrusive conditions which may normally only be imposed following either a finding of SMP or, in appropriate circumstances, to secure interconnection under Article 5(1). As I have said, for the reasons set out above we do not submit that the E-To-E obligation should be construed in a way that requires cost based charging.

THE CHAIRMAN: You say that you support Ofcom's submissions, but I am not sure whether actually what you and Orange are saying are consistent in that I understand Ofcom's submission to be that it could impose cost based pricing in the context of a dispute resolution in an appropriate case, but it just did not consider that this was an appropriate case for all the reasons that we have heard. But, are you saying that it would never, or rarely, be appropriate to impose a cost based price?

MR. WISKING: We are not saying never, but having regard to the regulatory framework it would be not the normal run of things. Also, given the dispute resolution process which, as has been said so many times, is a short, sharp way of quickly coming to resolution dispute, it would not normally be appropriate, or possible, or satisfactory to try and approach dispute resolution by reference to cost based charges.

THE CHAIRMAN: You heard what Mr. Roth said about cost based pricing and the circumstances why it was not used here. I am just trying to explore. Do you support that, or do you take a different, slightly stronger position?

MR. WISKING: We certainly support Ofcom's submissions as to why it did not use cost based charges in this case. In another case, it may be that Ofcom would say, "Look, this is an appropriate case for use of cost based charges", and we might differ with that. But, in this case -- You can see this dual approach in the domestic legislation. So, s.190, for example, contemplates that you can have dispute resolution and, as a consequence, move to a separate process of market review. You are looking at access conditions. So, the legislation contemplates that it is a different exercise. It may flow out of dispute resolution. It is

another tool, if you like, in the regulatory toolbox. It can be used together. They do not all have to be forced into dispute resolution.

In the particular circumstances of this case, the other thing is that we do have, from 1st April, regulation. To then, all of a sudden, at the last minute, to say, "Well, actually, we will apply it for the previous six months when no-one had that in mind" would be a complete by-passing of the procedures that had led up to the 2007 statement. Indeed, it would be effectively retrospective price control, which, as Ofcom has said, should be forward-looking.

Thirdly - and I do not want to go into the regulatory history any more than is necessary - again that makes clear that Ofcom was aware, first of all, because of asymmetric regulation of 2G and 3G rates that blended rates were possible and that blended rates could be higher than the regulated 2G rates. It also made clear that if there was an issue, the appropriate mechanism for dealing with that would be through an SMP price control condition - either modification of the 2004 statement or, as it in fact did, the 2007 statement. Ofcom being aware of that, it obviously thought it was appropriate not to take any steps until the 2007 statement. I set out in the note at 12(a) to (c) the regulatory history.

The fourth point is that dispute resolution is not really the right mechanism for setting cost based charges. In the present case, for example, the disputes took five months, which is longer than they should have done. That is nearly as long as the period of the disputed charges. Obviously SMP reviews take considerably longer. The appellants all urge that there are various lines of inquiry that Ofcom should have taken - perhaps necessarily even to somehow accommodate an examination of costs. That is going to take longer.

Obviously, in some cases the necessary cost data will not be available. In this case there may have been cost data available to Ofcom, but it was available for different circumstances. Again, that was provided in the context of the various consultations leading up to the 2007 statement.

THE CHAIRMAN: But is there not some evidence also that even apart from that, Ofcom, in anticipation of having to resolve disputes, had put together a costs model to use for this purpose?

MR. WISKING: I do not know whether that is the case or not. But, to use for what purpose?

THE CHAIRMAN: For dispute resolution. Perhaps I have mis-remembered that.

MR. WISKING: (After a pause): If that is the case, I can address that, but -- Indeed, the other point is that Mr. Amos, from BT, gives evidence that dispute resolution is not a commercially robust way of ----

MISS ROSE: Madam, just on that point, for the tribunal's note, there is such evidence at Bundle F1, p.287.

THE CHAIRMAN: Whose evidence is it?

MISS ROSE: It is a letter from Ofcom of 15th February, 2005 where they explain that they are developing a cost model, partly for the market review and partly to assist in resolving disputes.

THE CHAIRMAN: Perhaps if you can explore that ----?

MR. WISKING: Whether they did or not, they did not use it in this case. We say it would not be appropriate for all the other reasons that we set forth it would be appropriate to use in this case.

The final point is obviously that the disputes concern a very short time period. So, once again, there is the question of proportionality of gathering, considering, applying this sort of data.

Finally, I have set out some points in para. 15 about various aspects of the determinations. To some extent I think these have all been covered by Mr. Roth. The only point to highlight - as Miss Demetriou said in relation to Orange, and the same applies to Vodafone - is that actually there is no question of the application of pass-through as the charges in dispute allowed BT to make a margin. But, also, in fact in those cases BT was disputing existing charges rather than disputing attempts to increase charges. So, the outcome did not entail any reduction of BT's margins - it just meant that BT did not get the enhancement of margin which it would have obviously preferred had the price been reduced.

Unless there is any other way in which I can assist the tribunal ----

THE CHAIRMAN: There is just one factual question: When Vodafone first introduced the blended rate we have evidence that BT was not aware that it had done so. We have assumed from that that the blended rate fell below the maximum regulated 2G rate - otherwise, presumably, BT would have noticed that it was being charged at a rate above the regulated rate. Is that right?

MR. WISKING: No. My understanding is that Vodafone introduced blended rates from the beginning of the introduction of its 3G service, which was late 2004. From the start, the implicit 3G rate, if you like, was set at a slightly higher level so that the blended rate was slightly above the 2G rate.

THE CHAIRMAN: But, was the underlying 2G rate in the blended rate at the maximum that Vodafone could charge under the ----

MR. WISKING: Yes, apparently.

THE CHAIRMAN: Right. Thank you. (After a pause): Mr. Read, rather unobservant then of your clients, if that is the case.

MR. READ: The problem is, of course, that it is all dependent upon the volumes, and because the 3G volumes were so miniscule, without knowing the full figures and the full breakdowns involved it is not actually that easy to pick up precisely what is happening with the rates. That is the reason why, as I understand it, because we did not have a clear breakdown of the volumes in comparison to the rates, we were not in a position to work through the figures. Of course, that is compounded by the fact that for a lot of the calls BT would be acting as transit operator in any event and therefore would not necessarily know the precise figures involved. So, I think you are right, Madam Chairman, to assume that, but I also think it is right to say that BT cannot be accused of being incompetent for not having picked this point up earlier.

THE CHAIRMAN: It is simply that a lot of the tables that we see refer, for example, to the underlying 2G rate and then the headline regulated rate, without it being clear whether the 2G/3G MNOs have, at all times, charged the maximum that they can for the 2G determination. So, the underlying 2G rate and the blended rate equals the regulated 2G rate.

MR. READ: I do not think BT is ever in a position to know whether or not the MNOs have actually charged the maximum 2G rate they can because, of course, of the nature of the situation.

THE CHAIRMAN: I do not ask you specifically. I throw the question open if there is someone who can help ----

MR. READ: I think Ofcom knows because it monitors compliance. The answer is that they have always charged the maximum.

THE CHAIRMAN: They have always charged the maximum.

MISS ROSE: Madam, the point is, of course, that the regulated rate is a target average charge and different rates will be charged for day, weekend and weekday evenings, and BT will not know precisely what the volumes of traffic are that are being carried at each of those periods. So, therefore, BT will not be in a position to know, when you have got only a small blended 3G element, whether it is being charged the maximum 2G plus an additional 3G on top, which it was being charged, or not, because it does not know the volume.

THE CHAIRMAN: It might think that it is actually more daytime than weekend ----

MISS ROSE: Exactly - that it has been heavier daytime traffic.

THE CHAIRMAN: Right. But, Ofcom has all those figures and so it can check compliance with the ----

MR. ROTH: That is exactly right. We endorse what Miss Dinah Rose has just said.

THE CHAIRMAN: That is helpful.

MR. WISKING: I think the evidence is that BT knew from the beginning of 2006 whatever the case may have been prior to that ---- Unless the tribunal has anything else?

THE CHAIRMAN: Thank you very much, Mr. Wisking. Is there anything anybody wants to pick up on that? Mr. Roth, did you have something?

MR. ROTH: I will check something over lunch and then mention it. It will only take a minute or two.

THE CHAIRMAN: Thank you very much. We will resume then at five past two.

(Adjourned for a short time)

THE CHAIRMAN: Yes, Mr. Roth?

MR. ROTH: Madam, just two very short matters arising from what happened just before lunch.

First, reference was made to the letter from Ofcom to Hutchison of 15th February 2005. The reference is F1, p.287. That is the letter, you will recall, where Ofcom writes to H3G and says that Ofcom expects to hold a consultation for a 3G costs model in about six months time, distinct from the consultation on the market review. The position is that no such separate consultation in fact took place. In June 2005, as you know, there was the preliminary consultation on the market review. Thereafter, starting in about July 2005 and continuing, there were some workshops which all the MNOs attended, and indeed fixed operators as well. Then there was correspondence on costs modelling as part of the market review process. The costs model continued being developed and refined in the market review process.

THE CHAIRMAN: So the process that was envisaged in that letter was actually then subsumed into the market review process. Is that what you are saying?

MR. ROTH: Yes, subsumed. No separate process took place and it was subsumed into the market review and continued until the final costs model in the 2007 statement.

All these consultations, of course, are public documents.

Secondly, just coming back, if I may, on Professor Bain's question to Mr. Wisking, could a charge below cost be reasonable in the context of BT's End-to-End Obligation? Ofcom's answer is, no, Ofcom looks at the gains from trade not only for BT but also for the supplying MNO. The reference is the BT determination, para.7.12.

Thank you, madam.

THE CHAIRMAN: Yes, Mr. Cook?

MR. COOK: Madam, before I come on to the SIA issues there is actually one additional point that arose out of this morning that I need to deal with very briefly. That was the question about whether costs were passed on to end users or not, and that query. I pointed you to the statement in the witness evidence. Having taken further instructions from my client, the matter is actually somewhat more complicated than that. It is not simply a Cable & Wireless issue. In fact what we have in this case, and it arises from who is raising the OCCN in each case, my instructions are that in relation to Orange and Vodafone, because those are ones where BT initially accepted and then subsequently tried to lower, the transit price list would have remained in place at the higher price throughout the period. The transit price, I am instructed, did in fact change with the higher prices and then remained like that throughout the period. So in those cases my clients have borne the higher prices throughout, and that would have been reflected to one degree or another within their retail prices.

That is also somewhat true of H3G because, without obviously going into the numbers, we are in a situation in which there is an existing price. BT proposes a reduction in that price and H3G counter-proposes an increase in the price. The initial price continues throughout the period to be reflected in the carrier price list. Therefore, in all these situations, there is the situation where if Ofcom had accepted it was legitimate to lower the prices, in actual fact consumers were paying the higher price throughout the period. Certainly my clients were paying the higher price, and there is a factual question about the extent to which that would have been passed on entirely in relation to each of the customers in question. Of course we have the clear evidence from Mr. Harding of Cable & Wireless that in that particular case, and that was primarily its right to say their direct interconnection, that was expressly passed on.

It is always difficult in this circumstance to necessarily see a one for one pass on relationship because charges will be adjusted on a periodic basis and different amendments might be made depending on what the facts. There may be situations, particularly in this context in the telecommunications market where prices have, on the whole, decreased over time. What you may see of course is simply no reduction because you have got a higher transit charge, whereas if the transit charge had been lower there might actually have been a reduction. But certainly there was a pass on historically in relation to some parts of these matters to transit customers and potentially therefore on to end users.

It is not therefore as simple as Mr. Roth would like it to be treated as being. We would say these are all matters that inquiries should have been made of, and those inquiries should have been made by Ofcom.

THE CHAIRMAN: Thank you.

MR. COOK: That was the point that I wanted to raise, and I wanted to raise it now rather than in reply so people can see that is where we are going with it.

Madam, turning now to the SIA issues ----

THE CHAIRMAN: Mr. Turner just wants to come in there.

MR. TURNER: Madam, it is only that I had some brief remarks in relation to your question for the parties at the beginning of yesterday's session. I do not know if it is convenient to address them very briefly now or at the end.

THE CHAIRMAN: Are you going to address us more generally on SIA construction?

MR. TURNER: No, I am not. I am not going to do that because we, as the tribunal will be aware, have not pursued our grounds of appeal concerning the correct construction of clause 12.3.1.

THE CHAIRMAN: I think let Mr. Cook kick off and then anyone else who wants to add anything after that can do so.

MR. COOK: Madam, I actually was coming directly to the two matters you raised first thing yesterday morning. The first is a very small matter and that was the confusion about para.4.2 of Mr. Harding's witness statement. We have had a look at that and we are grateful to the tribunal for spotting what was indeed an unfortunate error there. The two sentences run together in a slightly peculiar fashion. What we have done is looked at that statement again with Mr. Harding and made some minor adjustments to those first two sentences which we hope deal with that problem. I am intending to hand a copy of that up. We have sent this to everybody else. We sent it through last night. I certainly have not heard any problems on it. It would be unexpected if there were any issues with it. (Same handed)

THE CHAIRMAN: What is this exactly?

MR. COOK: Paragraph 4.2 has actually been adjusted, the first two sentences.

THE CHAIRMAN: This is the same as the other witness statement except for that paragraph?

MR. COOK: Except for the first two sentences of that paragraph up to the point, "It was sent on 4th July 2006". That has just been adjusted in a minor way and I hope it now makes slightly more sense and I would seek permission to adduce that as an amended witness statement in that form.

THE CHAIRMAN: Yes, we grant you that permission.

MR. COOK: Thank you, madam.

Madam, the second initial matter which you raised was, why is pass-through relevant at all? That was your question. It is something that Mr. Roth has alluded to somewhat this morning but not in direct answer to that question. If I may, I will deal with it, but somewhat briefly. There is an initial and very simple answer here, which is that from the 1092 appellants' perspective it is very important because Ofcom has said BT can impact pass-through. At a very simple level, that is the statement by Ofcom that BT relies upon in coming to us and saying, "Therefore please now pay the money". It is not a situation where we are confident that we can simply go to Ofcom and say, "Here is a dispute, readdress the issue". Ofcom has already made a decision on it. So, very simplistically, from our perspective, it is vital to deal with and overrule that incorrect finding to make sure that we are in a position to deal with this on the merits with BT. We say that on that basis that will result in us not being liable for those sums of money, regardless of what the tribunal's decision turns out to be.

I think the wider question you were really asking was, why is it important from Ofcom's perspective and what was is the part of Ofcom's decision that relies upon these matters? I have gone through a number of paragraphs which I can simply give you the references to very quickly, and I will just summarise what Ofcom says in those. It is paragraphs from the determinations. It is para.4.107 to 4.112, 6.55 to 6.59, 7.8 to 7.11, and 8.9 to 8.14. Those are the key paragraphs as Ofcom walks it way through it, and I will briefly summarise those.

What Ofcom says is this is a gains from trade test initially. It says it would not be proportionate to force BT to bear a loss. What it also says is that since this is the first time it had been asked to determine a dispute in the context of the E2E obligation there were no relevant benchmarks in place to allow anyone to really know what the result was going to be. As a result, reflecting the fact that BT had not, in fact, made proportional raises in its prices, it took the view that it would be disproportionate to require BT to incur a loss even that in practice was really down to its failure to engage in pre-emptive price rises. Consequently, that is why it took the decision that the proportionate remedy was going to simply be the break-even charge.

Initially, it looked simply at a break-even charge across BT's entire traffic. There is a figure there in the documents as to what that would be, which was a lower figure than some other figures they came to ultimately decide were appropriate. That was the break-even charge

across the whole traffic. If you looked simply at BT's break-even charge for its retail traffic you got a much higher break-even charge.

Ultimately, the reason why pass-through was relevant was that it allowed you to say, "To the extent you are talking about transit customers, you can pass on, so you will suffer no loss at all, allowing us to only look at, when we come to consider the question of proportionality, your break-even charge simply on your retail transactions, which allows us to get to a number which is significantly higher". So the proportionality was a rationalisation for saying, "We are going to cap it but your break-even charge is a break-even charge on a retail basis only, not on a whole business basis".

So, madam, I think that is the answer to your question. Is that clear?

THE CHAIRMAN: Well, it is clear, I am not sure it is the answer to my question. If you are right that Ofcom should not have used the gains from trade test then there is no particular reason why it should have had in the context of these dispute resolution proceedings information about BT's costs, it would have information on your case about the MNOs' costs, which you say is relevant to the setting of the charge, but why would it have information about BT's costs, and if it does not have that in the context of this dispute resolution should it gather that information for the purpose of deciding whether to make the adjustment under s.192(d).

MR. COOK: Madam, I think the first point to bear in mind is the way in which Ofcom did this – certainly my understanding is not that it was a two stage test; it was not a situation where it determined "this is the correct charge" – step 1; step 2 – should there actually be a pay back? Effectively it worked out what was the appropriate charge, and then whatever that was was automatically to be paid back.

THE CHAIRMAN: It was not automatically paid back.

MR. COOK: Well it is slightly confused; it is in some ways a linguistic problem here which is they talk about the charge being reasonable E2E obligation and then say it is not proportionate, which is slightly problematic in language terms because it is difficult to see a charge being not proportionate but also being reasonable. Regardless of that, there is an aspect which they use two separate sets of tests – reasonable and proportionate, that is certainly true.

THE CHAIRMAN: The conundrum here that they had was that they had decided that the charge was reasonable even though on the basis of BT's prices it resulted in BT making a loss on that traffic over the interim period. But once you have decided that the charge is reasonable why then should H3G be kept out of the money that it would prima facie be due by

backdating the charge to the date of the OCCN plus 56 days because BT had not passed on the charge to its own customers?

MR. COOK: As a practical matter it may in part depend on the numbers of the case, that you are talking about a situation in which you have a very, very big increase in price arising on H3G, of the order of 50 – 60 per cent. perhaps, so you have a very significant increase in price. I suppose one could almost view it as being the analogy with what Ofcom does with the glide path, because it effectively allows you some time to catch up with such an enormous increase in price because it is such a great step change. It really does come down to the point, I would say, where Ofcom makes a mistake, but it is a terminological mistake I would say – no more than that, really – which is you cannot assess reasonableness in the isolation from proportionality. Proportionality is a relevant consideration in determining what is an appropriate charge, and consequently you should say "That is not an appropriate charge because it will force BT to bear a loss"; that would potentially be an appropriate way of thinking about it, but you would be saying the charge is therefore not reasonable.

THE CHAIRMAN: Well I can see that if – as seems to have happened here – the charge was held to be reasonable only because BT could pass it through, that is the second stage of the gains from trade test, that if the ability to pass it through prospectively is the justification for deciding that it is a reasonable charge then the ability to pass it through retrospectively may be relevant to the question of whether it is appropriate and proportionate to back date the charge. But on your clients' case, which is that the gains from trade test and, in particular, the second stage of the gains from trade test is not the appropriate test, in a situation where the reasonableness of the charge was determined on a cost base or some other basis, when deciding whether the person imposing the charge should have the benefit of that charge backdated is it relevant whether BT can pass that charge on to its customers?

MR. COOK: I am conscious that what I have been doing to some extent at the moment is simply trying to explain what Ofcom in fact did.

THE CHAIRMAN: Well I think we understand what Ofcom did.

MR. COOK: I am more than well aware I am saying that most of what Ofcom did was horribly wrong. It is important to bear in mind we are not saying it must simplistically be a cost-based charge, that is certainly a relevant consideration within it. But within a cost-based charge, within a properly determined charge there may certainly be an aspect of considering the extent of pass-on or not on the basis it is balancing the same way 'round, that you are simultaneously saying it is a reasonable charge for the MNOs, but also you are in part

asking if it is a reasonable charge for BT. If it cannot bear that price, if it cannot acquire custom at that price that may be a relevant consideration.

MR. SCOTT: Is there a distinction here between passing through to your clients, and passing through to consumers, because the point made to us by Mr. Roth is that there was no question here of passing through to consumers as we understand the point that he made?

MR. COOK: I am moving now deeply into reply submissions, I have no objection to doing so particularly. I think that the answer to that is that there is obviously a distinction in the sense that they are different categories of individuals, however when you go back to the terms of the Directives, in the provision it talks about "the interest of users", and in that context while we are not a consumer we are most certainly a user. Consequently, while there are two types of users the fact that one category of users, i.e. consumers may not be impacted, and you have already heard me say we actually think that is factually wrong. There is a category of users, namely transit customers, who are negatively impacted, and consequently regardless of whether consumers are, we are, and that is a consideration they should have taken into account and quite clearly did not we would say. So there is a distinction but simply showing there is no adverse impact on end users nowhere near gets Mr. Roth home.

Madam, of course, in primary terms my submission on the SIA issues are all to some extent based on the assumption that it turns out that you may be against me on the general issues, or that Ofcom may go back, do the job again and still find a higher charge which BT seeks to pass on. Certainly my principle submission is obviously the charge should be far, far lower, and naturally in those circumstances there would be no pass-on issue arising.

THE CHAIRMAN: But why would there not be a pass-on issue arising in those circumstances?

MR. COOK: Because charges would be going downwards is the answer.

THE CHAIRMAN: Yes, so then some of the MNOs might end up having to make an adjusting payment to BT?

MR. COOK: That is correct.

THE CHAIRMAN: And whether or not they can afford to do that does not depend on whether they have passed it through to their own customers. Anyway, carry on with your submissions and let us see where we get.

MR. COOK: That is where the issue is that there is no situation where we would say, if it is properly determined, we are going to end up having to pay higher rates, the rates should all be going downwards.

Yes, the SIA issue. Before getting into the detail of the issues I would like simply to reiterate certain factual matters which are, we would say, very important in terms of both setting the scene and governing how the Tribunal should look at these issues.

The first point is just to remind the Tribunal, of course, of the effect of the 22nd July 2003 Access & Billing Directive which prevents retrospective charging of customers more than four months back. It is actually quite a bit more complicated than that, and our skeleton has dealt with it in detail. But, in practice, it ends up not being more than four months ago.

Now, of course, there is an issue which is commercial backdating to retail customers. That is very, very difficult as a practical matter - writing to a customer and saying, "You made a call four months ago which we told you was going to cost this. It is actually going to cost you 50 percent more". Commercially, that is extremely problematic. But, in actual fact, my clients have never got into that situation because they are firmly prohibited from backdating their charges by the terms of the Access & Billing Directive. That is obviously a vital starting point here in looking at these issues.

The second point, factually, is the duration of the matter, which we say is also quite important in this context because, in actual fact, duration is the only reason why this matter is retrospective. The first OCCNs which were served in this context - which were actually relevant to the context of the determinations - were served in July 2006. Orange's, of course, were served back in May, but that was the one that was accepted. The disputes are not actually notified by anybody until 21st December. So, T-Mobile notifies on 21st December. BT, though, took until 22nd January, 2007. So, from the date when it started to be aware of these disputes, BT took six and a half months to actually take them to Ofcom. While it is certainly true to say that Ofcom was not that quick off the mark - in the sense that it took, from having received the notice on 21st December, it took ultimately from that date over six and a half months to resolve them - in actual fact in large measure the reason why Ofcom ultimately ended up determining these on a retrospective basis is the fact that BT took six and a half months to actually bring it to Ofcom's attention. Had it been dealt with relatively quickly, then it would have been a situation in which Ofcom might actually still have been determining at least part of it on a prospective basis. But, that is a consideration that we say is a relevant one to bear in mind.

The third matter is the lack of knowledge on the part of transit customers generally, both initially of the dispute; also of the rates involved; and, as well, of the possibility of retrospective charging.

Dealing, firstly, with a sort of generalised position across the industry, there are particular dealings that were dealt with in the witness statements, with particularly large customers, where BT did deal with them. That is the exception rather than the rule. But I will come back to those in a moment. But, just in general terms, unless a transit customer has a direct interconnection relationship with one of the MNOs - as you know, Cable & Wireless does have a small number of those, and others do in part -- But, unless you have that direct interconnection you will not be aware of the OCCNs because you will not receive them yourself and there is obviously no way of finding out about them independently.

What that means is that until it is sent to Ofcom -- until Ofcom publishes on its website, you do not know about the OCCN; you do not know about the dispute. In this case here, the first time that people may be able to find out generally was 9th February, 2007, which is when the matter was published on Ofcom's website. Again, we say that is rather important when you see the delay points - that actually having started back in July it is only on 9th February that anyone in the general market starts to find out about the nature of these disputes happening directly. Of course, even on 9th February all they know is that there is a dispute. They do not know the detail of the rates being proposed at that stage.

The 9th February bulletin - it is also very important to bear in mind that that did not include any reference to H3G's OCCN. It includes reference, of course, to BT's OCCN in relation to 3G saying, "Please lower the tariffs". It did not include reference to H3G's later OCCN saying, "Please raise the tariffs" and also in practice, saying, "Please raise the tariffs very substantially". So, there was no visibility of that dispute at the time. That visibility was only provided on 18th April, 2007 when Ofcom published that on its bulletin saying that H3G wanted to increase prices.

So up until that point, given the carrier price list reflected the old rate, people might have known there was a possibility that rates might go down for H3G, but there was certainly nothing available in the market generally that would tell people that rates might go up. Of course, the 18th April, 2007 publication did not actually mention the rates themselves. It simply said that H3G wanted to increase the rates. Bear in mind, of course, that this is 18th April. So, we are already after the end of the period - 1st April, 2007 being when the market review cuts in.

Draft determinations are then produced on 14th May, 2007. Again, there are no rates included in those. They are adapted from the end of the determinations. There is no mention of retrospection there at all.

We get the final determination on 7th July, 2007. The rates are then visible. Also, more importantly, there is the first mention generally of the possibility of retrospective charging by BT.

So, what we have throughout this period, with the exception of some specific discussions by BT with its customers (which I will come back to), BT made no attempt to inform its transit customers that OCCNs were being served; that they were being disputed; that they were being sent to Ofcom; the level of the rates involved; and, most importantly at all that this was of any relevance at all to transit customers - i.e. that if BT lost, it would seek to retrospectively charge. Of course, for the most part, BT did not tell them when that information was not otherwise available in any way.

Turning then to the fourth and fifth factual matters which I am going to approach together -- Those are, firstly, that we would say there is a general understanding in the market that retrospection did not apply to transit charges, and, secondly, that in the context of a number of the individual operators who were big enough to actually for BT to tell about the disputes (albeit quite often fairly late in the day) -- when BT did tell them about it, it made express reference to the fact that retrospection would not apply - so, in particular, that BT would not be seeking to recover higher rates.

So, we say there is both a general market understanding confirming specific cases by BT making that express statement. I will take you through the evidence here. It is important to bear in mind that the bulk of the evidence here is from witness statements. There has been the scope of BT to put forward witness statements, and to put in contradictions. It has chosen not to do so. There has been the scope for BT to cross-examine. It has chosen not to do so. That evidence is uncontradicted and unchallenged.

The evidence, in particular, is in Bundle D3. If I could ask you simply to turn that up quickly -- (After a pause): In the interests of simplicity I would like to start with Tab 2 first, which in fact is T-Mobile's evidence. This is Mr. Miller's witness statement, and in particular para. 7. I particularly refer there to the second and third sentences in para. 7. We say the second sentence there is an illustration of T-Mobile's understanding of the general lack of retrospection in this market. The third sentence is a confirmation of express representations to that effect being made to T-Mobile by BT and a number of individuals at BT.

Turning to my client's evidence at Tab 4 - the evidence of Mr. Harding -- We can carry on using the witness statement that is in the bundle because this paragraph is not changed that I am taking you to - para. 4.3. Again, Mr. Harding gives evidence in the final sentence of

that paragraph that they would not be increasing the transit prices and would take the risk in the event that they lost the dispute. So, again, specific representations being made that it was BT's problem and it was not a matter of concern for transit customers.

Mr. Granberg's witness statement is in the next tab. Paragraphs 3.2 and 3.3. I would ask you to read those two paragraphs. (After a pause) Again we would say those paragraphs and the evidence reflect two matters. Firstly, in 3.2 express representation has made to the effect there would be no retrospective charging; and in 3.3 Mr. Granberg confirms the general industry wide understanding that that was how the world operated in any event.

I would also just quickly ask the tribunal to look at 3.4 where he explains the effect these representations and the general understanding had on Opal Telecom where they made no provision for the possibility of excess increased charges at all.

Madam, I would also refer to Vodafone's statement of intervention. It is para.40 of the that which is in tab 9. This obviously comes with diminished weight, I would accept that, not because it is Vodafone but because it is simply a statement of intervention. It is not an individual giving evidence, it is Vodafone stating something happened, but nonetheless I would say it is all of a part of what has gone before and Vodafone confirms that similar representations were being made to it.

THE CHAIRMAN: It is not in Mr. Tillotson's statement then?

MR. COOK: No, that is right.

MR. READ: Madam, can I make one point. I do not want to jump up and interfere with this, but I will be taking some points about whether or not any of this material is actually relevant to the issue that you have to decide on the SIA, but I will make those points later. I have got no objection to them being heard *de bene esse*, but I will be objecting to the nature of the evidence now being put before you.

MR. COOK: In any event, Vodafone simply confirms that they, themselves, agreed to similar representations. I rest my case more on the ones received by my clients than the express witness evidence of T-Mobile, but I am flagging the fact that Vodafone also agree that it was something that happened to it.

Madam, we would say that is the relevant factual background. What is, of course, important here is chunks of that were unknown to Ofcom because it did not do the sort of process of carrying out proper consultation, consultation that allowed it to know about many of these matters. Nonetheless, that is the background to what is now before you and you can look at these matters in the correct context as a result.

Turning now to the question of retrospective charging, I would like to start with the SMP conditions. The reason I start there is we would say the SMP conditions are absolutely vital in terms of how you approach the SIA for two reasons. Firstly, as a matter of construction, it goes without saying that there are two possible constructions being put upon something, one of which is consistent with the SMP conditions, one is not. You should adopt the construction which is consistent with the SMP conditions. Ultimately though, if there is no construction you can reasonably put upon something that will comply with the SMP conditions, the terms of the SIA must give way to the SMP conditions.

Looking though at the SMP conditions, it is condition AA1(a).2, the provision of network access shall be provided on fair and reasonable terms, conditions and charges. In my submission, imposing retrospective charges without having given any warning, despite the fact that a warning could have been given many months earlier. A clause allowing that is not a fair and reasonable term, and the charge itself is not being imposed in fair and reasonable circumstances and therefore it stops being a fair and reasonable charge.

Just to be clear, more broadly than the facts of our case, about where we draw the lines about when a charge is reasonable or in what circumstances you can recover on a retrospective basis, we are not saying that retrospective charging is impermissible in any circumstance. There are a number of situations we can refer you to in which it might well be permissible. The most obvious one, we would say, is where Ofcom itself says that a charge shall be backdated, and that is what clause 12.3.2 would permit.

We would have no challenge certainly to BT doing that. BT would be doing what Ofcom told it. It might well be that we would be trying to explain to Ofcom why that should not be done factually or whatever else, but if Ofcom takes the decision to backdate a charge and it within 12.3.2 of course BT must levy it. So that is an example where it would be legitimate to charge retrospectively.

The other circumstance would be where there is a truly retrospective charge. By that I mean a charge which actually applies prior to the date of the OCCN, which is what H3G tried to do in its OCCN, which is backdate the charges. Again in those circumstances we would accept that if BT is in a position where it does not know about a proposal there is obviously no way it can tell its customers and give them any warning. In those circumstances it would not be fair and reasonable for BT to pass that on. There would obviously be questions about whether Ofcom should resolve a dispute by allowing a charge which is backdated before anyone could have known about it, but that is a completely separate question.

So there are circumstances in which retrospective charging will be permissible. The problem here is the fact that it is by stealth, it is by surprise, it is an ambush charge that applies months after the facts when warning could have been given in circumstances in which it actually would have been pre-emptive warning. So that is the particular factor that we focus upon here as making clear that that is not fair and reasonable, it is not going to be a fair and reasonable term if it allows retrospective charging in those circumstances.

There is a very important consideration as a matter of competition and a very important consideration in terms of the reason why SMP conditions were imposed on BT, as to why that is a particular problem. That is the question of uncertainty. If you know what charges you can price on a particular basis. In particular, you can price relatively keenly because you know that is your fixed charge and you can therefore say, "That is the margin I need, I can price right down to that level". If, on the other hand, you are uncertain and you know there is a possibility months after the event that someone can come back and change your charges retrospectively you obviously cannot price in the same sort of aggressive fashion because you need to ensure that there is always a bit of headroom so that when and if it does happen you are not in difficulty and you do not have to go back and change your customers, which in many cases we know you cannot do, you have already got a bit of headroom there. So that is the reason why it is a very important matter.

There is no suggestion on my part that BT is doing this in any way deliberately on the facts of this case, the point being that actually it could be manipulated in an anti-competitive way by BT by not telling people about it and then actually damaging its competitors. The reason why it has SMP conditions in this way is because of its central position as a transit operator. If it is in a position, whether by lack of compliance with a duty to tell people, whether BT improves its position deliberately in order to gain the anti-competitive advantage or simply has a better position as a result of a failure to tell people what is going on, that becomes a very real problem in terms of the ability of anybody else to compete with BT because BT is always able to price that slightly more aggressively because it has certainty, and nobody else does.

That is the reason why we say it is entirely consistent with the purposive of SMP conditions to prevent retrospective charging in these kinds of situations of ambush charging.

The point that we would say does arise as well out of the SMP conditions, a slightly discrete point, which is where there is a general market understanding or a specific understanding that has been created by representations made by BT, we say it would not be fair and reasonable for BT to resile from that understanding or its representations. That is a point

that can arise in two ways. I can run these issues, and I do, as a matter of general law, as estoppel points, firstly, as estoppel by convention, and we say that is where the general market understanding is relevant if everyone thinks it operates in a particular way and you cannot resile from that when it is detrimental and unfair. That is a point that we say arises here. Secondly, I can also run express representations as an estoppel by representation point, and again I do, because there are express representations being made, detrimental reliance, people have not increased their charges because there was no risk of retrospection and it would be unconscionable for BT to resile from that position.

That is matters of general law, but in the context of the SMP conditions, there is a specific additional obligation, we would say, which exists on BT under the terms of its SMP conditions not to resile from those matters because it stops being fair and reasonable, the terms and conditions, the charge is not a fair and reasonable charge if it is imposed in circumstances which are not fair and reasonable. So both as matters of general law but also in terms of specific SMP obligations, BT is obliged to stick with general market understanding or stick with the specific representations it makes about how its contracts operate.

That, we say, is the SMP, the regulatory overlay, that one needs to look at the SIA and the context of it. Of course Ofcom ignored all of this in looking at the SIA issue.

Turning then to the SIA – when I talk about the SIA I am talking about all of it and of course we have the SIA and we also have the carrier price list which is also a contractual document that governs the relationship between BT and its transit customers.

The first issue is how do you approach these documents in terms of construction. The first one I have already dealt with. SMP involves the fact that you have to try and construe them in accordance with the SMP conditions, and also ensuring that they operate in fair and reasonable circumstances.

The second point we would say is something that BT's own witnesses in the Orange preliminary issue have referred to, and in particular I would refer you to Mr. Annette's witness statement at paras.5-16, and Mr. Amoss's witness statement at para.8. That is in the context of a slightly different clause, clause 13.7 of the SIA. The point they both make is that in the context of looking at and construing bits of the SIA, it should be construed in a way which reflects industry understanding and practice. We would absolutely agree with that particular point by BT that you should look at construction of the SIA, construction of the carrier price list on that basis. It should be done in a way which is consistent with practice, not contrary to practice.

THE CHAIRMAN: That is Mr. Annette's statement in the Orange preliminary issue?
MR. COOK: That is correct. Madam, I am conscious those are not in the bundles and that your colleagues were not in that case. We could send in those extracts if it would assist.
THE CHAIRMAN: We have copies of them here.
MR. COOK: Madam, taking account of those considerations we can now look at the specific provisions that we are talking about here. The key point of course is 12.3.1. It is not suggested by anyone that we are in the context of 12.3.2. It is not currently suggested but apparently it may be, so I reserve my position as to when that is said.
MR. READ: It is in one of the footnotes to our statement of intervention, madam. It is made quite clearly. We just say that actually that is not the basis upon which Ofcom actually did it. We say in order to stop the remit of these issues going further than they are already, perhaps we ought to concentrate on 12.3.1, but it was made absolutely clear in para.16 of our statement of intervention and the footnote thereto, which I think is footnote 18, that we are taking that very point.
THE CHAIRMAN: Are you asking us to decide then on the question of the interpretation of 12.3.2?
MR. READ: Madam, I do not want to anticipate my submissions but I say that virtually everything you have been hearing today, apart from a little bit that we may now be going on to, is completely irrelevant to what is in the Altnets notice of appeal.
THE CHAIRMAN: All right, let us carry on.
MR. COOK: We are looking at 12.3 generally. Certainly I would accept, as a matter of ----
THE CHAIRMAN: Where is it set out?
MR. COOK: It is set out in the BT statement of intervention at para.15.
THE CHAIRMAN: Where do you want to take us to in the documents where we have the wording of the clause and the CPL wording set out?
MR. COOK: The CPL wording is set out in our skeleton argument among other places. I am actually not sure if it is anywhere in the documents.
THE CHAIRMAN: Is 12.3.1 also in your skeleton argument? I think it is.
MR. COOK: H1, 13, is ----
MR. SCOTT: I think, if you look at D3, p.71, we find 12.2 and then 12.3.1, 12.3.2 on p. 71.
MR. COOK: Yes. Madam, we would accept that if you look at clause 12.3 in isolation without taking account of any of the matters that I have talked about one could certainly come to the construction that Ofcom and BT would be urging upon you, these are facts that fall within it. We would say the key factors are the SMP conditions but, more importantly, the carrier

price list, and the carrier price list is set out there at para.63. If I might assist "POLO" is payments to other licensed operators.

The first issue is what does that carrier list price statement mean?

THE CHAIRMAN: Well the first issue is what does 12.3.1 mean – or do you want to come to that second?

MR. COOK: I am going to come to that, I am accepting that if you look at it in the abstract then the construction that Ofcom and BT suggest is correct will be on that you would come to. I am saying when you understand the carrier price list exception then it actually does not matter. If it does matter then you have to approach it on the SMP basis which I will come back to.

My first submission is really going to be saying that carrier price list is the point which makes clear the position in relation to transit charges, and actually therefore 12.3 does not matter. We say that 12.3 ----

THE CHAIRMAN: Well do it as you were intending with the carrier price list exception.

MR. COOK: The carrier price list then, the statements that are made there. We say what is being said there is clear.

THE CHAIRMAN: Well a … submission, Mr. Cook. (Laughter)

MR. COOK: Well certainly I will come back to say that actually there is only one interpretation that is being put forward of what this means, that in actual fact Ofcom says simply they do not admit our interpretation, they do not put forward a contrary one. BT says it is Delphic, but does not put forward any alternative explanation. So we would say perhaps "clear" was going a little further than I can or should go; there is only one possible explanation for what this means, and it is clear in that sense. We would say what this statement says is there are two sentences, sentence two is the more important, but sentence one is also relevant.

Sentence one says that the Billing Team only provides one month back dated billing for transit charges.

THE CHAIRMAN: "Billing Team" that is presumably BT's Billing Team?

MR. COOK: Yes.

THE CHAIRMAN: So that "Please note that BT's Billing Team only provides one month back dated billing for transit charges."

MR. COOK: As I said, the second sentence was the more important of the two, but again that is making clear that bills are back dated by a month, but we are not going to bill months and months ago, which is all I draw from the first sentence – if it was not there it would not matter to my submission, but certainly we say the fact it is there is not unhelpful from our

perspective. The second sentence though is where I place my submissions which is saying "retrospect ion" as a term by Ofcom is not applicable in the context of payments to other licensed operators. It is under the section which deals with transit charges and it is talking therefore about charges which are going to be imposed upon us, and we say it can only be dealing with the fact that to the extent of charges to other parties "we are not going to seek retrospection from you".

THE CHAIRMAN: So you say that this means that whatever 12.3.1 and 2 mean that even if it was a charge of the kind that you said could be retrospective and still be fair and reasonable under the SMP condition, that this carrier price list still rules it out from being retrospective in respect of transit charges?

MR. COOK: Yes, we would say that what BT has done is contracted out of its ability – it would have a wide ability under the SMP conditions to impose retrospective charges in certain circumstances I have just gone through. BT has, however, in the context of carrier price lists said: "We will not seek retrospection", and what we are dealing with here is transit charges; there are other categories of charges where there are not similar provisions, so in those cases BT can seek retrospection. But in this context it is said retrospection as determined by Ofcom is not applicable here.

THE CHAIRMAN: But what is the "as determined by Ofcom" wording doing there? Is that linking it in to 12.3.2 rather than 12.3.1, because 12.3.2 seems to deal with retrospection which is imposed by Ofcom?

MR. COOK: We would say it does apply to both 12.3.1 and 12.3.2, which is saying whenever the charge is being altered retrospectively, and it is as a result of a determination by Ofcom. 12.3.2 we would say deals with a situation where Ofcom requires BT to pass on a different charge to its customers. Here we are dealing with a situation in which Ofcom has determined that the underlying charge shall be increased retrospectively, which is 12.3.1, so in each case there is a determination by Ofcom for the charge that, prima facie, can be seen as being retrospective. So either way we would say it is clear that what that clause is saying is retrospection is not applicable.

We would suggest the right way of looking at it is that if there is any uncertainty at all, if this is an exception to what is being talked about in 12.3, if BT wanted to make clear that this was a limited exception it should have done so in very clear terms. If not, it should be treated and read in the natural way. I come back to the point, of course, that it should be construed in a way that is consistent with industry understanding. The point I have made, and it is dealt with in the witness statements is that industry general understanding was that

retrospection did not apply to transit charges. It was not industry understanding that retrospection of some kind applied to transit charges, it was no retrospection, and that is entirely consistent with what is being said there, that it is any form of determination by Ofcom, not certain kinds of determination by Ofcom.

So as I foreshadowed, there is not actually a construction – you perhaps advanced a contrary one that I have no doubt my learned friend will jump on it, but prior to this point nobody said there is a contrary construction. Ofcom simply did not admit our construction; did not put forward an alternative and BT simply said it was very "Delphic". Now that particular point obviously does not take them very far, the fact a clause might be Delphic you still have to give meaning to it, it was obviously intended by the parties to it to have meaning and it should be given meaning. I would say it is very important – madam, you have obviously raised a potential alternative – that nobody else has come up with that, and in particular BT has not.

THE CHAIRMAN: I am not raising any alternatives, Mr. Cook, I am just trying to work out what this sentence means.

MR. COOK: Madam, you are raising something that may be jumped on by my learned friend as an alternative, I am simply making the point that I would say that it is important to note the fact that it has not been raised by anybody else before on the basis that that strongly suggests that no one thought that that was what it meant, and the general industry understanding is no retrospection of any kind at all.

So we would say the carrier price list, this provision makes clear there shall be no retrospection. That is sufficiently clear for our purposes, it is the only possible reasonable construction, and what that means then is that that makes clear the position for this situation.

The other point taken by Ofcom and BT is to say "no", under the terms of the SIA you simply have a position where in the event of a conflict between the SIA and the carrier price list, the SIA takes precedence, it is higher up the contractual chain of importance. Again, we would say that is simply not right for a number of reasons.

First, it is a standard situation in which you have layers of contracts, that you end up with general principles being stated in the head contract, and detailed terms in schedules quite frequently, or in supplemental detailed documents. Often what one gets therefore is a general principle, and then layers of detail which may include exceptions to the general principle, being within lower documents. That is not a situation of an exception, a contradiction between the two, it is a situation where you read the two together and you

understand as a general principle, and then it applies in particular circumstances as defined by the detailed terms. That is simply where the documents work together, they are not in contradiction with each other, and we would say that is exactly the situation here. The general terms of the SIA may well provide for generalised ability to retrospectively charge. We then have the detail and the detail says that in this particular limited context transit charges only, that is not something that we say does apply, and so it is a situation of elaboration not contradiction. So that point we say simply does not apply.

MR. SCOTT: One of the difficulties here is that we are looking at this in total isolation from the rest of the documents ----

MR. COOK: I am sorry there is not a copy here, but I can tell you what is in the rest of the document of which this is the only bit, it is a statement at the top of the particular pages, which then go on for many pages and deal with transit charges, so it is not a detailed set of provisions of which this is one.

MR. SCOTT: I understand that, but what you appear to be suggesting is that this is exceptional and that there are other parts of the price list where 12.3.1 and 12.3.2 still apply, they being the general principles. Now, you may not know the answer to that.

MR. COOK: This is a provision that applies in the part of the carrier price list which deals with transit charges. It is not replicated in any of the other bits and where the transit price list operates, and there are many separate chunks of it, there is no similar provision in any of the other parts of it. We have not printed it out ----

MR. SCOTT: No, no, I understand.

MR. COOK: So what you have is simply nowhere else does it say that retrospection does not apply and therefore we are back to the general principle in the SIA, where you do have a specific provision saying just in relation to transit charges, not all the other type of charges that BT applies when you want to phone BT's customers, or anything else, then the general principle governs, but it does not govern where there is an exception put in.

So we would say that that is both as a matter of simple general legal principles but of course the SMP overlay comes back over here in terms both of the fact that there is a general understanding in the market and the fact that where you have made a statement like this it will be contrary to the SMP conditions, it would be unfair and unreasonable for BT to step back from it in that situation.

Where does this leave the Tribunal? We would say where it leaves the Tribunal is relatively simple, namely, Ofcom is wrong. Ofcom's consideration initially was far too limited, it was not aware of the terms of the carrier price list, it did not give any thought at all to the SMP

conditions, it did not raise any inquiries that would have allowed it to (a) understand the general understanding of the market; and (b) the specific representation that BT was making, so that is the initial matter, that Ofcom is wrong. In my submission the Tribunal can go further than that and say that actually the contractual relationship here with all the additional factors that I have referred you to, and which are not contradicted or denied by BT in this forum is such that it is clear that there can be no retrospection in these circumstances. Ultimately what it comes down to in terms of the arguments is very simply the carrier price list says what I say it says, and that takes priority. If not, then the SIA 12.3 should be construed in a way which is consistent with SMP, and I would say that taking account of what I have said about the inability to ambush charges, if the clause allows ambush charges it is not a fair and reasonable charge and therefore you need to find a construction of 12.3 which prevents ambush charging, so the simplest and easiest way of doing that is either to say that it is applying to true retrospection, true retrospection being where it is a situation where the charge wants to backdate prior to the OCCN, or if necessary you end up with a situation in which this clause is simply not permissible, and the only way BT could enforce it was by ensuring that it was not ambushing people. Beyond that though I was not intending to make any submissions on the construction of 12.3.

MR. SCOTT: You said just now that Ofcom was not aware of the price list. Are you saying that in the context that they did not take the price list into their consideration in this dispute resolution process, or that as a matter of fact – and you may not know the answer to this – they were not in possession of the price list?

MR. COOK: I am saying that they failed to take any account of it. I cannot answer you as to whether in fact there was a copy of it somewhere in a locked dusty closet in Ofcom; the determination process did not take account of it and that is all I need to show.

Unless I can assist you further, those are my submissions.

THE CHAIRMAN: Thank you very much, Mr. Cook.

MR. WISKING: I wonder if I could say a few words? My learned friend's position essentially is to support the Altnets in relation to this particular issue. As Mr. Cook has covered most of the ground, I do not want to repeat that. I just want to make a few points to supplement what he has said.

First of all, I want to explain that Vodafone's interest in this is as a transit customer. So, as regards H3G, at the relevant time, whilst it had I think just entered into a direct interconnection agreement, it had no physical link and therefore was transit-ing via BT. Vodafone was in an identical position to the transit customers notwithstanding the fact that

it was a participant in a dispute with BT at the time because it had no visibility, in the way that Mr. Cook explained, as to the position of the disputes as between BT and H3G.

The second point to make - and this perhaps starts to deal with the tribunal's questions raised yesterday - is that obviously we support Ofcom in terms of the gains from trade test. So, as we see this issue, it is a limited one in that it goes simply to the level of the repayment which BT was ordered to make to H3G in respect of that period in question, and that it does not therefore go beyond that and to the validity of the pass-through, part of the gains from trade test. Nevertheless, this issue is relevant because Ofcom has made it relevant. As Mr. Cook explained, Ofcom has used this very narrow assessment of the SIA to effectively require BT to make a higher repayment to H3G, which, in turn, has led BT to seek to recover those amounts from transit customers, including Vodafone.

So, in terms of the questions the tribunal raised yesterday, first of all, you asked about the appropriateness of Ofcom's order under s.192(d). In effect, I think we are saying that the logic of the games from trade test was that there would be no modification for proportionality in the particular circumstances. I think Mr. Cook addressed this previously. From our perspective, it was perfectly reasonable for Ofcom to limit the repayment to H3G to the break-even level. The only question was therefore: What is the appropriate break-even level? There is no issue in these proceedings, as I understand it, that BT should have made higher repayment to H3G. So, the only question is: is the repayment level the one that is currently in place? Or, in our submission, should it be the lower repayment level that was contemplated in the draft determination by Ofcom?

The second question was the extent to which these issues are relevant. As we say, obviously Ofcom has made these issues relevant. Had it not even entered into this question, we would not be arguing it. However, I do accept - and this may address what Mr. Read is going to say - that it is not going to be possible for the tribunal to reach a decision as to particular disputes between BT and transit customers. Clearly the tribunal does not have the full facts before it, and it is not relevant to these proceedings. What is relevant to these proceedings - and why its evidence is relevant - is that it goes to the question as to whether Ofcom reached its decision about the break-even level on an appropriate basis, and whether it conducted an appropriate inquiry.

The thrust of Mr. Cook's submissions is that there is serious doubt as to whether Ofcom's interpretation of the SIA was correct, having regard to the CPL which is referred to, and also the SMP obligation which bears on the interpretation of the SIA.

The other point to make - and this is a point raised by BT itself in its notice of appeal at paras. 85 to 86 of its skeleton at p.107 - is that BT criticise Ofcom for failing to make the wider, practical, factual commercial inquiry. The logic of Ofcom's assessment is whether BT had the ability - which is a mixed question - to recover this money from the transit customers. It should not have stopped its inquiry at just: What is the meaning of Clause 12? It should have gone wider. Now, if what Ofcom says is, "Well, actually, it was disproportionate to have gone wider", then in our submission it should not have done it at all. It is either, "It didn't enter into this factual inquiry", or, "It did it properly". To just do it half-way is just not satisfactory.

So, we would say the evidence is relevant to that question, but obviously the tribunal cannot deal with the sort of questions of estoppel which are hinted at in some of the evidence, save that that evidence is relevant because it shows that there are much wider and much more complicated questions at issue here which Ofcom did not investigate.

On the construction of the SIA, one point to add to Mr. Cook's submissions is that the SIA specifically provides in Clauses 12.10 and 13.16 (F1, Tab 3, pp.16 and 18) -- Those are both final sub-clauses of Clauses 12 and 13. They provide that the liabilities and obligations of the parties in the agreement -- The agreement is without prejudice to the liabilities and obligations of the parties under their license. That is the version of the SIA in the bundles. I suspect that is a very old version of the SIA which has not been amended for the Communications Act. I do not know whether BT will take this point, but the version of the standard SIA on BT's website refers to 'conditions'. So, effectively, the SIA itself expressly provides that it is without prejudice to any license obligations, which just reinforces Mr. Cook's point that they need to be read together, and they need to be read consistently.

The only other point to mention - and it does trespass to some extent on to non-core issues, but I raise it here - is that Ofcom's defence on the question of whether it should have looked at the SMP obligation is that no-one raised it with them, and so that comes into the failure to consult part of the non-core issue. Nevertheless, we would submit that when it comes to regulatory obligations, that is something that Ofcom should have taken account of of its own initiative.

Those are my submissions, but they are only intended really to supplement Mr. Cook. Unless I can assist the tribunal further ----

THE CHAIRMAN: Thank you very much, Mr. Wisking. Mr. Turner, would now be a good moment for you to make your points?

MR. TURNER: Madam, I do not know how long Mr. Read proposes to address the tribunal for. I seem to recall the tribunal said that you had to rise at 4.30 sharp today, but I may have mis-remembered that. I can either do so now, or after Mr. Read, as the tribunal pleases.

THE CHAIRMAN: Miss Demetriou looked as if she was rising to her feet ----

MISS DEMETRIOU: Madam, it is just formally to adopt what my learned friends have said before me. We also support the Altnets' position on this point. I do not have anything further substantive myself to add. It is just for the tribunal's note.

THE CHAIRMAN: Mr. Roth, are you going to be addressing us on this point?

MR. ROTH: Only to explain in a few words why I will not be addressing you. It seems sensible for Mr. Read, representing the other party to the contract, which is the carrier price list, to address you first.

THE CHAIRMAN: Mr. Read, why do you not go ahead?

MR. READ: Madam, can I start by making three preliminary points in connection with this? Yes, in terms of the construction of the contract we entirely agree, with one or two exceptions which we made clear in the statement of intervention, with the stance that Ofcom have actually taken in their approach to it. However, we do not - and I want to make this absolutely clear - accept that Ofcom was right to look at it solely from the point of view of the strict construction of the contract. To that extent, Mr. Wisking has correctly identified what we say about this, because we say that it is a corollary of the flawed gains from trade test and the pass-through assumption and the measures that have to be taken in respect of that that one ends up with this situation of looking at the contract in the first place, but divorcing it from the very real commercial concerns and pressures that are involved in this. First, and most importantly, it pre-supposes that all the other operators will actually accept that BT will be in a position to pass the charges on. I think it is self-evident from the argument that you have heard already today that that is not the position. To the contrary - BT is finding it an immensely difficult task to have to recoup the money. Even those people we got the money from - and that includes Vodafone - are saying, "Well, we paid it under protest. We will have it back if we think there is the opportunity of getting it back at any stage". The Altnets have not even paid us yet because they are saying, "Well, all this has to be held back".

So, in other words, it illustrates, in our respectful submission the whole flaws with the pass-through assumption because it looks solely at the strict contractual position rather than looking at the actual commercial reality behind it. Mr. Cook made various points about it being difficult for us to pass it on; we did not know what was going on, and so on, and so

forth. I do not think he was trying in any way to be pejorative about BT. But, we say that is the inevitable consequence of the test that Ofcom adopted.

I think, in reality, you have most of my points that I have already made about that. But, we do say that this whole question is relevant in that context because it shows the inherent flaws with, in particular, the pass-through assumption and the way it is applied. So, that is the first point I want to make.

The second point I want to make really relates back to, I think, the point that was being raised yesterday, but I may have misunderstood. Certainly the way that Ofcom has characterised it when trying to explain the determination -- They say, in terms, that Ofcom's understanding of Clause 12.3(1) had no impact on its conclusion as to the reasonableness of the charges proposed by H3G. Now, we do not accept that because we say that the logic of the determination is that it did impact on the charge that they actually set. This was not (as I think it has been characterised certainly in Ofcom's Annexe B to its defence) simply a question of the level of repayments that were due, or not due. It was actually a determination that fixed the price that H3G were entitled to recover under the determination. One sees that at the point Mr. Anderson took you a long time ago - a week ago - in the determination itself in Bundle B, Tab 4, p.74. That is the actual declaration of rights and obligations in respect of H3G. You can see that in the first element there,

> "The charges contained in the letter of H3G to BT of 22nd November, 2006 are reasonable charges for the purposes of the E-To-E obligation".

We say that is setting the terms and conditions - and I am parroting what Mr. Anderson said - under s.190(2)(b). Then, and separately as a result of that, in para. 2 there was a re-adjustment of the prices which we say is the s.190(2)(d) and that that is how it operated. But, in deriving whether or not the charge under the letter of 22nd November, 2006 was reasonable or not, the question of the construction of the SIA came into play.

Madam, I can trace that through, if you want to, from the determination, but I suspect you probably have seen it enough times. The short answer - and I think this has been characterised more or less correctly by Mr. Cook - is that they started by saying, "Would we meet the gains from trade test?" In H3G cases the answer was, "No", and so therefore we only passed on the pass-through assumption. They then come to a third stage where they say, "But it would be disproportionate in the circumstances to impose the loss effectively on BT, and therefore we set the price at such-and-such a level". But, it is a question of setting the price.

Madam, in fact we criticised this in our notice of appeal because we actually said in terms that there was apparently a degree of an inconsistent application of the very test that Ofcom had actually imposed on us in the way that it approached the pass-through test. It certainly was not simply a question of under-payment or over-payment, it was actually a question that they set the price on the basis of that construction. So therefore we do not accept the characterisation as it has been put forward in Ofcom's defence, particularly at para.21, I think it was, of annex B and the other paragraphs.

Indeed, I do not know whether it may become relevant or not, but I will just make this point, that one cannot, in reality, separate the remedy from the reasonableness, otherwise the consequence of that would be to put BT in an impossible situation because Ofcom's test assumes that BT will make a profit. Ofcom then specifically decided BT could retrospectively charge and therefore adjust the price on that basis. Then to suggest somehow that it is BT's commercial decision or not whether to follow through the consequences of Ofcom's determination is really the same Pontius Pilate approach I was suggesting they adopted in respect of their other dispute resolution powers, that they just are not accepting responsibility for the price they have imposed upon BT and the consequences that flow from it.

Those are the first two preliminary points that I would make on it, madam.

The third preliminary point is what is this actually about? We say that the notice of appeal, which of course is the only matter that is in front of you in terms of what you are having to decide this on – I do not need to take you to the tribunal's powers on this but of course it has to be in accordance with the notice of appeal – if one actually looks at what the Altnets are actually asking, and of course they are the ones who are only still *extant* in dealing with this point, and Vodafone as interveners are only able to argue the case in so far as it within the scope of that appeal. If I can take you very briefly to what the Altnets or the 1092 appellants are asking. It is bundle D3, tab 3, p.55. This is the summary of the grounds of appeal being put forward by the Altnets. It lists out in para.11, which is on p.54, the determinations of Ofcom erred in key respects and then at (d):

> "Ofcom proceeded on the basis of an error of law in interpreting BT's standard Interconnection Agreement, and in particular its implication for BT's ability to recover from the Appellants with retrospective effect certain costs associated …"

Perhaps if one just goes on to the end of this document to see how exactly the characterise it in the relief they seek, which is at p.89 in the same tab. Paragraph 140, "Relief sought", where they seek the following relief, and then over the page at (b)(v):

"… whether on a proper construction of the SIA, BT would be able to recover from the Appellants any amount determined as due to the MNOs pursuant to the Determinations …"

So it is contractual construction that one is concerned with here in this appeal and nothing more, which is why, when one gets on to some of the complaints that have been raised – and I note that Mr. Wisking very deftly said that they are part of the broader picture, to wit the competition complaint that he talks about, the issues of estoppel, and all the rest of it – they are not really a factor that can be taken into account in the context of the issue before you on this point. Of course, BT would say that it simply supports its arguments about this is a flawed test and BT cannot in fact pass through the monies that has been done, but that is a separate point. Certainly we would very strongly urge you to stay away from getting involved in estoppel or issues of competition law or the like which have been specifically raised at various points.

THE CHAIRMAN: So what is going to happen if we uphold the decision to the effect that we then deal with this question of the SIA construction and we say suppose we come to the conclusion that it is right, it does allow BT to pass on the charges retrospectively and we do not think this is inconsistent with the SMP conditions, there then has to be litigation in the High Court or whatever because you will then try and recover these sums and they will say, "No, you are estopped from relying on those clauses?" What in those proceedings then is the status of this tribunal's findings as to the construction of the contract?

MR. READ: I think the status would undoubtedly be sufficient, given that the parties involved in it, to commence a summary judgment application on the basis that that is the construction. Of course that does not rule out the parties wanting, if they really want to chance their arm on arguments of estoppel and the like, to say, "Well, we have got another defence of the whole matter which is whether or not we can raise an estoppel by representation or estoppel by conduct", or however they want at the end of the day to put the matter, and to say, "That is the basis upon which we can defend these proceedings". I am not going to say that that would give them a defence because we would say in the course of the summary judgment application that it does not give them a defence. But certainly the construction issue will not be, at the end of the day, something that needs to be taken further because that will already have been determined.

MR. SCOTT: Staying with the notice of appeal but just going up a couple of sub-paragraphs we are asked:

"… whether the 'gains from trade' test was inappropriate in determining mobile termination disputes."

Let us for a moment say that the gains from trade were acceptable to us, then you go to (iv):

"… an appropriate approach to determiniing the reasonableness of the MNOs' termination rates …"

So we might in any event be called upon to give some guidance as to the relevance of all this to the proper application of the gains from trade test.

MR. READ: Of course it is BT's fundamental point that the whole approach that Ofcom has actually taken to this is flawed.

MR. SCOTT: No, I entirely understand that, but ----

MR. READ: We would probably, in the context of that, be adopting, I suspect, a similar approach to what the Altnets would be doing about saying how exactly the test should be applied, or the correct test that should actually be applied.

MR. SCOTT: From the point of view of us making a judgment, were we to find the gains from trade was an appropriate approach that would necessarily mean that we would find that it had been applied in an appropriate way, and that would then take us back to the considerations to which Ofcom should have had regard in applying it. As I understand it, that would then take us back into how far they should have had regard to these matters.

MR. READ: That is absolutely right, in my respectful submission, because all BT is looking at and defending here is saying that Ofcom have actually got the construction of the contract right. In so far as that was an essential part of their determination then, yes, BT accepts and agrees with that, but of course it all starts from the proposition that BT does not accept that it got it right. I think the point is whether or not in that context you might have regard ---- I think there are two separate things here. The first is whether or not the evidence and the arguments that are being raised, the very fact that we have got the Altnets and Vodafone raising these points here, whether or not it actually supports at the end of the day Ofcom's overall approach to the dispute determination and in particular the consideration of whether BT could retrospectively pass these charges through, that obviously is a question for determination. If and in so far as ultimately BT is still forced to have to retrospectively charge down the line through its contract then there may be different issues, but they will be call based rather than tribunal based. I think that is probably the answer.

THE CHAIRMAN: Nobody has ever suggested that you should have to pay the full readjustment if it is not the case that you can go back and collect it from the transit customers. So the choice that Ofcom had was if it is not right that you can collect it from the transit customers

then you should only have to pay the difference the breakeven charge and what you have paid. If it is right that you can recover it then you should have to pay the whole amount, but nobody has suggested that you should have to pay the whole amount even if it is not true, and you cannot recover it from the transit customers. What you are fearful is that we will decide that it is the case that you can recover it from the transit customers and therefore you should be liable to H3G for the whole of the back-payment and yet in some later proceedings it is held that actually you cannot recover it, but that is not anything that Ofcom has ever suggested is possible.

MR. READ: No, but it does form, if I can put it in this way, part of our notice of appeal, because we say that the tests that Ofcom have applied are inherently flawed, and this is actually an illustration of it.

THE CHAIRMAN: Yes, we have got that.

MR. READ: Subject to that point, I agree, madam, that it has not been put at any stage on that basis in terms of our recovery of H3G charges.

The way that Ofcom appear to have applied this is to, in theory, give us the benefit, i.e. that we should not have to pay it, but then H3G pop up and say that, in fact, we should pay it because otherwise we will get a double recovery because we can recover this money under the contract and still not have paid them. Our simple answer to that is, "Well, actually that is quite difficult because of the very fact that the Altnets and Vodafone are here".

THE CHAIRMAN: Yes.

MR. READ: As the point on construction has been raised, BT really has not got much option but to argue its construction of the contract before you. I will try, therefore, to go through that as promptly as I can. Can I start by really looking at contract construction. I do not think I have ever been in a case before where a contract construction has been an issue but there has been virtually no authority to actually support a number of the propositions that are being put forward, certainly by the Altnets about how fairness and reasonableness comes into the equation and how, for example, the SMP condition must apply.

We have cited a passage **Chitty** in para.106 of our skeleton argument, which we say is the basic test to be followed in contract construction. If you want to have a look at it, it is bundle A, tab 9, p.38 of the internal numbering. If one is looking at the issue of contract construction the starting point is to ascertain the intention of the parties, but one ascertains it objectively. That starts from the document itself, what it would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation they were at the time:

> "The cardinal presumption is that the parties have intended to say what in fact they said, so that their words must be construed as they stand. That is to say that the meaning of the document or of a particular part of it is to be sought in the document itself …"

In other words, the starting point for this is that it is an objective test, it is what a person construing, firstly, the document would reasonably understand it to mean. It does not take into any account the subjective intentions of the parties when they entered into that contract, and that is quite important when we come on to look at the issue of what may or may not have been said by any of the BT employees.

Of course we accept that in construing a document you are entitled to have regard to the factual matrix that is around at the time that the contract is entered into. That again we say is quite an important point in this case, because of course you are being referred to SMP conditions entered into in 2003 long after, when we know, because we have just been looking at the 1997 version of the SIA, long after the contract terms have already been drawn up and considered by the parties. We say it is really straining contractual interpretation to say "This seems to be inconsistent with an SMP condition imposed many years later", and you have to interpret those contractual documents in light of something that happened years after the event. That is not how you approach the construction of a contract in our respectful submission. Obviously, I am concentrating on the contract rather than on what may or may not be the regulatory position further down the line, but in terms of construing the contract you look at what was there when the parties entered into the contract. We know, for example, from the Orange case, I think it was 1995 that the SIA was entered into there, and I do not think there was any doubt that all of these contracts would have been entered into well before 2003. So any assumption that you can apply consistency from a document made long after the terms had been agreed just does not work as a principle of contractual construction, so that is what we say is a key starting point.

There also appeared to be suggestion that this contract has to be construed with the common regulatory framework. Well, with respect that is not right, and indeed there is the case of *White v Waring* which was the Motor Insurers' Bureau case and we can get hold of it if need be, which says the complete opposite, that you start from looking at the contract and the key to it is construing the contract.

It may be that in the context of the regulatory framework, because there is an inconsistency with an SMP condition the contract subsequently has to have been altered. I am not suggesting in any way that the contract can bar regulatory intervention, all I am saying is

that if you are construing a contract you do not construe it simply by the terms of other material that may have a bearing in a regulatory context.

Against that I think it is quite clear that it is being accepted now, and I suspect this is as a result of having set the arguments out in some detail in BT's statement of intervention that absent of anything else it is quite clear that BT is entitled retrospectively to recover the moneys back in this situation under clause 12, certainly when construed with clause 13 of the main body of the agreement, that is what is meant by "retrospective" in this instance.

Madam, I can take you back through the statement of intervention and actually demonstrate that again, but I really apprehend the way Mr. Cook put it, and Mr. Wisking put it, that they were not really relying on any argument that 12.3 – certainly when interpreted vis-à-vis clause 13 – actually results in BT being unable to do what it has done.

The whole gist of it seems to have been put upon firstly the carrier price list and that does seem to be actually when he was driven to it the fundamental for saying that the contract has been varied. Secondly, there were hints of "Well, there is the SMP condition, there is what the employee said …" etc. If I can just deal with the last two first.

As regards what the employees may or may not have said then it is as plain as a pikestaff that that cannot be used as a means to interpret a contract already in existence; it runs contrary to the principle that is set out in the passage in **Chitty** that I have cited in para.106.

Also, Ofcom have correctly identified the *James Miller v Whitworth* authority (House of Lords' authority) in their defence which again makes it absolutely clear that what the parties say or understand their contract to mean after it has been concluded cannot be used as a guide to construing what it actually means. If one only thinks about it for a moment one sees why that is ----

THE CHAIRMAN: But I think their point goes a bit beyond that to saying that there may or may not be an estoppel.

MR. READ: Well that is right, madam, but for the reasons I have already said we agree with Mr. Wisking that that is not something that you can possibly be in a position to deal with and, madam, I have already dealt with that point. I wanted to make it absolutely clear that in construing the contract that is a complete irrelevance.

The second point is the SMP condition ----

MR. SCOTT: Sorry, just before you leave the price list, my recollection ----

MR. READ: Well I was coming back to it. I was trying to knock out the obviously demonstrably wrong points and then go on to the still wrong …(Laughter) … but perhaps lesser points.

The other point is the SMP condition. For the reasons I have already indicated, you cannot use that as a guide to construing a contract that had already been formulated many years before. It is simply not the way that you work with contract construction. I can spend some time going through knocking down each point why we say that in fact looking at the SMP conditions is actually flawed. One has to also put this in the context that this contract has been around for a long time, and if people really felt that this contract was infringing the SMP conditions one might have expected someone to do something about it if not before, certainly after this matter has come to light in the context of the ----

THE CHAIRMAN: I do not think the point was really that you have to construe it, or that the SMP condition is an aid to construction of the clause, rather that you can only enforce the clause insofar as it is not inconsistent with the SMP condition.

MR. READ: My learned Junior is actually pointing out we do not think that is the way it was being put we think it was being put on construction, and we think that the reason why Mr. Cook was putting it on construction was because that is actually the only way he can get the SMP condition in because it comes back to the distinction between the contractual interpretation and the regulatory framework that may happen and be imposed upon you independently of it, and if you are looking at contractual construction the only way, it seems to us – and we apprehend it was the way that Mr. Cook was putting it – is to say that you have to interpret the contract in order to be consistent with the SMP condition. Matthew is about to tell me I am wrong.

MR. COOK: I am about to agree with both of you actually. I was putting it on both grounds. I am saying that it is something that should be influenced as a matter of contractual construction, but ultimately it does come down to the fact that if construction only gets you so far you reach the stage where you say it can only be enforced to the extent that it is compliant with the conditions.

MR. READ: That is helpful, madam, I think I have dealt with one of those limbs. As regards the second limb, well that is a regulatory matter and not a contractual interpretation matter, but I do make the point very forcefully that if this really was such a big issue one might have expected the regulator, who is fully aware of the position, to have taken a view on it one way or another, and the regulator has not.

Can I now turn to the carrier price list? I think Mr. Cook slightly mischaracterised us by saying we just called it “Delphic” and nothing else. We did say in terms that we thought, when one looked at it, that what was being involved here was BT offering a service to BT’s

customers, and one can see that in para.32 of our statement of intervention, which is at bundle D3, tab 14, p.252.

THE CHAIRMAN: This is looking at it in a different place from where we were looking at it before.

MR. READ: Yes, sorry, madam, I have done that so you can actually see the arguments and the way we have actually approached it . The note is set out again. In para.32 you can see what we are actually saying about the note, that it:

> "… appears to be an observation about BT's billing team only *offering* a service to BT's customers which allows those customers one month backdated billing."

THE CHAIRMAN: Those are transit customers?

MR. READ: Those are transit customers.

THE CHAIRMAN: And do they pay prospectively for their ----

MR. READ: Well, we did think about trying to give some evidence on this point, but unfortunately, as I pointed out, that brings one back into the very legal floor that we accuse the other parties of, which is to try and use the intentions of the parties to explain what it meant. I can only but do it by reference ----

THE CHAIRMAN: So the first sentence you say is that they are offering a service to their customers that they will do backdated billing for transit charges, but only one month's worth?

MR. READ: Yes.

THE CHAIRMAN: What do you say the second sentence ----

MR. READ: The second sentence – to be absolutely frank there is something that has gone wrong here with this, because it really does not make sense, in our respectful submission, either way – the way that it is being interpreted by Mr. Cook or the way it has been interpreted by us. (laughter) I say that candidly because it could be much clearer, so you are actually at the end of the day having to decide between two competing, if you like, constructions of this note. But it does appear that one is looking at retrospection by Ofcom and if you link that with the first sentence what we say that that would actually mean is that if an originating network operator has been retrospectively determined by Ofcom and that service cannot be passed back down the line for one month.

I do not pretend in any way to say that this is particularly clear. We do say "Delphic"; we say "Delphic" because we say his construction is just as difficult in many respects as ----

THE CHAIRMAN: So let me get this clear, that you are then saying: "We will only provide you with one month backdated billing for transit charges, and even if Ofcom has retrospectively

set charges for you beyond that one month we will not provide you with billing", is that what you are saying?

MR. READ: That appears to be the interpretation that, if you like, gains most favour with BT, but I do make the point that it is not clear. I fully accept that, and that is one of the problems with trying to spell out from this note on the CPL a whole process of overturning the very clear scheme that has already been laid down by clauses 12 and 13 in the main body of the agreement.

I will just briefly take you, I think to the actual 2006 SIA just so that you know where it is in the bundle system, and also just to deal with what the carrier price list is. If one takes bundle F2 at p.371B one has the July 2006 version of the SIA. Madam, also included within the bundle, and if one goes on to p.371X one comes to annex D, which is the definitions' section. I know that you, madam chairman, will remember this, but in deference to your wing members, the SIA is of course the main body of the agreement, which is what we looked at earlier with Mr. Wisking. Then there is annex A which deals effectively with technically specifications. Annex B deals with various charges, how you actually operate charges. Annex C then deals with the schedules on which the prices are actually dealt with, and annex D deals with the definitions, and then there are various other annexes after that.

MR. SCOTT: It is incomplete, is it not, without the price list?

MR. READ: The price list is one further point. I cannot do this on the documentation before you, but certainly having perused this document on numerous occasions, what happens is that you have in annex C various schedules for the type of service that is actually being provided. Within those schedules there is normally a reference to the carrier price list so that you have the terms upon which that service is particularly provided and there is just a reference then to the prices being as are in the carrier price list. Indeed, the carrier price list was correctly described as an Excel spreadsheet document that just has ranges and ranges, and ranges of numbers, depending upon the particular category of schedule that they are derived from, listing out the prices. So, in fact, it is not a written document as the rest of the SIAs. It is actually an Excel spreadsheet document.

PROFESSOR BAIN: The whole thing, including those spreadsheets, constitutes the agreement.

MR. READ: That is absolutely right. But, if one wanted the whole agreement, then ----

PROFESSOR BAIN: I entirely understand why we have not got it with us, but I am concerned about the characterisation of the price list as in someway being subordinate - whereas in fact, as I understand it, the whole thing is the agreement.

MR. READ: Absolutely. I am not detracting from the fact that the CPL is part of the Standard Interconnect Agreement. If I had not made it clear, I should make it clear - it is one part, along with all the other annexes and the schedules to Annexe C, and so on, and so forth. So, yes, we fully accept that, and, of course, one does then come to the question of: Well, how does the contract itself define the method for resolving any inconsistencies between the various documentation?

I just want to conclude this by showing you the definition of carrier price lists which is at p.371GG. It is defined as the price list having that name which contains charges for a BT service or facility, charges in relation to network components, charges for services provided by the operator, and some other charges in the information. So, primarily, it is a document looking at the document which then feeds back, as I have already indicated, to Annexe C in the schedules that are within that.

The core point, in our respectful submission is: How does the contract itself approach the issues of construing the documents together? That is to be found at 371E, which, again, is the main body of the agreement -- the main terms. As one can see in para. 1 - Definitions of Interpretations - at para. 1.3,

> "The following documents form part of the agreement and, in the event of any inconsistencies between them, the order of precedence shall (unless expressly stated to the contrary) be as follows:
>
> 1) main body of agreement;
>
> (2) Annexe D (which is the definitions);
>
> (3) Annexes A, B, E, and F;
>
> (4) the specifications;
>
> (5) Annexe C; and
>
> (6) the carrier price list".

We say that if you are considering the construction of a contract, you have to construe it in accordance with the express terms of the contract as to how you deal with any potential inconsistencies between the various documents within it. We say this is a complete answer to the point that Mr. Cook is trying to build on the basis of the carrier price list. What, in essence, he is asking the tribunal to do is to say, "Yes, I accept that paras. 1.2 and 1.3 of the main body of the SIA would have this effect, but for this note in the CPL". We say that if there is an inconsistency between them, then at the end of the day 1.3 resolves the problem.

THE CHAIRMAN: It is not really an inconsistency though. It is an exception. Are you also saying, "Looking at the carrier price list, it says it contains charges and information. It does

not say 'charges, information and important exceptions to some of the clauses which are set out in the main body of this agreement'".

MR. READ: Absolutely, madam. In essence, what is being said is that the carrier price list is building in an exception to paras.12 and 13 of the main body of the agreement. We say that that is not the way you approach interpreting a contract - to say, "Well one little bit of the information stuck right at the end in the lowest of the batting order items of the documentation cannot have the effect of varying ----" We do say it is varying. It may be by way of saying that this is an exception, but it is still varying the clear terms of paras. 12 and 13 of the main body of the SIA.

One can get further assistance from that if one goes to p.371U in the bundle, which is Clause 30 of the main body of the agreement. So, again, under 1.3 there is important precedence to be given to this. 30.1,

> "Except as expressly provided in this agreement, no variation of this agreement shall be effective unless agreed in writing by the parties [plural] and signed by a person nominated in writing on behalf of: BT by the managing director; the operator by a director of the company or a company secretary".

THE CHAIRMAN: Presumably the CPL was signed in writing?

MR. READ: No, madam. There certainly is no evidence to that effect. But, I think, madam, it is absolutely certain that there will be no signatures on the CPL because it is simply a spreadsheet document that is circulated. I am sure that if it had been signed in any way someone might have identified that point because it is a point we raise specifically in our statement of intervention.

MR. COOK: Madam, might I just ask for clarification as to whether Mr. Read is in fact saying that the carrier price list is not a valid contractual document? If not, my clients will be delighted to take their money back from many other cases where they have paid some of the money ----

THE CHAIRMAN: No, I do not think he is saying that, Mr. Cook.

MR. COOK: Just to be clear exactly what he is in fact saying is his status if it is not ----

THE CHAIRMAN: I do not really quite understand the variation point. It does not seem to me that this was a contractual variation. It seems to me that one has to look at the CPL and try and work out what that second sentence means, having regard to how the CPL is described in the rest of the document. I do not think the variation point really takes you much further, Mr. Read.

MR. READ: Madam, that is probably correct because we say we did get to the correct construction in any event. But, what I am saying is that whether it is derived as an exception, or not, to Clause 12.3 of the main body of the agreement, if, in effect, you are going to put an exception on that, then you would need a variation to it because of the precedence that it is actually being given in the contract document. That is how we say 30 comes into play.

Mr. Cook's point is slightly different - to say, "Well, what is the effect of the carrier price list?" Answer, "The effect of the carrier price list is to state the prices that are very clearly described in the schedules to Annexe C". But, he is not looking at the prices. He is looking at a note that happens to have been in it. He is saying, in effect, that it has completely changed the position on paras. 12 and 13 of the SIA.

Madam, if you could just give me a moment, I will just check to see if there is any other point which I need to specifically deal with? (After a pause): Madam, I do not know whether it is really a serious live issue, but I will just mention it: of course, Vodafone do suggest in their statement of intervention that the appropriate course would have been for BT to have paid H3G's charges under protest, pass them on to the transit operators, and then pursue a dispute with Ofcom. Madam, you, I know, are aware of how the Clause 13 procedure operates. That simply is not tenable under the Clause 13 procedure. It is not an option that would have been there. We would have been having an Orange preliminary issue, no. 2 at the very least. I would suspect that Ofcom would quite rightly say, "Well, if there's no dispute, why are we going to get involved in this? You have accepted it. There is nothing under the contract still in argument". Madam, we do not think there is anything in that point.

Madam, unless there is anything I can help you further on, those are our submissions.

THE CHAIRMAN: Thank you very much. Miss Rose, do you have anything you want to say on this issue?

MISS ROSE: I do not.

THE CHAIRMAN: Mr. Turner, I think your moment has finally come.

MR. TURNER: It will be a concise moment, madam. First, just to clarify what I was saying before, we are obviously not pursuing this point on the construction of Clause 12.3.1 in the appeal. I should clarify that that is not a concession that Mr. Cook's admirable arguments are in any way wrong. Our point is simply that it is unnecessary to take that point, and we have concentrated out fire power on the plain and obvious mistakes made by Ofcom in the test which it adopted.

Madam, the tribunal raised the question yesterday at the outset as to the relevance of the costs recover issue, in principle because ordinarily where a charge has been determined as reasonable one would expect that to translate through directly into the remedy which is applied under s.190 of the Act. T-Mobile's position is that we agree with that analysis. Ofcom's need to make an adjustment in this case, therefore, is an anomaly. We say that if there is a need ----

THE CHAIRMAN: By 'adjustment' there you mean i.e. not making an order ----

MR. TURNER: -- that reflects the reasonable H3G charge ----

THE CHAIRMAN: Not backdating.

MR. TURNER: Yes - on the basis of the pass-through. Therefore, if there is a need for a correction, it ought to suggest that there is something fishy about the substantive test itself. This arises - if one thinks about it - because the core logic of Ofcom's test is the pass-through assumption. The point I was endeavouring to make at the outset today by reference to para. 133.1 of Ofcom's defence is precisely that they themselves say, "Our test at the first stage is not sufficient". They have said that without the pass-through assumption the upper bound of what is reasonable for the purposes of E-To-E would depend on the level at which BT has chosen to set its retail and transit prevailing prices. Clearly the reasonableness of a charge should not depend solely on the downstream pricing decisions. It is because of that that we come through to the pass-through part of the test. On that pass-through test, any proposed charge higher than BT's break-even can be passed through. The parties have made the point that there appears to be no clear limit to where that takes you . It is because of that test that we are into the need for a correction. So, let us appreciate why we are here. Having done that, we have two considerations that we would draw to the tribunal's attention - not because of what they say about the proportionality check in itself, but because of the light that they cast for the tribunal on the gains for trade test itself, and its justifiability. The first point, if the tribunal would pick up the BT determination in Bundle B, Tab 4 as the justification ----

THE CHAIRMAN: Mr. Turner, I do not want you to re-visit the submissions that you made in relation to the gains from trade test. You have had your time and submissions on those. The point that I was making yesterday was that if one does not apply the gains from trade test, is it relevant to the question of whether BT should have to pay a backdated adjustment if the reasonable rate is determined to be higher than what it has in fact paid over the period of the dispute -- is it relevant ordinarily that it can, or cannot, go back to its own customers to get the money?

MR. TURNER: Yes. The tribunal has our submissions on that. If the tribunal accepts our proposition that, for example, it is a cost based charge up to a point depending on the circumstances, then the answer is, "No there would be no need for a correction" and the analysis adopted by Ofcom would not apply. Therefore, we agree with the tribunal's assumption and the remarks that, Madam Chairman, you made yesterday morning.

THE CHAIRMAN: Thank you. That is your submission?

MR. TURNER: That is our submission on that question.

Madam, the only point I was going to make - and I understand if you consider I am trespassing on what I ought to reserve for a written reply - is that when one looks at the proportionality test as it was applied by Ofcom in this case, it also tells you something further about the incorrectness of the gains from trade test as a whole. But, I am happy to reserve that.

THE CHAIRMAN: Thank you. Mr. Roth?

MR. ROTH: Madam, I would ask, if I may, for about ten minutes. I had not thought I would need them from what I had indicated earlier, but having listened to Mr. Read and the opening submissions he made on SIA, there is a point that I need to respond to. I will not be getting into the detail of the construction of the BT contract. It is really about the ambit of this point. Mr. Read said at the outset that it affects, or infects, the gains from trade test and pass-through, and Ofcom's overall approach. We, with respect, strongly refute that. In fact, it goes, we say, to only a very small part of the BT determination -- it obviously has no effect at all on the MNO determination, but even in the BT determination. That is with regard to the H3G charge and, specifically, the remedy with regard to that charge. If this were all on a prospective basis, then, of course, this issue would not arise. It is all about whether, on the true construction of the SIA, there can be retrospective recovery. This is all about the remedy. The charge proposed by H3G was assessed as being reasonable. One can see that in the determination at Bundle B, Tab 4. Mr. Read referred rapidly to various paragraphs without taking you to them, and I must ask you, please, if I may, to look at them. One can see quite clearly how this arose.

At para. 4.98 you get the conclusion in the reference to the draft determination - a finding that by applying the gains from trade test and pass-through,

> "Ofcom's provisional conclusion was therefore both sets of H3G charges were reasonable".

That then fed through. There is discussion about O2 and T-Mobile. It fed through to paras. 4.110 to 4.112, where, in para. 4.110, Ofcom notes that this is the first time it has been

asked to resolve this, and so on, and that there may have been genuine uncertainty. The last sentence of 4.111,

> "In not passing through the higher charges, customers who have benefited through the payment of a lower charge and Ofcom considered that, in those circumstances where there may have been genuine uncertainty as to the prices which Ofcom would uphold as reasonable under the end-to-end obligation, it would be disproportionate to require BT to incur a loss as a result of the remedy Ofcom is imposing in determining the dispute.
>
> In the light of this, Ofcom's provisional conclusion as set out in the draft determinations was that the proportionate remedy is to determine that BT should be required to pay to H3G amounts which reflect the break-even charge - which is Ofcom's estimate of the highest price that H3G could have charged BT without imposing a loss on BT ----"

That is then set out. The figure is quoted. So, that is what Ofcom was proposing to do. Although the higher charge had been held to be reasonable because of those circumstances the provisional view was the proportionate remedy in the situation where it was entirely retrospective basis was only to allow H3G to recover at the breakeven point.

That draft determination H3G responded to in s.6. At the very end of s.6, p.55 in the document, 6.55 records H3G's response. This is how the whole matter arose:

> "H3G has also stated in response to the draft determination that under Clause 12.7 of the SIA BT would be able to recover the full costs of H3G's proposed termination charge increase from originating operators. As Ofcom had determined this charge was reasonable under the E-To-E obligation, H3G has stated that Ofcom should require that BT repay the full amount of this proposed increase to H3G - not Ofcom's calculation of BT's historic break-even charge to H3G".

H3G is referred to Clause 12.7 in support of its argument that,

> "BT is able to claw back any additional amounts from originating operators and BT refers to Clauses 12 and 13 of the SIA in the same respect. Clause 12.7 refers only to the provision setting out the means of recovery which is a consequence of the operation of Clause 12.3. Clause 12.3 provides ----"

It is set out. Then you see set out below Ofcom's understanding of Clause 12.3.1.

THE CHAIRMAN: You are not saying that as a general rule before you apply s.190(2)(d) in order to order a back payment you have to check whether the person who has to make that

back payment can in fact go back and collect the money from all the people who it traded with over that period?

MR. ROTH: Absolutely not.

THE CHAIRMAN: No. It finds the money wherever it can.

MR. ROTH: That is correct. It is just this very special situation where one felt that where normally one would, it would not be proportionate here because of what had happened. The point that was put to us to H3G when we thought it was not proportionate -- We go to BT, saying, "What do you say about it?" at 6.58. They come back, saying that that they agree with that as the legal position. They say it is their current interpretation of the relevant provision.

THE CHAIRMAN: It puts them in a bit of a spot, does it not?

MR. ROTH: They could say that it is unclear, or that the position is complicated. They go on to talk about commercial considerations, which we felt was not relevant. Then we go to 8.9 -----

MR. READ: Madam, while you are there, can I just ask you to read para. 6.5.9 which actually sets out part of BT's reasoning? (Pause for reading)

THE CHAIRMAN: That seems to be making the point about whether Ofcom should have taken into account not only all the contractual issues that we have considered - whether or not those include just looking at the terms of the contract, or looking at contractual issues such as estoppel, but also whether it should have looked at commercial issues. Well, even if it is true that BT can go back to the transit customers, is it actually feasible commercially for it to do so? You are saying, "Well, we cannot possibly make a decision about that".

MR. ROTH: Yes. I think I addressed that earlier, and I think I did read it out earlier in my submissions.

That was the response to the draft determination. Then one goes to the actual conclusions which is s. 8, starting on p.61. At 8.9 Ofcom considers the charges proposed by H3G to BT on 22nd November, 2006 are reasonable charges in the context of end-to-end obligation. But (at 8.11), As set out in paras. 6.56 to 6.60, following H3G's response to the draft determinations Ofcom asked BT for its view on whether it could recover the full costs of H3G's proposed increase insofar as the costs of that increase relate to traffic transited to BT from other originating operators and not traffic originated on BT's own network. As this means that BT would not be required to absorb a loss if it was required to make payments to H3G in relation to transit traffic, Ofcom's conclusion in respect of the dispute between BT and H3G now takes this into account.

Then one gets the final position that therefore it is proportionate to reduce the recovery by means of the remedy.

Then one goes to the actual determination where Mr. Read took you at p.74. He suggested that this had affected the actual determination of the charge. But, with respect, that is simply not right. Paragraph 1 on p.74, the charges contained in the letter of H3G to BT of 22nd November 2006 are reasonable charges. So that is entirely consistent, of course, with what one has read.

THE CHAIRMAN: They are reasonable because you can pass them through, you say, but one does not need to rely on clause 12.3.1 in order to pass them through prospectively you just put your prices up and the prices can be put up by ----

MR. ROTH: That is right, you just pass them through prospectively. But then there is in para.2 the remedy, and while normally, as you said, madam chairman, it would just follow, but here it is in those figures that the adjustment comes down because the remedy has to be proportionate, and because of these particular circumstances it is reduced, and so it is only dealing with remedy. Ofcom had to take a view, given what was being said to it, and now both sides to the contract are here, it is a standard form of contract between various parties, and Ofcom as regulator has no particular concern to favour one construction or the other construction.

THE CHAIRMAN: Well you are trying to resolve a dispute between BT and H3G, and the question is as regards H3G, should they be kept out of their money for any reason? You say that it would have been fair to keep them out of their money if BT was being forced to make a loss on these sales, but not if they were not – if they choose to make a loss for commercial reasons then that is fair enough, but that is no reason why H3G should not have the full benefit of your determination.

MR. ROTH: Exactly so, and H3G having raised the point firmly before us we had to address it, and we went to BT and those are the answers we got. One may feel, having listened to all this, that perhaps it would be better if Ofcom had not gone down that road and had said to H3G "Well, no, we do not want to be concerned with that". But doubtless if we had then put the figure down and not at the level that has been termed as "reasonableness" H3G would no doubt have appealed that point and we would be having exactly the same argument in reverse.

THE CHAIRMAN: What you could have said, I suppose, was "Well, BT, you are a very large company, you can find this money from somewhere else, you do not have to go back to

your customers, and H3G is entitled to it. We have seen that you thought that that was a proportionate way to ----

MR. ROTH: That is how we approached it, yes. So that is what we did and, as I say, if the construction is wrong then results follow, but as a regulator that does not raise any issue of regulatory policy for Ofcom at all, and I am not going to address you on the details of the construction of either the clauses or the mysterious carrier price list. (laughter). So that is all madam, that I wish to say on that point.

THE CHAIRMAN: Thank you very much, Mr. Roth. I think that concludes this hearing. A number of matters just to mention.

The TRD appellants are going to serve written replies.

MALE SPEAKER: (No microphone) … SIA issue, I would hope it does.

THE CHAIRMAN: Yes, if you want to serve a reply, then yes, you are entitled to do so, yes. At the moment we were considering setting next Wednesday as the time for those on the basis that we realise that the longer we give you the longer the replies are likely to be … (laughter) … and that the parties should not really feel that they have to put in anything more substantial than they would have said had they replied in an extemporary manner as is usually the case, but Mr. Read, you still ----

MR. READ: Well, madam, as the person who actually said we should be dealing with replies this afternoon I do not think I can be blamed for standing up and therefore asking could we have an extra couple of days to deal with it? I am personally in great difficulties this week, so I cannot get around even to looking at the transcripts this week, and it would be of assistance to us if we could have two extra days until Friday.

THE CHAIRMAN: So to Friday of next week – nobody objects to that, presumably? So that is 15th February. Having now dealt with all the issues in this hearing, the spill over days that we had set aside in February do not need to be used for that purpose. We have however slotted into the 25th February the hearing in relation to the formulation of the questions to be referred to the Competition Commission in the BT and H3G MCT appeals. It is difficult for the Tribunal to predict at the moment before seeing the parties' submissions how long that is going to take, but we would hope that certainly 27th, insofar as it was held in reserve for the spill over should be able to be released, and so we will limit those days to 25th and perhaps a bit of 26th February.

The timetable for the non-core issues, there was a letter setting out what the parties had agreed, I cannot now remember who had written that letter – BT I think wrote to the

Tribunal setting out the agreed timetable, leading up to the hearing on 31st March, I think that is right, the Tribunal is happy with those times, and will make an order accordingly. I would like to express our thanks, and the thanks I think of everyone in this room to the transcribers of these proceedings for the marvellous job that they have done in producing the transcripts so accurately and thoroughly and with such rapidity, and my wing members and I would also like to express our thanks to you for your very clear and helpful submissions which have greatly assisted us in the task we now face.

(The Tribunal confer)

THE CHAIRMAN: Yes, Mr. Roth, you wanted to say something?

MR. ROTH: Yes, may I just add two very brief postscripts. First, on our behalf on this side, but I suspect on behalf of all the advocates may I express our thanks to those in Baker & McKenzie, and I suspect they are rather junior individuals, who prepared the bundles; they have been done, without wanting to sound pompous, in my experience with really exceptional good sense and diligence to avoid duplication and the way it has been arranged, and it has been of great assistance to those of us having to work on what, on any view, is a very heavy case.

Secondly, as regards the issue of the price control questions and the hearing on 25th and perhaps 26th February, I suspect we have all found the benefit of having a timetable for submissions for the day, and discovered that if two days are set aside counsel will make sure it extends for two days, and maybe we can do it more shortly. May I respectfully suggest that we seek, obviously also in discussion with counsel for the Competition Commission who I think will be addressing you as well, to agree a timetable for submissions which we can send to the Tribunal. If we cannot agree, then maybe there are two alternative timetables that can be sent, but pursuing Professor Bain's analogy from another part of the case you would not be restricted to adopting a timetable within the two parameters you have set your own timetable, which could be outside them and then we would all have to stick to that, and I would hope that would help – maybe it can even be done within one day.

That is all that I wish to add, thank you.

THE CHAIRMAN: Thank you very much.