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Dear Graeme

Valuing Copper Access

We welcome the opportunity to provide comments on Ofcom's consultation on the above subject.

SSE is primarily an energy company but has subsidiary businesses which are involved in the telecoms market: two as code operators who provide infrastructure and services to business customers; and one as a telephony service provider. We recognise the importance of the valuation of the copper access network for the prices of the wholesale access products that are available to us to meet the needs of our customers e.g. wholesale line rental (WLR) and partial private circuits. We also recognise, as the owner of regulated energy networks, the value of stability in network valuation methodologies.

In relation to WLR, it is worth noting that the input wholesale line rental cost to WLR operators, of which the cost of copper access forms part, is only one aspect of the competitive environment they face. The other crucial aspect for such operators is the minimum fixed retail price set by BT for line rental, as this defines the margin within which they can operate. Currently, as Ofcom are aware, this margin is negative. While a reduction in the wholesale input charge would clearly be welcome to the extent that it provides a positive margin, the other key factor in assessing the viability of the WLR market, is BT Retail's pricing policy. We look to the outcome of the strategic review of telecoms to deliver transparency and true equivalence of input cost for copper access between BT and its competitors so that pricing behaviour can be judged by all according to the normal rules of competition.

Turning to the issues raised in this consultation, we have a few comments on the proposed approach, but not for every question posed. Therefore, we have grouped our comments under the headings used in the summary of consultation questions.

Policy Aims and the Regulatory Framework

We note that Oftel mandated a change to the valuation methodology used for BT's copper access network in 1996/97. At this time, the historic cost accounting (HCA) valuation methodology was changed to a current cost accounting (CCA) approach. At that time, any windfall benefit or "over-recovery" accruing to BT from the change in methodology was expected to be eroded through competitive processes in due course, although such competition has, in fact, failed to materialise. Given that Ofcom has assessed that BT would continue to over-recover if CCA continued to be used without amendment, we support Ofcom's proposal to make adjustments to the CCA methodology on a forward-looking basis. We would not support any clawback of assessed over-recovery for historic periods. Finally, we support the criteria that Ofcom has set out for evaluating potential valuation approaches – particularly that of minimising regulatory uncertainty going forward.

Valuation Options

This section covers a number of detailed issues associated with the valuation methodology. Of these, we would comment on spare capacity, duct sharing and efficiency adjustments.

On the issue of spare capacity, we agree with Ofcom that it is not appropriate to reduce the access network valuation to take account of assets that are spare, faulty or stranded as a result of competition. If Ofcom are happy with BT's planning approach, which they seem to be, then a degree of spare capacity should be regarded as inevitable. It is not possible to have perfect foresight in planning and we do not consider that BT should be penalised for having a reasonable margin of spare capacity on its access network.

The apportionment of costs of duct shared between the access network and the core network were considered in Ofcom's Part 1 consultation on this topic. We note that Ofcom accepts that the current approach to apportioning the costs of shared ducts based on cross-sectional area of cables leads to the access network taking a larger share of these costs. There does seem to be a competitive issue here if the apportionment of costs is skewed away from the more competitive core network assets and towards the less competitive access assets. In our response to the Part 1 consultation, we supported the equi-proportional mark-up approach and are disappointed to note that Ofcom now considers that there are practical difficulties associated with this approach. Perhaps this is an area that could be revisited in the future.

We note Ofcom's consideration of the efficiency of BT's operating expenditure in running its access network and agree that this is a valid consideration for setting price controls and access charges. While we can see the relevance of operating efficiency in that context, we agree with Ofcom that such efficiency factors should not be used in the valuation of the actual network assets.

Calculating over-recovery adjustments

As noted above, we support Ofcom's forward-looking approach to this issue. We also welcome the further clarity on the "RAV" approach provided in the recent supplement to this consultation paper. Thus we support the proposal to disallow the over-recovery between 2005/06 and 2009/10.

Proposals

We support Ofcom's proposed approach of continuing the existing valuation methodology with adjustments to cater for longer asset lives and the prospective over-recovery on pre-1996/7 assets for the period noted above.

I hope these comments are helpful.

Yours sincerely

Rob McDonald
Director of Regulation