



Replicability: the regulation of BT's retail business exchange line services

Consent

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Section 1

Introduction

Summary

- 1.1 On 28 November 2003, Ofcom published the market review entitled *Fixed narrowband retail services markets*¹ (“the retail market review”) in which, amongst others things, Ofcom concluded that BT had significant market power (“SMP”) in the provision of retail residential analogue and digital exchange line services and business analogue and digital exchange line services. As a result, Ofcom imposed a number of obligations on BT and these included SMP services Condition D3 which requires BT to publish charges, terms and conditions and notify Ofcom of amendments to them (“the requirement to publish charges SMP services condition”). The requirement to publish charges SMP services condition ensures transparency and means that Ofcom and BT’s competitors can monitor prices to check against behaviour which might be anti-competitive. The retail market review also imposed an obligation on BT not to discriminate unduly (“the no undue discrimination SMP services condition” – SMP services Condition D2).
- 1.2 For some time, however, Ofcom has been asked by business customers, as well as BT itself, to allow BT to respond to the demands of individual business customers by offering unpublished bespoke prices for services in business retail markets. The requirement to publish charges SMP services condition presently prevents this. Publication of prices can, however, lead to price following and Ofcom’s current interpretation of the no undue discrimination SMP services condition, which is that Ofcom assumes that bundles of SMP and non-SMP products would be likely to be unduly discriminatory, means that BT’s ability to tailor packages is limited. Both can reduce competition in retail markets.
- 1.3 Ofcom recognised these potential weaknesses and accepted that, once wholesale inputs were of sufficient standard to enable other Communications Providers to offer retail services that were commercially and technically replicable to those that BT might offer, the requirement to publish charges SMP services condition could be disapplied for certain customer types. Additionally, Ofcom stated that it would no longer presume that bundles of SMP and non-SMP products were likely to be unduly discriminatory under the no undue discrimination SMP services condition.

The April 2006 statement and replicability

- 1.4 On 12 April 2006, Ofcom published the statement entitled *The replicability of BT’s regulated retail business services and the regulation of business retail markets* (“the April 2006 statement”)² in which it stated that should BT address certain specific deficiencies with wholesale line rental (WLR) (see paragraph 1.8 below), carrier pre-selection (CPS) and low bandwidth leased lines, Ofcom would consent to the non-application of the requirement to publish charges SMP services condition. To begin with, Ofcom explained that, the consent would be limited to offers made to customers with an annual spend with BT in excess of £1million per year on a projected basis (assessed on the basis of anticipated spend in the next 12 months consequent on BT being awarded the contract for which it would be bidding). These customers are subject to close account management by senior BT staff and, therefore, it can be

¹ http://www.ofcom.org.uk/consult/condocs/narrowband_mkt_rvw/fixednarrowbandrsm.pdf

² <http://www.ofcom.org.uk/consult/condocs/busretail/statement/statement.pdf>

expected that BT would be better equipped to ensure that the company did not violate competition law rules and behave anti-competitively. Additionally, Ofcom considered that any deregulation at the retail level would need to be accompanied by additional provisos intended to control BT's behaviour given that it retains SMP in the relevant markets. These provisos are set out in paragraph 1.15 below.

- 1.5 Ofcom also explained in the April 2006 statement and the earlier statement entitled *BT's pricing of services for business customers* ("the May 2004 statement")³ that service bundles which mix SMP products and non-SMP products would no longer be presumed to be discriminatory once BT's retail services could be replicated on the basis of wholesale inputs. Ofcom explained in the May 2004 statement that competition law should be sufficient to deal with the risk of anti-competitive behaviour and a reduction in retail regulation was consistent with the European framework which states that remedies should be targeted in upstream markets.
- 1.6 The April 2006 statement further explained that BT had to judge whether it had or had not resolved the outstanding issues which were believed to be a bar to replicability. Once it believed that the outstanding issues were resolved, Ofcom expected BT to write to Ofcom and provide evidence that this was the case. Ofcom would then need to determine whether or not the outstanding issues had been resolved satisfactorily and no longer constituted a bar to replicability. If they were, Ofcom stated that it would consult on the draft form of Consent as required by section 49(4) of the Communications Act 2003 ("the Act") and disapply the requirement to publish charges SMP services condition for certain customer types. Ofcom added that BT need not wait until it had resolved all the outstanding issues with each product set (WLR, CPS and PPCs) before writing to Ofcom. Instead, Ofcom explained that each product set could be examined individually.
- 1.7 On 17 November 2006, BT wrote to Ofcom stating that it believed that it had resolved the outstanding issues in relation to WLR ("BT's request for consent") and that the solutions put in place were stable and meant that other Communications Providers could replicate retail business analogue and digital exchange line services on the basis of WLR.

WLR and retail business exchange line services

- 1.8 Ofcom explained in the April 2006 statement that retail analogue and retail digital business (ISDN2 and ISDN30) exchange line services could not be considered to be replicable until BT had resolved certain issues in relation to WLR. Ofcom considered that competitors utilising WLR were not able to offer a commercially and technically replicable service to BT Retail until the following matters had been addressed:
 - provision of call mapping on UXD5 exchanges to facilitate services such as 1571 voicemail;
 - availability of pre-validation to reduce order rejections;
 - elimination of the disparity in provisioning times between WLR and BT Retail exchange lines;
 - commitment to parity with respect to the forecasts for the WLR3 product;

³ http://www.ofcom.org.uk/consult/condocs/pricing_business_customers/ofcom_statement/business_pricing.pdf

- provision of improved and consistent eCo repair availability; and
- provision of improved access to appointment books in line with BT's relevant undertaking.

1.9 BT's request for consent explained that:

- BT's Switch Upgrade Programme enabled the provision of network services on UXD5 exchanges from 28 April 2006;
- the functionality enabling pre-validation was delivered on 15 April 2006 and the service was provided with effect from 26 July 2006;
- BT has ensured that for a sustained period the disparity in the provision of services to BT Retail customers and customers of WLR providers has been closed;
- forecasting is not required for WLR3;
- eCo repair was consistently available for the required minimum period of three consecutive months; and
- improved access to appointment books was delivered on 24 April 2006.

The March 2007 consultation

1.10 On 1 March 2007, Ofcom published the document entitled *Replicability: the regulation of BT's retail business exchange line services*⁴ ("the March 2007 consultation") in which Ofcom explained that in its opinion BT had resolved the outstanding bars to replicability in relation to WLR. Ofcom explained, therefore, that it intended to disapply the requirement to publish charges SMP services condition to the extent that it applied to businesses spending in excess of £1m per annum on BT's communications services. Ofcom also stated that mixed services bundles involving digital and analogue exchange line products and non-SMP products would no longer be presumed to be unduly discriminatory.

Respondents' views

- 1.11 BT welcomed Ofcom's conclusion that Communications Providers utilising WLR were able to offer retail business analogue and digital exchange line services that commercially and technically could replicate those that BT Retail might choose to offer. BT therefore supported Ofcom's proposal to disapply regulation in the manner described in the March 2007 consultation.
- 1.12 Other respondents strongly disagreed with the proposal. First, they disagreed with the concept of replicability and believed that it sat uncomfortably with the Undertakings given by BT under the Enterprise Act 2002 ("the Undertakings")⁵ and the concept of equivalence of inputs. Second, they did not believe that business retail analogue and digital exchange line services were replicable in any case. Third, they also expressed concern about the practical implementation of the policy and Ofcom's

⁴ <http://www.ofcom.org.uk/consult/condocs/draftconsent/draftconsent.pdf>

⁵ <http://www.ofcom.org.uk/telecoms/btundertakings/btundertakings.pdf>

ability to ensure that prices for products would not fall below the proposed price floor. They also believed that they would not be able to monitor anti-competitive behaviour.

Ofcom's decision

- 1.13 Ofcom has given considerable thought to respondents' views and concluded that none of their concerns are sufficiently strong to convince Ofcom that its proposal needs to be revised substantially. It has, however, made some minor clarifications which are aimed at addressing a number of respondents' concerns particularly in relation to the safeguards put in place to ensure that BT keeps to the letter and spirit of the deregulatory approach.
- 1.14 The main reasons for not revising its policy are that:
- a) Ofcom considers that the bars to replicability set out in the April 2006 statement have been satisfactorily resolved and none of the other points raised by respondents have made Ofcom doubt that exchange line services could be commercially and technically replicated;
 - b) Ofcom considers that replicability, whilst being an intermediate step towards equivalence of inputs, is a different concept from equivalence as set out in the Undertakings; and
 - c) in the interests of transparency, Ofcom and BT have published the latter's Governance Process for Bespoke Pricing (see Annex 2 and www.bt.com) which Ofcom believes satisfactorily sets out the means by which BT will ensure that it meets the letter and spirit of the disapplication of the requirement to publish charges SMP services condition and the price floor as required by the Consent.
- 1.15 For these reasons, Ofcom has published at Annex 1 the Consent to the disapplication of the requirement to publish charges SMP services condition to the extent set out therein. As a result, Ofcom gives its Consent to the non-application of the requirement to publish charges SMP services condition in relation to the provision of business exchange line services to customers with an annual spend of £1m per year on a projected basis with BT on communications services in the UK. This would mean that the requirement to publish charges SMP services condition would no longer prevent BT from offering bespoke prices to these customers and that these prices need not be published. The Consent is, however, given on the provisos that:
- for SMP services, the price offered does not fall below a price floor which covers transfer charges for network components plus fully allocated retail costs; and
 - BT puts in place and maintains appropriate internal management systems to ensure that prices do not go below the price floor set out in the Consent.
- 1.16 Additionally, Ofcom will no longer presume automatically that bundles of retail business analogue exchange line services, business digital exchange line services, and non-SMP services are unduly discriminatory. Ofcom would, however, continue to presume that mixed service bundles involving inland calls and/or leased lines, which are not replicable, and products in non-SMP markets would be likely to be unduly discriminatory.

Next steps

- 1.17 The Consent to the disapplication of the publication of charges SMP services condition applies with immediate effect. However, the Consent could be withdrawn in the future should it no longer be possible, in Ofcom's view, for other Communications Providers to continue to replicate BT's retail business analogue and digital exchange line services. This might reflect a deterioration in the performance levels of the WLR analogue and digital business exchange line products or might be due to changes to either BT's retail analogue and digital business exchange line products or the WLR analogue and digital business exchange line products which, in Ofcom's view, might present a new bar to replicability or the re-emergence of an old bar to replicability.
- 1.18 Ofcom might in the future eventually extend the scope of the Consent to all customers of business exchange line services (i.e. including those with an annual spend with BT which is less than £1 million per year on a projected basis). Such an extension could be considered should Ofcom be satisfied that the application of the monitoring procedures set out in the Governance Process (see Annex 2) would also suffice to ensure compliance with the requirements identified in the Consent as well as competition law and BT's regulatory obligations more generally. Ofcom does not expect, however, to extend the Consent beyond that set out at Annex 1 for at least one year.

Section 2

Replicability of exchange line services

Introduction

- 2.1 Ofcom explained in the April 2006 statement that it did not consider that BT's competitors could replicate BT's retail analogue and digital business exchange line products through the utilisation of WLR. Ofcom considered that there were a number of deficiencies with WLR that were a bar to replicability. Ofcom explained, however, that once these bars to replicability were resolved Communications Providers would be able to commercially and technically replicate services that BT Retail might choose to offer and therefore certain retail regulation could be disapplied for some customer types. The deficiencies highlighted in the April 2006 statement were:
- an absence of call mapping on UXD5 exchanges which would be able to facilitate services such as 1571 voicemail;
 - a need to make pre-validation available to reduce order rejections;
 - a need to eliminate the disparity in provisioning times between WLR and BT Retail exchange lines;
 - a need to provide a commitment to parity with respect to the forecasts for the WLR3 product;
 - a need for the provision of improved and consistent eCo repair availability; and
 - a need for the provision of improved access to appointment books in line with BT's relevant undertaking.
- 2.2 The April 2006 statement explained that BT had to judge whether it had or had not resolved the outstanding issues which were believed to be a bar to replicability. Once it believed that the outstanding issues were resolved, Ofcom expected BT to write to Ofcom and provide evidence that this was the case. Ofcom would then need to determine whether or not the outstanding issues had been resolved satisfactorily and no longer constituted a bar to replicability. If they were, Ofcom stated that it would consult on the draft form of Consent as required by section 49(4) of the Communications Act 2003 ("the Act") and disapply the requirement to publish charges SMP services condition for certain customer types

BT's request for consent

- 2.3 On 17 November 2006, BT submitted its request for consent in relation to WLR. BT explained that it believed that it had resolved the outstanding issues in relation to WLR and that the solutions put in place were stable.
- 2.4 BT's request for consent explained that:
- BT's Switch Upgrade Programme enabled the provision of network services on UXD5 exchanges from 28 April 2006;
 - the functionality enabling pre-validation was delivered on 15 April 2006 and the service provided with effect from 26 July 2006;

- BT has ensured that for a sustained period the disparity in the provisioning of services to BT Retail customers and customers of WLR providers has been closed;
- forecasting is not required for WLR3;
- eCo repair was consistently available for a period of three consecutive months; and
- improved access to appointment books was delivered on 24 April 2006.

Call mapping on UXD5 exchanges

2.5 BT explained in the request for consent that it had enabled network services including 1571 to be available from 28 April 2006. This was relayed to Communications Providers on 24 February 2006 and the new functionality for UXD5 switches was set out in Openreach's *Briefing WLR020/06*⁶. Call mapping was one of a number of functionalities that were delivered on the same date.

Pre-validation

2.6 BT explained in the request for consent that the pre-validation functionality was delivered in the service provider gateway ("SPG") drop in April 2006. The functionality of pre-validation was set out in Openreach's *Briefing WLR023/06*⁷. The functionality was not available immediately because further views were needed on the legitimacy of passing through consumer information. Pre-validation was subsequently made available on 26 July 2006 as set out in Openreach's *Briefing WLR097/06*⁸.

Provisioning disparity

2.7 BT explained in the request for consent that the relative provisioning times for WLR and retail exchange lines requiring an engineering visit had dropped to a replicable level. The disparity between the two had been shared with the industry and, furthermore, Openreach stated that its immediate aim was to reduce the difference to less than 5% which equates to approximately one day or less. This target has been achieved consistently since September 2006 and frequently WLR Communications Providers have received a better service than BT Retail. This is shown in Table 1.

⁶ <http://www.openreach.co.uk/orpg/news/productbriefings/wlrdownloads/Briefing%20WLR020%2006.doc>

⁷ <http://www.openreach.co.uk/orpg/news/productbriefings/wlrdownloads/Briefing%20WLR023%2006.doc>

⁸ http://www.openreach.co.uk/orpg/news/productbriefings/wlrdownloads/Briefing_WLR097_06.pdf

Table 1 – Provisioning disparity between BT Retail and WLR

	Sept.06	Oct.06	Nov.06	Dec.06	Jan.07	Feb.07	Mar.07	Apr.07
Overall WLR	21.84	22.59	19.75	18.89	21.94	17.43	16.83	15.74
Overall BT Retail	20.6	21.9	20.9	19.4	22.70	19.7	17.8	18.1
Overall Difference	1.24	0.69	-1.15	-0.51	-0.76	-2.27	-0.97	-2.36
Different from WLR	6.02%	3.15%	-5.50%	-2.63%	-3.35%	-11.52%	-5.45%	-13.04%
Business								
Business WLR	21.63	22.45	19.53	18.72	21.73	17.18	16.59	15.58
Business BT Retail	21.2	20.3	21.4	20.0	23.30	20.4	19.3	19.4
Business Difference	0.43	2.15	-1.87	-1.28	-1.57	-3.22	-2.71	-3.82
Different from BT Retail	2.03%	10.59%	-8.74%	-6.40%	-6.74%	-15.78%	-14.04%	-19.69%
Residential								
Residential WLR	23.86	24.08	21.53	20.52	23.80	19.82	19.00	17.42
Residential BT Retail	20.3	22.6	20.6	19.1	22.30	19.3	16.9	17.4
Residential Difference	3.56	1.48	0.93	1.42	1.50	0.52	2.1	0.02
Different from BT Retail	17.54%	6.55%	4.51%	7.43%	6.73%	2.69%	12.43%	0.11%

Forecasting for WLR

2.8 BT explained in the request for consent that forecasting will not be required for WLR3.

Stability of eCo repair

2.9 BT explained in the request for consent that it achieved the stability target set out in the April 2006 statement by 12 July 2006. The stability requirement stated that Openreach had to demonstrate to Ofcom that the eCo repair platform was consistently available for a period of three consecutive months. The preceding 3 months had seen short duration interruptions to eCo repair and these had a minor impact on other Communications Providers. BT explained that reliability of the eCo repair platform had been achieved by:

- providing additional server capacity;
- deploying back and front-end code fixes;
- providing an alternative route via a separate website address;
- reducing systems clustering and improving load balancing;
- improving user interfaces; and

- providing for customer visits and diagnostics.
- 2.10 Ofcom has received no complaints from WLR Communications Providers with regard to the performance of the eCo Repair platform and is not aware of any significant eCo Repair specific outages since the three-month period of consistent availability was completed in July 2006. It is on this basis that Ofcom considers that eCo repair is functioning satisfactorily.

Improved access to appointment books

- 2.11 BT explained in the request for consent that improved access to appointment books was delivered by the software drop on 24 April 2006. This was relayed to Communications Providers on 24 February 2006 and was set out in Openreach's *Briefing WLR020/06*⁹.

Ofcom's view

- 2.12 Two of the requirements set out in the April 2006 statement (disparity in the provision of services and stability of eCo repair) were not, however, requirements that BT addressed at a specific point in time and therefore the improved performance in relation to both of these needs to be maintained. For instance, in terms of provisioning timescales, Ofcom would not expect the level of equality that has been achieved to change dramatically in favour of BT Retail as this might bring into question the replicability of retail business analogue and digital exchange line services. Also, the eCo repair platform needs to be available and stable consistently.
- 2.13 Nonetheless, Ofcom considers that, on the basis of the information set out in BT's request for consent, BT has addressed the issues that were identified in the April 2006 statement and, therefore, Ofcom has published the Consent which disapplies certain retail regulation. The applicable reduction in retail regulation for analogue and digital retail business exchange line services is explained in Section 4. The Consent is set out at Annex 1.

⁹ <http://www.openreach.co.uk/org/news/productbriefings/wlrdownloads/Briefing%20WLR020%2006.doc>

Section 3

Respondents' views

Introduction

- 3.1 Ofcom explained in the March 2007 consultation that it had reviewed BT's submission (as repeated in Section 2) and considered that BT had addressed the required functionality and/or service improvements in relation to analogue and digital WLR exchange line services that were set out in the April 2006 statement. It stated that on the basis of the new service functionality and/or service improvements that BT had delivered, Communications Providers could utilise analogue and digital WLR services to replicate exchange line services provided by BT.
- 3.2 BT agreed that other Communications Providers could use analogue and digital WLR exchange line services to commercially and technically replicate services that might be offered by its retail division. Others, however, did not. They believed that a number of barriers to replicability remained (see paragraphs 3.8 to 3.28) and that these needed to be addressed before retail price publication regulation was disapplied. They also raised a number of concerns in relation to the practical implementation of the policy and enforceability of the proposed price floor.
- 3.3 Additionally, respondents believed that replicability was a confusing concept and that it sat uneasily with equivalence as set out in the Undertakings.

The concept of replicability and the Undertakings

- 3.4 Ofcom explained in the April 2006 statement that the concept of replicability is distinct from the concepts of equivalence of inputs and equivalence of outcome as set out in the Undertakings. Replicability was discussed in depth for the first time in the consultation document entitled *BT's pricing of services for business customers*¹⁰ (October 2003) in which it was recognised that competitive conditions may not be homogenous within markets and therefore retail regulation might be able to be applied differently within them. The May 2004 statement concluded that once replicability was ascertained, and BT's competitors could replicate the supply of services on a basis which was technically and commercially viable, Ofcom would no longer presume automatically that bundles of SMP and non-SMP services would be unduly discriminatory. Ofcom had therefore given a commitment to make changes to regulation of BT's retail services when these services could be considered "replicable". Ofcom explained, however, that replicability could not be achieved as long as wholesale products were materially different to products supplied to BT's downstream divisions.
- 3.5 *The Final Statements on the Strategic Review of Telecommunications, and undertakings in lieu of a reference under the Enterprise Act 2002* ("the TSR Statement"), which were published on 22 September 2005¹¹, noted that the May 2004 statement had set out the circumstances in which Ofcom considered that it would be appropriate to allow BT to offer discounted prices for bundles of services. The TSR Statement also noted that Ofcom was consulting once more on the

¹⁰ <http://www.ofcom.org.uk/static/archive/oftel/publications/licensing/2003/price1003.pdf> - it had, however, been considered in the retail market review

¹¹ http://www.ofcom.org.uk/consult/condocs/statement_tsr/

replicability of retail business exchange lines¹² and also on whether deregulation contingent on replicability should be extended to include consent to offer unpublished bespoke prices¹³.

- 3.6 The extent of deregulation set out in this document falls far short of full deregulation in favour of a reliance on regulation of upstream wholesale markets, which is the goal identified by the strategic review. As such, deregulation contingent on replicability is an intermediate step on the deregulatory path identified by the strategic review. Replicability does not require BT to use the same gateways, systems and processes as other Communications Providers and is a different concept from equivalence as set out in the Undertakings.

Replicability of exchange line services

- 3.7 As explained in paragraph 3.2, respondents questioned whether retail business exchange line services were replicable and raised issues which they considered continued to be a bar to replicability. None of these were identified as potential bars to replicability in relation to exchange line services in the April 2006 statement. Ofcom has, nonetheless, set out below its views in relation to each of these additional points.

WLR3 and forecasting

- 3.8 Respondents queried how forecasting requirements in relation to WLR3 were relevant given that take-up of WLR3 remains low.
- 3.9 As explained in the April 2006 statement, BT had to give a commitment to provide parity with respect to forecasts for the WLR3 product. WLR3 will provide for parity in relation to forecasting requirements. It should also be noted that the nature of replicability is that BT must make available tools and products which allow others to replicate retail products BT might choose to offer; it does not depend on whether others choose to use those tools and products as this is outside of BT's control.

WLR and CDR delays

- 3.10 Respondents alleged that call data records (CDRs) were consistently delivered in breach of Openreach's service level agreements (SLAs) and this remained a bar to replicability.
- 3.11 Ofcom has been informed by Openreach that the drop in performance of CDRs noticeable last year resulted primarily from increases in volumes and that this was addressed through a software upgrade in September 2006. Openreach further explained that the extent to which Openreach has failed to meet its SLAs in relation to the provision of CDRs has been overstated due to reporting errors.
- 3.12 CDRs are, in any case, lists of call records which BT aims to make available on the data exchange distribution system (DEDS) in 99% of cases by 8pm the next working day. Ofcom considers, therefore, that they are not directly relevant in the context of replicability of exchange line services. Ofcom also considers that the availability of call records in line with SLAs is likely to be less of an issue in relation to large businesses in any case.

¹² http://www.ofcom.org.uk/consult/condocs/bt_retail/bt_retail.pdf

¹³ <http://www.ofcom.org.uk/consult/condocs/busretail/busretailreq.pdf>

- 3.13 Ofcom does not currently believe that the level of performance in terms of CDR delivery presents a bar to replicability.

Renumbering

- 3.14 Respondents explained that their customers were unable to retain telephone numbers when moving to a new address within the same exchange area unless the customer remained on the same remote concentrator unit or others that were located adjacently. They suggested that BT's customers could retain their telephone number should they remain on the same exchange and that this was unequal and therefore a bar to replicability.
- 3.15 Openreach has assured Ofcom that there are no differences in the restrictions that apply to WLR communications providers and BT Retail. Both can retain numbers should they remain within the boundaries of the serving exchange.

Network Call Performance

- 3.16 Respondents explained that BT Retail had direct access to BT Wholesale systems to log and report upon incoming CDRs to specified CLIs and that this functionality can be useful for small businesses who might wish to track, for instance, outgoing call performance without needing to acquire a private branch exchange which would enable them to track call information internally.
- 3.17 Ofcom understands that network call performance is a customer requirement for WLR3.
- 3.18 As stated previously, however, replicability is not the same as equivalence. Equivalence requires BT Retail to use the same systems and processes as other Communications Providers. Replicability does not.
- 3.19 It should also be noted that the Consent initially limits BT's freedom in relation to large business customers spending in excess of £1m per annum and, as such, Ofcom does not believe that the lack of availability of network call performance at the moment presents a bar to replicability.

Remote Call Forwarding on Digital Lines

- 3.20 Respondents explained that BT Retail is capable of supporting remote call forwarding (RCF) on digital lines whereas WLR2 does not enable other Communications Providers to do so. They stated that this functionality is important for certain customer types.
- 3.21 Ofcom understands that RCF has never been a key customer requirement for WLR2 and has not therefore been delivered. RCF is, however, a customer requirement for WLR3 ISDN and therefore is being considered as part of the design scope for the product.
- 3.22 As with network call performance, Ofcom does not consider that RCF is likely to be a significant issue for businesses spending in excess of £1m per annum. RCF is a product that is likely to be relevant to smaller business customers who do not have other more sophisticated means of managing their telephony services. Ofcom considers that the lack of availability of RCF does not present a bar to replicability in this context.

Operator Services

- 3.23 Respondents explained that BT Retail customers can dial BT's Operator Services on 100 and obtain, amongst other things, advice and duration of charges for individual calls.
- 3.24 Ofcom does not believe that this issue is relevant in terms of the discussion on replicability. Ofcom is of the view that there are no major barriers to entry for Operator Services and therefore it is open to any Communications Provider to set up its own self-provision of such services. Ofcom does not consider that this issue presents a bar to replicability.

Pre-validation

- 3.25 Respondents considered that the price for pre-validation on WLR2 meant that it was not economic to use the service.
- 3.26 BT is required under SMP services condition AA3 to ensure that charges for Network Access are reasonably derived from the costs of provision based on a forward looking long-run incremental cost approach and allowing an appropriate mark up for the recovery of common costs including an appropriate return on capital employed. Ofcom does not consider that this issue presents a bar to replicability because existing regulation prevents BT from setting excessive prices.

Line-tests via eCo for ISDN2

- 3.27 Respondents considered that line-tests for eCo repair were generally inconclusive and this necessitated manual intervention. This meant that on each occasion eCo for ISDN2 was used the Communications Provider would subsequently need to contact Openreach to resolve the matter.
- 3.28 eCo repair for ISDN2 was delivered in July 2006¹⁴. Ofcom has no conclusive evidence that suggests that eCo repair for ISDN2 is not functioning appropriately and understands that Openreach has not previously been informed of any problems either. Communications Providers experiencing problems with eCo repair for ISDN2 need to raise this matter with Openreach in the first instance to give it an opportunity to solve any problems or provide an enhanced solution. Ofcom does not consider that this issue presents a bar to replicability.

Practical implementation issues

- 3.29 Respondents raised a number of concerns in relation to the implementation of the proposals and these included: amortisation of costs; end of presumption that bundles of SMP and non-SMP products are unduly discriminatory; and issues in relation to the form of Consent and compliance monitoring more generally.
- 3.30 Ofcom has considered each of these points and sought clarification from BT where necessary. These are addressed below.

Amortisation of costs

- 3.31 Respondents wished clarity on how BT would amortise its costs. They suggested that BT may choose to amortise its costs over the length of the contract and include break

¹⁴ http://www.openreach.co.uk/orpg/news/productbriefings/wlrdownloads/Briefing_WLR092_06.pdf

clauses whereas competitors might choose not to do so because of the commercial risk involved.

- 3.32 Ofcom has included at Annex 2 a BT document entitled *Governance Process for Bespoke Pricing for Business Exchange Lines in accordance with the requirements set out in Ofcom's draft consent to the Regulation of BT's Retail Business Exchange Line Services* ("BT's Governance Process"). This document was set out in a confidential annex which accompanied BT's response to the March 2007 consultation. Ofcom has held discussions with BT since the end of the consultation period and obtained its agreement to the publication of this document. BT also intends to publish the document on its website (www.bt.com).
- 3.33 The publication of BT's document in this statement is for reasons of transparency only and should not to be regarded as an approval by Ofcom that the governance process proposed therein is always deemed to be an appropriate internal management system within the meaning of the Consent. Of course, Ofcom would have to consider any complaints or disputes in this respect on a case-by-case basis scrutinising all relevant facts and evidential documents that are available to Ofcom at the time.
- 3.34 The Governance Process explains that:
- "An analysis will be prepared to demonstrate that the combined single price for the business exchange lines and the non-SMP elements is above the 'price floor' over the term of the contract."
- 3.35 Ofcom sought clarity on what would happen should a customer switch between a standard BT contract and a bespoke contract or between bespoke contracts. BT explained that it would not intend to treat the early termination of a contract any differently to the way in which it treats the termination of standard contracts currently. This might mean that penalty clauses would be included to ensure that all costs are cleared to that point in time. Ofcom would, nonetheless, need to consider any complaints or disputes in relation to BT's behaviour in the same way in which it considers any other complaints or disputes.
- 3.36 Given these assurances and the assurance that relevant retail SMP services are replicable and relevant SMP wholesale services are available on fair, reasonable and not unduly discriminatory terms (where required), Ofcom believes that BT's competitors will equally be able to bear the risks of normal commercial trading.

End of presumption that mixed service bundles are unduly discriminatory

- 3.37 Respondents stated that ending the presumption that bundles of exchange line services and non-SMP services should no longer be considered to be unduly discriminatory caused them concern. They stated that it would be difficult to track instances of margin squeezes.
- 3.38 Ofcom explained in the May 2004 statement that mixed service bundles involving SMP and non-SMP products should no longer be presumed to be discriminatory once other Communications Providers could replicate services offered by BT Retail in markets in which it retains SMP. Ofcom reiterated this in the March 2007 consultation.
- 3.39 As Ofcom has stated, retail business exchange line services that comprise part of a bundle would need to be priced at or equal to a cost floor derived from transfer

charges and fully allocated retail costs and that other non-SMP products that are part of the bundle would need to cover their incremental costs.

3.40 This was explained in the April 2006 statement which stated that:

“any consent to BT offering unpublished bespoke prices for services from markets where it has SMP should be conditional on those prices observing a price floor equivalent to BT’s non-discriminatory transfer charges for wholesale services plus its Retail FAC” (paragraph 8.16)¹⁵.

3.41 Ofcom further explained that:

“any comparison of prices and costs should take place at the level of the bundle as a whole”¹⁶.

3.42 Ofcom accepts that the prices of individual elements of the bundle might not be visible because BT would not have to publish its prices of these bundles. This is presently also true of products in non-SMP markets.

3.43 Ofcom has, however, set a price floor and BT’s Governance Process explains how it intends to ensure, amongst other things, that prices do not fall below the price floor.

Consent and Compliance Monitoring

3.44 Respondents made a number of comments in relation to the March 2007 consultation and compliance monitoring more generally. Ofcom believes that the revised Consent (Annex 1) and BT’s Governance Process (Annex 2) address these issues.

3.45 In particular, following a comment made by one respondent, Ofcom amended the wording of paragraph 1 (b) of the Consent to clarify that the threshold of £1 million applies only to monies spent by a customer of BT on electronic communications services and associated facilities in the United Kingdom.

BT’s view

3.46 As explained in paragraph 1.11, BT welcomed Ofcom’s conclusion that Communications Providers utilising WLR were able to offer retail business analogue and digital exchange line services that commercially and technically could replicate those that BT Retail might choose to offer. BT therefore supported Ofcom’s proposal to disapply regulation in the manner described in the March 2007 consultation (and as proposed in the April 2006 statement). BT did, nonetheless, question the basis of the proposed price floor and questioned whether Ofcom needed to wait for 12 months before reassessing whether to extend the Consent to all businesses.

The price floor

3.47 BT explained that the price floor should be set at the level of transfer charges and its incremental retail costs rather than its fully allocated costs. BT argued that the use of incremental costs would be consistent with previous Ofcom decisions whereas the usage of fully allocated costs for the price floor was inconsistent with the approach used under competition law for the telecommunications sector.

¹⁵ <http://www.ofcom.org.uk/consult/condocs/busretail/statement/statement.pdf>

¹⁶ *ibid*

- 3.48 As explained in the April 2006 statement, Ofcom is of the view that the use of retail fully allocated costs remains appropriate. Although in the telecommunications sector LRIC is the floor below which a charge is presumed to be anti-competitive, this general assumption cannot be simply reversed. As a result, it is not in general sufficient for a price to be above LRIC to demonstrate that it is not anti-competitive. In the case of a multi-product firm with significant common costs such as BT, it is also necessary for the prices of each combination of products to be sufficient to recover the costs which are incremental to that combination but not to any individual product within it, that is, common costs. It may also be necessary to consider other factors such as whether low prices are targeted at particular rivals.
- 3.49 The April 2006 statement went onto explain that, in theory, a series of combinatorial tests could be conducted which, if passed, would ensure that all prices covered incremental costs and that in aggregate they were sufficient to cover common costs. However, because potentially there will be a large number of unpublished bespoke prices, Ofcom considers that it is not practical to carry out the relevant combinatorial tests for each such price. In addition, even if the combinatorial tests were satisfied, a pattern of pricing whereby bespoke contracts tended to be priced at or close to LRIC with common costs recovered elsewhere could itself be suggestive of anti-competitive pricing. In these circumstances, and as a first step in relaxing regulation, Ofcom's view is that it is reasonable to require bespoke prices to be above FAC. The effect of this of course is not to prevent lower prices being offered, but to ensure that any such prices are transparent and not targeted at an unduly narrow set of customers in a way which could be anti-competitive.

Assessing the effectiveness of BT's Governance Process

- 3.50 BT urged Ofcom to carry out its assessment of the effectiveness of the management systems put in place by BT to ensure that prices remained above the price floor after six months. It suggested that should Ofcom be satisfied that the systems are effective and functioning properly the Consent could be extended to all businesses. If not, the limitation could remain in place.
- 3.51 Ofcom considers that it is unlikely that it would have sufficient evidence in six months to properly assess the effectiveness of the management systems put in place. There is a limit to BT's flexibility at this point in time because the Consent relates to exchange line services only and therefore there might be little in the way of meaningful data available after six months. Ofcom does not, therefore, intend to assess the effectiveness of BT's management systems in six months' time as proposed by BT.

Section 4

The Consent

Publication of prices

- 4.1 As explained in Section 2, Ofcom believes that BT has addressed the issues that were in need of resolution. Also, as explained in Section 3, Ofcom does not consider that respondents' concerns are sufficiently robust individually or collectively to make Ofcom re-think its policy in relation to replicability. Ofcom considers that analogue and digital WLR business exchange line products enable other Communications Providers to replicate commercially and technically retail business analogue and business exchange line products that BT Retail might choose to offer.
- 4.2 Ofcom has concluded, therefore, that it should disapply the requirement to publish charges SMP services condition to the extent that it applies to businesses projected to spend in excess of £1 million per annum (assessed on the anticipated spend in the next 12 months consequent on BT being awarded the contract for which it would be bidding) on BT's communications services. The Consent applies to BT's UK communications business only and to products and services that are inextricably linked to communications services (e.g. information technology equipment).
- 4.3 Ofcom considers that these customers are subject to close account management by senior BT staff and, therefore, it might be expected that BT will be more able to ensure compliance with ex-ante conditions and competition law. BT's Governance Process supports this view.
- 4.4 The disapplication of the requirement to publish charges SMP services condition in this case means that, to the extent that it applies to services sold to customers whose spend is projected to be in excess of £1 million on BT's UK communications services, BT:
- need not seek Ofcom's consent should it choose to deviate from its published price list;
 - need not publish retail analogue and digital business exchange line services prices, terms or conditions for such customers;
 - need not publish any amendment to retail analogue and digital business exchange line services prices, terms or conditions for such customers;
 - need not place on its website any information relating to prices, terms or conditions for these customers;
 - need not inform Ofcom should it choose to change such prices, terms or conditions for these customers; and
 - may depart from charges, terms and conditions set out in its published price list for these customers.
- 4.5 There are, however, certain provisos attached to this consent and these are that:
- for SMP services, the price does not fall below a price floor which covers transfer charges for network components plus fully allocated retail costs; and

- BT puts in place and maintains appropriate internal management systems to ensure that prices do not go below the price floor.
- 4.6 Ofcom further notes that BT's prices, of course, should not breach the Competition Act 1998 or any regulatory obligations.
- 4.7 Under BT's Governance Process BT, amongst other things, commits to:
- the provision of quarterly reports to Ofcom in relation to any bespoke contracts offered in that period;
 - the retention of the contract for the life of the contract or 2 years, whichever is shorter;
 - the maintenance of the documentation that was used to demonstrate that the customer was expected to spend £1m on BT's communications services in the first 12 months of the contract; and
 - analyse the actual revenues charged to the customer in the first 12 months of the contract.
- 4.8 Additionally, as explained in the April 2006 statement, Ofcom intends to conduct audits of BT's unpublished bespoke price offerings and will liaise with competitors to identify suitable cases for audit.
- 4.9 Ofcom may also reapply the requirement to publish charges SMP services condition should BT fail to satisfy Ofcom that bespoke prices remain above the costs floors referred to or be unable to demonstrate that its management systems are sufficient to ensure compliance. The provisions may also be reapplied should a new bar to replicability emerge or an old bar to replicability re-emerge.
- 4.10 The Consent is set out at Annex 1.

Mixed service bundles

- 4.11 Ofcom explained in the May 2004 statement that once competitors could replicate exchange line services using wholesale inputs it would no longer presume that service bundles which mix SMP products with non-SMP products would be unduly discriminatory. The presumption that service bundles which mix SMP and non-SMP products would be likely to be unduly discriminatory is not expressly set out in an SMP services condition. Instead, Ofcom stated that it would interpret the no undue discrimination SMP services condition in this way.
- 4.12 Given that Ofcom considers that retail business analogue and digital exchange line services can now be replicated, Ofcom will no longer presume automatically that mixed services bundles are unduly discriminatory. The new interpretation of the no undue discrimination SMP services condition relates to service bundles that mix retail business analogue and digital exchange lines with products from markets in which BT does not hold SMP. Ofcom will continue to presume that mixed service bundles involving inland calls and/or leased lines, which are not replicable, would be likely to be unduly discriminatory.
- 4.13 The new interpretation shall not prejudice Ofcom's ability to decide otherwise in relation to abuses under the Competition Act 1998.

Communications Act tests

- 4.14 Ofcom considers that the Consent set out at Annex 1 meets the tests set out in the Act.
- 4.15 Ofcom has considered its duties under section 3 of the Act and all the Community requirements set out in section 4 of the Act. In particular, the Consent is aimed at promoting competition and securing efficient and sustainable competition for the maximum benefit of retail consumers. In a competitive market place, Communications Providers would be able to and need to compete for individual contracts and would need to set prices at the competitive level. They would not be able to simply undercut BT Retail's prices because they would not know the exact level at which they were set. Consenting to the removal of the obligation to publish prices would allow the market to set prices and avoid price following whilst still implementing a safety floor for BT's prices. In combination, Ofcom considers that this would help to promote competition in downstream narrowband markets.
- 4.16 Section 49 of the Act requires directions to be objectively justifiable, non-discriminatory, proportionate and transparent.
- 4.17 Ofcom considers that the Consent is:
- i) objectively justifiable as the Consent is aimed at promoting competition for retail business analogue and retail business digital exchange line services which are now considered to be replicable by other Communications Providers;
 - ii) proportionate as the Consent would apply to retail business analogue and digital exchange line services only as Ofcom considers that BT has resolved satisfactorily the outstanding issues that were a bar to replicability. The Consent will not apply to other markets in which BT Retail has SMP;
 - iii) not unduly discriminatory to BT because there is no other provider with SMP currently specifically required to provide WLR services; and
 - iv) transparent in that the disapplication of the requirement to publish charges SMP services condition to the extent that it applies to services sold to customers whose spend is projected to be in excess of £1 million on BT's services in the next 12 months (assessed on the anticipated spend in the next 12 months consequent on BT being awarded the contract for which it would be bidding) and this is clearly set out in this document.

Annex 1

Consent under section 49(4) of the Communications Act 2003

Consent under section 49 of the Communications Act 2003 ('the Act') and SMP services condition D3 imposed on British Telecommunications plc ('BT') as a result of the market power determinations made by the Director General of Telecommunications ('the Director') that BT has significant market power in markets for retail business analogue exchange line services, retail business ISDN2 exchange line services and retail business ISDN 30 exchange line services in the UK excluding the Hull Area

WHEREAS:

- (A) as a result of a market analysis carried out by the Director, he proposed on 17 March 2003 and on 26 August 2003, in accordance with sections 48(2) and 80 of the Act that BT has significant market power in the markets for retail business analogue exchange line services, retail business ISDN2 exchange line services and retail business ISDN 30 exchange line services in the UK, excluding the Hull Area, and the setting of certain SMP services conditions including SMP services condition D3;
- (B) the Director considered every representation duly made and on 28 November 2003 pursuant to sections 48(1) and 79 of the Act by way of publication of a Notification identified the relevant services markets, made market power determinations to the effect referred to in recital (A) and set certain SMP services conditions on BT to take effect on 28 November 2003, unless otherwise is stated in Schedule 1 thereto, including SMP services condition D3 which is as follows:

"D3.1 Except in so far as the Director may otherwise consent in writing, the Dominant Provider shall publish charges, terms and conditions and act in the manner set out below.

D3.2 The Dominant Provider shall publish charges, terms and conditions, including bundled charges, terms and conditions (whether or not those bundles include charges, terms and conditions for services supplied in markets to which this Condition does not apply.

D3.3 The Dominant Provider shall publish any amendments to the charges, terms and conditions published under paragraph D3.2, including charges, terms and conditions for any new services, within 24 hours of the time that amendment comes into effect

D3.4 Publication referred to in paragraphs D3.2 and D3.3 shall be effected by placing a copy of the information on any relevant website operated or controlled by the Dominant Provider.

D3.5 The Dominant Provider shall send to the Director a written notice of any amendment to the charges, terms and conditions published under paragraph D3.2 (including charges, terms and conditions for new services) within 24 hours of the time that the amendment comes into effect and shall send a copy of the notice to any person who may reasonably request such a copy.

D3.6 Where it would be impracticable for the Dominant Provider to publish under paragraphs D3.2, D3.3 or D3.5 any charges or amended charge, the Dominant Provider shall instead publish the method to be adopted for determining that charge or amended charge.

D3.7 The Dominant Provider shall provide services at the charges, terms and conditions published under this Condition, and shall not depart there from either directly or indirectly.”

- (C) by virtue of the Transitional Provisions the Director was able to exercise the powers under the Act for an interim period. OFCOM assumed those powers as of 29 December 2003;
- (D) this Consent concerns matters to which SMP services condition D3 relates;
- (E) OFCOM published the draft Consent on 1 March 2007 and sought comments on its proposals by 5 April 2007 and has considered respondents' comments;
- (F) by virtue of section 49(9) of the Act, OFCOM may give effect to the proposal set out in the Notification, with or without modification, only if –
 - (a) they have considered every representation about the proposal that is made to them within the period specified in the notification; and
 - (b) they have had regard to every international obligation of the United Kingdom (if any) which has been notified to them for this purpose by the Secretary of State;
- (G) for the reasons set out in the explanatory statement accompanying this Consent, OFCOM are satisfied that they have acted in accordance with the relevant duties set out in sections 3 and 4 of the Act;
- (H) for the reasons set out in the explanatory statement accompanying this Consent, OFCOM are satisfied that, in accordance with section 49(2) of the Act, the Consent is:
 - (i) objectively justifiable in relation to the networks, services, facilities, apparatus or directories to which it relates;
 - (ii) not such as to discriminate unduly against particular persons or against a particular description of persons;
 - (iii) proportionate to what it is intended to achieve; and
 - (iv) in relation to what it is intended to achieve, transparent.

NOW THEREFORE, PURSUANT TO SECTION 49 OF THE ACT AND CONDITION D3.1 OFCOM GIVES THE FOLLOWING CONSENT:

1. The obligations placed on BT which are set out in SMP services condition D3 shall not apply to retail business analogue exchange line services, retail business ISDN2 exchange line services and retail business ISDN30 exchange line services to the extent that:-
 - (a) any prices do not fall below a price floor which covers transfer charges for network components plus fully allocated retail costs;

- (b) the Consent applies only to Electronic Communications Services sold to customers whose spend with BT in the 12 months following award of the contract is projected to be in excess of £1million on the provision by BT of such services and associated facilities in the UK; and
 - (c) BT puts in place and maintains appropriate internal management systems to ensure that prices do not go below the price floor set out above.
2. For the purpose of interpreting this Consent, the following definitions shall apply:
- (a) **'Act'** means the Communications Act 2003;
 - (b) **'OFCOM'** means the Office of Communications;
 - (c) **'Transitional Provisions'** means sections 408 and 411 of the Act, Article 3(1) of the Communications Act 2003 (Commencement No. 1) Order 2003 and Article 3(2) of the Office of Communications 2002 (Commencement No.3) and Communications Act 2003 (Commencement No. 2) Order 2003;
3. Except insofar as the context otherwise requires, words or expressions shall have the meaning assigned to them in paragraphs 2 above and otherwise any word or expression shall have the same meaning as it has in The Notification or, if the context so permits, in Schedule 1 thereto, as appropriate, and otherwise any word or expression shall have the same meaning as it has in the Act.
4. For the purpose of interpreting this Consent:
- (a) headings and titles shall be disregarded; and
 - (b) the Interpretation Act 1978 shall apply as if this Consent were an Act of Parliament.
5. This Consent shall take effect on the day that it is published.

David Stewart
Director of Investigations

A person authorised under paragraph 18 of the Schedule to the Office of Communications Act 2002

29 May 2007

Annex 2

BT's Governance Process for Bespoke Pricing

Governance Process for Bespoke Pricing for Business Exchange Lines in accordance with the requirements set out in Ofcom's consent to the Regulation of BT's Retail Business Exchange Line Services¹⁷

Introduction

Subject to certain provisos, Ofcom have proposed to consent to not apply SMP services condition D3 to retail business analogue exchange line services, retail business ISDN2 exchange line services and retail business ISDN30 exchange line services¹⁸. One of the provisos is that "BT puts in place and maintains appropriate internal management systems to ensure that prices do not go below the price floor set out above."¹⁹ In their Explanatory Statement (paragraph 1.10) Ofcom further state that BT's management systems should be adequate to ensure compliance with the Competition Act 1998 and any ex-ante safeguard tests.

This document outlines BT's internal governance processes to comply with the Consent. This governance process will ensure that:

- BT will not offer bespoke prices which are below a 'price floor'²⁰. The price floor represents the sum of the charges for the wholesale input into the product plus the retail costs of the product calculated on a fully allocated cost (FAC) basis.
- BT will put in place and maintain appropriate internal management systems to ensure that bespoke prices offered to customers are not less than the 'price floor'.
- Clearly, the bespoke prices offered by BT do not result in BT being in breach of the Competition Act 1998 or any ex-ante regulation.
- The bespoke pricing will only be available to customers whose spend on services supplied by BT is projected to be in excess of £1million in the first 12 month period of the contract.
- BT will retain the necessary contractual and associated financial documentation for a minimum of two years or for the life of the contract, whichever is the shorter.

BT's proposal is that the governance will be built on existing processes, in three parts. The first part is to calculate minimum prices that can be used for this bespoke pricing. The second is to identify the customers to which this process may be applied and negotiate the appropriate prices. The third part is to retain the necessary documentation for audit purposes.

Calculating the minimum price

¹⁷ The governance process is without prejudice to BT's position set out in the response.

¹⁸ This applies to connections and rentals.

¹⁹ Draft Consent, Replicability: the regulation of BT's retail business exchange line services (1 March 2007).

²⁰ Based on the requirements detailed in the Ofcom Draft Consent, March 2007, "Replicability: the regulation of BT's retail business exchange line services"

The minimum price that can be offered to a customer on a bespoke basis is the 'price floor'. BT will use its existing regulatory 'cost stack' model to determine the price floors for exchange lines for business customers. BT's model separately identifies costs for exchange line connection and rental charges. The model includes:

1. The published prices for Wholesale Line Rental (WLR) connections and rentals, as published in the Openreach Price List.
2. The retail costs involved in the supply of a business exchange line. These costs are calculated on a FAC basis using the most recent full-year data from the relevant system used to produce BT's annual audited Accounting Separation statements for the appropriate products.

The regulatory 'cost stack' model will be updated regularly to take into account full-year Regulatory Accounting data, once the above-mentioned audit is completed, and any revised Openreach prices. The changes will be authorised by Regulatory Finance.

The model will then be used by the BT Global Services and BT Retail pricing teams to calculate the minimum prices that BT will be able to offer to prospective customers on a bespoke basis. These minimum prices will be revised in line with the updated information from the cost stack model, to ensure that the bespoke prices offered to customers are not below the 'price floor'.

Process for Standalone Business Exchange Line Bespoke Pricing

This process applies where BT offers a customer bespoke prices for business exchange lines on a stand-alone basis (i.e. not in conjunction with other services or products).

A salesperson will engage with business customers for sales opportunities, as normal. As part of the customer engagement process, the salesperson will establish sales opportunities where the customer may be able to receive business exchange lines that are priced on a bespoke basis. For example, the salesperson will establish whether a customer is intending to spend over £1m on BT products and services related to telecommunications in the UK. The details of the process described are generally applicable and may vary depending on the specific circumstances.

If a sales opportunity arises where the customer may qualify for bespoke business exchange line prices, the salesperson will, in conjunction with a BT finance team, establish the lowest prices that may be offered to the customer. The salesperson will then negotiate prices with the customer. The salesperson will ensure that the final prices offered are at or above the 'price floor'.

The proposed price offer for the customer will then be processed and authorised using the existing sign-off processes within BT Global Services and BT Retail.

The approved offer will then be made to the customer.

If the customer accepts the offer, a contract will be signed by BT and the customer. If the customer does not accept the offer, negotiations will either cease or continue (in which case the negotiation process described above will be repeated).

BT will bill the customer for business exchange lines using the relevant billing system. If the price points for business exchange lines, as set out in the customer contract, do not already exist in the relevant billing system, then the new price points will be added.

The following documentation will be provided to a nominated member of the regulatory team in BT:

1. Copy of the contract – provided by the appropriate contract lawyer or commercial contracts manager.
2. Copy of the financial analysis demonstrating that the business exchange line prices will be at or above the 'price floor' over the period of the contract. This analysis will be completed in a standard format – provided by the appropriate contract accountant.
3. Assumptions used in the financial analysis – provided by the appropriate contract accountant.
4. Copy of documentation that demonstrates that the customer is expected to spend £1m with BT in the first 12 months of the contract (as explained above). This may include an analysis of the previous 12 months spend (e.g. using the relevant customer relationship management (CRM) system) or written confirmation from the salesperson that the customer has confirmed that the proposed expenditure will be in excess of £1m per year with BT.
5. An analysis of the actual business exchange line revenues charged to the customer for the first 12 months – provided by the appropriate contract accountant after a year of the contract term has passed.

The nominated member of the regulatory team will retain this information for the life of the contract or 2 years, whichever is shorter subject to the Data Protection Act and other applicable laws.

Once BT has been given consent, BT will report quarterly to Ofcom in the first year on any contracts signed where BT has sold business exchange lines using bespoke pricing.

The nominated member of the regulatory team will be responsible for liaising with Ofcom for audit purposes.

Single Price Process - For Business Exchange Lines sold together with another, unregulated product

Where a single price is required for a combination of business exchange lines and non-SMP elements or products, the governance process is different from the stand-alone standard process described above.

In this case, additional cost information will be required for the non-SMP elements (whether a bespoke element or another product) for the purpose of calculating a new 'price floor'. The costs of the additional elements will be added to the bespoke business exchange line 'cost stack' model, although the retail costs of the non-SMP elements will be calculated on an incremental cost (IC) basis instead of FAC used in the stand-alone standard process.

An analysis will be prepared to demonstrate that the combined single price for the business exchange lines and the non-SMP elements is above the 'price floor' over the term of the contract.

The financial analysis provided to the nominated member of the regulatory team will specify separately the price and costs associated with the non-SMP elements or products as well as the business exchange lines.

18th May 2007

Annex 3

Respondents to the consultation

- BT
- Federation of Communications Services
- Scottish and Southern Energy
- UKCTA

Ofcom also received four confidential responses