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IN THE COMPETITION
APPEAL TRIBUNAL

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

Victoria House,
Bloomsbury Place,
London WC1A 2EB

14th November 2013

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

BETWEEN:

BRITISH TELECOMMUNICATIONS PLC Appellant

- and -

OFFICE OF COMMUNICATIONS Respondent

AND BETWEEN:

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

- and -

OFFICE OF COMMUNICATIONS Respondent

AND BETWEEN:

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

- and -

OFFICE OF COMMUNICATIONS Respondent

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

A P P E A R A N C E S

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

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

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

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

1 THE PRESIDENT: Good morning. The Tribunal has received a letter arrived by fax at ten to
2 one this morning from Herbert Smith Freehills concerning the evidence of Mr. Robinson. It
3 has just been given to the members of the Tribunal about ten minutes ago. We have not yet
4 had a chance to digest it and its implications and to hear any submissions upon it as to what
5 steps we should take. But we note that the end of the letter says that further information has
6 been proposed to be provided to the Tribunal. It says "as soon as possible", the words of the
7 letter. So we shall read it and at an appropriate time hear any submissions as to what
8 significance it may have.

9 MR. PICKFORD: I do not believe it is relevant to this morning. We simply tried to get it to the
10 Tribunal as soon as we could, and the further supplementary information coming, I
11 understand, should be in the course of the day. Simply to say that it came out, hot off the
12 press as it were, as soon as it was ready.

13 THE PRESIDENT: Yes, Ms Gallafent.

14 MS GALLAFENT: Good morning. As I anticipated might be the case, unfortunately Mr. Saini is
15 in the Court of Appeal both today and tomorrow. I am afraid it is myself for Ofcom today,
16 together with Mr. Mussa and Ms Neill. No discourtesy is intended by Mr. Saini's absence.
17 It falls to me, then, to call Ofcom's only witness, Mr. Myers, if I may.

18 MR. GEOFFREY RICHARD PLATT MYERS, Sworn

19 Examined by Ms GALLAFENT

20 Q Mr. Myers, could I ask you please to take up core bundle D tab 13. You have there a
21 witness statement with your name on it?

22 A Yes, I do.

23 Q Turn to p.119 in that tab. We can see a statement of truth and again your name at the end of
24 that?

25 A Yes.

26 Q Sir, for the record, a signed copy should be in the Tribunal's bundles at DF1 tab 3. I was not
27 intending to go to it unless necessary.

28 THE PRESIDENT: No.

29 MS GALLAFENT: Mr. Myers, do you adopt this statement as your evidence in these
30 proceedings?

31 A Yes, I do.

32 Q I am grateful. Sir, with the permission of the Tribunal, I would just like to ask Mr. Myers
33 two questions in relation to two additional documents that have been provided. They were
34 sent to the parties yesterday afternoon. Both are responsive, one in relation to the document

1 provided very helpfully by Mr. Pickford at the end of last week. They have already been
2 inserted into the additional documents bundle 2 at tabs 36 and 37. Could I ask that Mr.
3 Myers be given additional documents bundle 2.

4 MR. PICKFORD: Sir, we do have a concern in relation to one aspect of this letter. I am happy to
5 deal with it now. It may be sensible for me to deal with it before.

6 THE PRESIDENT: Yes. Can I just see, what are the additional documents? Tab 36, is it? Ms
7 Gallafent, which tabs?

8 MS GALLAFENT: Tab 36, sir, and 37. 36, I hope, is a document entitled "Calculation of return
9 on capital employed".

10 THE PRESIDENT: Yes. Can you tell me what it is before you ask any questions?

11 MS GALLAFENT: Yes, it is a note in response to that provided by Mr. Pickford, which I
12 understand is at tab 35. If you just turn back one tab one sees the document entitled
13 "Calculation of return on capital employed (ROCE) if price is set to DSAC".

14 THE PRESIDENT: We do not have anything at tab 35.

15 MS GALLAFENT: I am so sorry, I spoke to Mr. Hiendl who indicated it was perhaps at least in
16 his bundle. It is one of the documents that were helpfully handed up before we rose at the
17 end of last week.

18 THE PRESIDENT: Yes. (Handed)

19 MS GALLAFENT: Mr. Pickford's was the single page, just one side of A4.

20 THE PRESIDENT: We have got it.

21 MS GALLAFENT: We do have some spare copies amongst ourselves. If necessary, perhaps I
22 can hand those up. (Handed)

23 THE PRESIDENT: Yes. So that is tab 35. This is not original evidence; it is just a note that has
24 been prepared for the purposes of this hearing?

25 MS GALLAFENT: Exactly, and Mr. Pickford had very helpfully handed that up with an
26 indication that it would save time in terms of his cross-examination of Mr. Myers. Equally
27 in that spirit, Mr. Myers has prepared the note that you see at tab 36 which sets out the
28 return on capital employed on the full range of Ethernet products on four different bases
29 relating to four different assumed sets of prices.

30 MR. PICKFORD: No objection is taken by us in relation to that.

31 THE PRESIDENT: Yes. The next one at tab 37?

32 MS GALLAFENT: The next one at tab 37 sets out the fixed common costs relevant to WES and
33 BES services. Again, that is not an original document; that has been prepared for the
34 purposes of these proceedings. That, as we explained in the covering letter which we sent to

1 the parties last night - I am happy to hand up copies of that letter if the Tribunal would find
2 it useful --

3 THE PRESIDENT: I think that might assist, if you have got copies of that.

4 MS GALLAFENT: I do indeed. (Handed) Of course, Mr. Myers can confirm the position in
5 relation to it. If one turns to the second page of Ofcom's letter from yesterday, the second
6 paragraph on that second page, the second document is entitled "Fixed common costs
7 relevant to WES/BES services". It is prepared by Ofcom economists at Mr. Myers'
8 instruction in response to the reference made last Thursday to Mr. Houpis' assertion there
9 was a total difference from DSAC and FAC of over £350 million between 2007 and 2011
10 and the questions put to Mr. Houpis about this assertion (we have given the reference to the
11 transcript there), and indicated that Mr. Myers would explain the purpose of the notes in his
12 evidence in chief, and counsel (I) would ask the Tribunal's leave at the commencement of
13 the hearing today. So I do that. I understand that Mr. Pickford has a comment to make.
14 Before he does, could I just make it clear, we have asked BT to clarify whether they
15 consider there was anything confidential in either of those notes. They have confirmed that
16 there is not. So whilst they are both marked as being confidential, there is not any material
17 which cannot be referred to therein.

18 THE PRESIDENT: Yes.

19 MR. PICKFORD: Sir, if I could just briefly explain our position, the problem that we see and
20 then our proposed solution in relation to it?

21 THE PRESIDENT: Yes.

22 MR. PICKFORD: The difficulty in relation to this second document, and it is only the second
23 document we have any concerns about, is that we had no understanding of what Mr. Myers
24 proposed to say in relation to these issues and, indeed, some of the figures are not entirely
25 clear to us at the moment. The suggestion that is made by Ofcom, the reason why this is
26 being advanced to us on the eve of Mr. Myers' cross-examination is that it relates to
27 something that Dr. Houpis said in his evidence about the difference between DSAC and
28 FAC being £350 million. That was evidence that Dr. Houpis gave back in July in his fourth
29 witness statement at para. 3.49 and, indeed, various other paragraphs, so we say it is not
30 really sufficient or appropriate to be putting in new material responsive to that particular
31 figure some four months later just before Mr. Myers is about to be cross-examined.
32 The difficulties we have, before I outline what we propose to do about it, are that obviously
33 Dr. Houpis has had no opportunity to provide his view about what these figures mean or
34 what one can derive from them, and I have had no proper opportunity to prepare any cross-

1 examination in relation to it and so taking that reason it is an unsatisfactory situation and
2 could have been dealt with four months ago.

3 However, because we wish to be as accommodating and as pragmatic as we possibly can be,
4 we are not objecting to the course that is proposed that Mr. Myers should provide some
5 explanation of these figures in his examination-in-chief, however, we may - depending on
6 what Mr. Myers says and what implications he intends to draw from this evidence - need to
7 have some response from Dr. Houpis, because obviously if it had been done four months
8 ago, we could have had that and it could have been explored with Dr. Houpis in his cross-
9 examination but we no longer have that liberty because his evidence has been given.

10 THE PRESIDENT: I think, first of all, you are not cross-examining Mr. Myers until the end of
11 the day.

12 MR. PICKFORD: That is right, Sir, I have some time to try to work out what it all means.

13 THE PRESIDENT: I think if it is put to him and he can explain it and why it is so significant,
14 then we can also consider whether we think it is really of much relevance.

15 MR. PICKFORD: Indeed, and as I said, we are not objecting to it, we are just noting that it
16 potentially causes an issue we may have to address.

17 THE PRESIDENT: Yes, that is helpful. Ms. Gallafent, you can put the documents, and we will
18 see what happens regarding your second one.

19 MS. GALLAFENT: I am grateful. Mr. Myers, in that case can I ask you, please to turn to tab 36,
20 and the document entitled "Calculation of Return on Capital Employed? Mr. Myers, please
21 could you assist the Tribunal by explaining the purpose and provenance of this document?

22 A This document was prepared by Ofcom economists at my suggestion and the purpose was to
23 provide some further factual information to set in context the information that was in the
24 note handed up to the Tribunal by Mr. Pickford last Friday.

25 So if we turn to table 1 the return on capital employed, the brackets shown there for the four
26 years and the overall average that is labelled "1", that is exactly the same as the numbers
27 that Mr. Pickford provided in his notes. Those are computed on the following basis: the
28 costs that are taken into account are the fully allocated costs in BT's unadjusted regulatory
29 financial statements. The revenue is the revenue if BT had set all of its prices for Ethernet
30 services at the DSAC. That is a hypothetical because BT did not set all of its prices at
31 DSAC, as we know it set some above but it also set some below.

32 THE PRESIDENT: Do you say all of its regulated prices, or Ethernet at DSAC?

33 A As I understand it, it is all of the services in this market, which are covered by the cost
34 orientation obligation, that is my understanding.

1 Q Not just the disputed services?

2 A Indeed, yes.

3 Q So the column that is labelled "2", the actual ROCEs, so that is BT's actual revenue for all of
4 these services, and the return on that revenue relative to the fully allocated costs. So, as we
5 can see, sometimes they are higher and sometimes they are lower, overall somewhat lower,
6 and the reason why they are overall somewhat lower is because BT did not set all of its
7 prices at DSAC, it set a number of them materially below DSAC. But, the actual ROCEs do
8 include or are inflated by the effects of BT's overcharging on the services that Ofcom found
9 in the Determination had been overcharged, and so the purpose of columns 3 and 4 is to take
10 out the effects of that overcharging. So in column 3 these take out the effects of the
11 overcharging on the external revenue, i.e. the services sold to CPs and, as you can see, that
12 gives a lower set of ROCEs, but that still includes, because we are looking at the entirety of
13 BT's revenue here, it still includes BT's internal revenue, i.e. BT's sales to itself, and it still
14 includes the effects of BT's revenue in excess of DSAC on that internal revenue. As well
15 as the external overcharge that excess of internal revenue over DSAC is also taken out in
16 column 4. So column 4 takes out, if you like, all the effects of pricing in excess of DSAC.

17 Q This is on the RFS without the ----

18 A Exactly.

19 Q -- when you say "unadjusted"?

20 A As published by BT, which is the same basis as the numbers in the note that Mr. Pickford
21 handed up, and that perhaps leads into the reason why table 2 is also included in this note,
22 because table 2 is the same four sets of calculations but on the adjusted RFS data, i.e. the
23 RFS data after the adjustments applied by Ofcom. There are a few other minor points of
24 detail in difference, but they are kind of set out in the note on the footnotes.

25 MR. HARRISON: Just so I understand the ROCE at the end, there is no adjustment for, if you
26 like, the denominator that has been used as a result of the removal of the internal revenue?
27 Is that how it was done?

28 A Sorry, it is not removing the internal revenue, it is only removing the excess of internal
29 revenue over DSAC. So it is doing an analogous thing for the internal revenue as is done to
30 remove the overcharge for external revenue.

31 MS. GALLAFENT: I am grateful. If I could ask you then, Mr. Myers, to turn to tab 37 and you
32 have there a document entitled "Fixed Common Costs Relevant to WES/BES Services."
33 Could I ask you, please, also to explain to the Tribunal the provenance and purpose of this
34 note?

1 A So, similarly, this note and the numbers in it were calculated by Ofcom economists at my
2 suggestion and the purpose is to set in context the £350 million number that Dr. Houpis has
3 referred to. What I mean by setting it in context is that recognising that the concern that is
4 being expressed is that there is a risk of, or there is an over recovery of BT's fixed and
5 common costs. What this note is just showing is the size of those fixed and common costs,
6 and therefore one can look at the £350 million relative to this number. So it is simply
7 putting it in context essentially. It is not trying to draw a definitive conclusion about over
8 recovery of costs or not, it is just putting it in context.

9 THE PRESIDENT: This is not in any way querying here the £350 million?

10 A No, that's correct. And the way to compare them would be the £350 million, as I understand
11 it, is calculated over a five year period, so that is on average £70 million a year. The figure
12 in this note, which I understand I can say, which is £2.2 billion (£2,200 million) that is an
13 annual figure. So it is the £70 million that you would compare to this £2.2 billion and, as
14 you can see, these fixed and common costs are very large, so the £70 million is of the order
15 of 3 per cent, I think, of the £2.2 billion.

16 MS. GALLAFENT: I do not have any further questions, Sir. Mr. Myers, if you would wait there,
17 please?

18 THE PRESIDENT: Yes, Mr. Thompson?

19 Cross-examined by Mr. THOMPSON

20 Q Just before I start, consistent with the approach we have taken elsewhere, I am proposing to
21 deal with, as it were, the slightly more conceptual issues I suppose one might call them, and
22 Mr. Read is going to deal with the particular issues arising at the start of the period and the
23 specific issues of adjustment and things of that kind. We have obviously made a slightly
24 late start. I had hoped to have finished in the morning, but I may not manage that and I
25 think Mr. Read was anticipating that he would be about two hours, so we will endeavour to
26 finish within time but obviously the time we have spent so far has been largely on Mr.
27 Pickford's agenda, so we will do our best.

28 Mr. Myers, first, I would like to ask you about your role here. It is not in any way a
29 criticism, because it accords precisely with the direction of the Tribunal, but it is fair to say
30 that you are here to defend Ofcom's Decision effectively as the champion of Ofcom against
31 all comers rather than as an independent expert. Is that fair?

32 A No, that is not correct. I understand I have two roles here. One is to explain the basis for
33 Ofcom's reasoning or conclusions. My other role is to give my view as a professional
34 economist and I have signed a declaration that it is my full and complete professional

1 opinion, and I am very conscious of my duty to the Tribunal to look at these issues on an
2 independent professional basis.

3 Q At para.3 you say that you had responsibility for the economic analysis during the
4 investigation of this case. There are a number of regulatory decisions relevant to this case,
5 the original 2004 Review; the Energis Determination; the THUS complaint; the 2008
6 Market Review; the 2009 Charge Control, and the PPC's Decision. Were you involved in
7 any or all of those decisions or determinations?

8 A I was involved in some of those. I was involved in the 2004 Leased Line Market Review; I
9 was involved in the PPC Determination. I was not involved in the 2008 Business
10 Connectivity Market Review or the 2009 Leased Line Charge Control. I am sorry, what
11 were the others?

12 Q The others were the Energis case and the THUS complaint.

13 A I am just trying to remember. The THUS complaint I think I had a peripheral involvement
14 in, not a central one. The Energis case was ----

15 Q That was in parallel to the 2004 Market Review. You may remember that there was a
16 dispute as to whether or not the LES services should be provided on a wholesale basis, and
17 Ofcom considered that matter in parallel with the 2004 Market Review, and I am just asking
18 whether you were involved in that.

19 A I do not have any recollection of that case. I am not sure.

20 Q There is a second issue by way of introduction. Would you accept that there are three high
21 level issues in this case, and I will give them to you and see if you agree? First of all, which
22 charges are required to be cost orientated, so the issue of scope, as it were. That is one
23 issue. Do you accept that?

24 A Yes.

25 Q The second one is how is compliance with cost orientation and Condition HH3.1 to be
26 assessed. What I might call "the compliance issue", and that is a second issue?

27 A Yes.

28 Q The third is how Ofcom should exercise its discretion to order repayments or not, including
29 the issue of interest. That is a third and separate issue. Do you accept that?

30 A Yes.

31 Q The third issue relates to the discretion of Ofcom in December 2012. That is when the
32 decision was taken, was it not?

33 A Yes.

34 Q Whereas the compliance issues relate to when BT set its prices between 2006 and I think

1 2011. That is right, is it not?

2 A That is when BT set its prices, yes.

3 Q So the issue of compliance relates to those dates?

4 A Relates to charges set during that period, yes.

5 Q Can we now look slightly more at the scope issue? I think you were present when Dr.

6 Houppis was cross-examined. Is that correct?

7 A Yes.

8 Q So I discussed some of these issues with him so I propose to take them more shortly with

9 you. I assume you accept that market definition of SMP findings are modelled on EU

10 competition law principles. You would accept that, I think?

11 A Yes.

12 Q One finds that in the Access Directive and Commission guidelines, which I am sure you are

13 familiar with.

14 A Yes.

15 Q The second point is that the power to impose cost orientation is based on a concern over

16 excessive pricing or margin squeeze on a relevant market. Would you accept that?

17 A Yes.

18 Q That reflects Article 13.1 of the Access Directive. I think you would probably accept that

19 this case does not concern margin squeeze. The remedy in HH3.1 would be completely

20 unsuitable to deal with a margin squeeze, would it not?

21 A Yes, it is not targeted at a margin squeeze.

22 Q Concerns about price distortions within a market as against excessive pricing on a market

23 are not within the scope of Article 13.1. Would you accept that?

24 A I do not feel able to comment on that.

25 THE PRESIDENT: That is a bit of a legal question, is it not?

26 A I can comment on that from an economic point of view and I would say that that depends on

27 the issue that arises. I think one certainly can have concerns economically about prices

28 within a market, not just prices across the entirety of the market.

29 MR. THOMPSON: Indeed. I will leave the legal question there. Can we now turn to the finding

30 in *PPC*, which is at Core Bundle E, Tab 9. If you turn to para.215, p.63, I know you are

31 familiar with this case and you will recall that there were two sets of conditions, Condition

32 G and Condition H. One applied to the market for the provision of wholesale trunk

33 segments at all bandwidths within the United Kingdom and the other applied to the market

34 for provision of traditional interface symmetric broadband origination with a bandwidth

1 capacity up to and including eight megabits per second within the United Kingdom. Those
2 were the two markets, were they not?

3 A (After a pause): I am sorry, I just ----

4 Q I am just reading ----

5 A Yes, yes. Those correspond to the market definitions.

6 Q Then at 217 the Tribunal says:

7 "It seems, therefore, very clear that the various conditions imposed by the 2004
8 LLMR Statement apply to clearly defined markets: Conditions H apply to trunk
9 segments and Conditions G apply to terminating segments".

10 That was a finding of the Tribunal in *PPC*. If you apply that finding to the present case,
11 then would you accept that it would be very clear that the cost orientation obligation in
12 Condition HH3.1 applied to wholesale AISBO services at all bandwidths in the 2004
13 LLMR? Would you accept that that would be the implication of that finding?

14 A Well, I am slightly loathe to make inferences where there are legal matters concerned, but I
15 accept that the definition of the AISBO market was "at all bandwidths".

16 Q Yes, and in 2008 it was wholesale AISBO services up to 1000 megabits, so it was a
17 narrower market?

18 A Yes, that is right.

19 THE PRESIDENT: I am sorry, in 2008 it was?

20 MR. THOMPSON: It was the low bandwidth AISBO market, which is up to 1000 megabits. It
21 was a narrower market definition.

22 A The market definition was split in 2008 between low bandwidth and ----

23 THE PRESIDENT: There were two markets in 2008, were there not?

24 MR. THOMPSON: There were but no conditions were imposed on the high bandwidth.
25 Condition HH3.1 was limited to the low bandwidth market. It was a narrower definition.

26 THE PRESIDENT: Yes.

27 MR. THOMPSON: Can we turn briefly to the meaning of Condition HH3.1? Would you accept,
28 first of all, that a condition such as HH3.1 must be clear if it is to be important? Would you
29 accept that as a matter of principle? You have made various remarks about legal certainty.

30 THE PRESIDENT: Mr. Thompson, that may well be a good argument but it is a legal
31 submission, is it not, that it must be clear? It is not a matter of economics.

32 MR. THOMPSON: There are quite a number of expressions of opinion of that kind in Mr. Myers'
33 report.

34 THE PRESIDENT: Saying what?

1 MR. THOMPSON: The importance of regulatory certainty as a general point and I am simply
2 saying that that applied also in this case.

3 THE PRESIDENT: What you are saying is that when Mr. Myers refers to "regulatory certainty"
4 does that have the implication that the condition should be clear?

5 MR. THOMPSON: Yes.

6 THE PRESIDENT: That is a fair question. Would that be one aspect of regulatory certainty?

7 A That would be one aspect of regulatory certainty. I think there is always a question of how
8 much detail or granularity is set out but, in general, yes, that would be one aspect of
9 regulatory certainty.

10 MR. THOMPSON: Can we turn to paras.284 and 297 of your report?

11 THE PRESIDENT: Can we put away Bundle E or shall we keep it out?

12 MR. THOMPSON: I think we will need Bundle E. Bundle E will be necessary in my cross-
13 examination.

14 THE PRESIDENT: We will keep it out.

15 MR. THOMPSON: In the last sentence ----

16 THE PRESIDENT: Which paragraph?

17 MR. THOMPSON: Of para.284.

18 THE PRESIDENT: Just a moment. (After a pause): 284, yes.

19 MR. THOMPSON: You say:

20 "Ofcom did not consider that BT had made any argument which supported a
21 conclusion to depart from the requirement clearly set out in Condition HH3.1 that
22 "*each and every charge offered*" should be cost orientated".

23 Then at 297 you say essentially the same thing in the last sentence, but you do not specify
24 what the charge should be for. Would you accept that it is important that one knows what
25 the charge should be for in determining what it means? It is not good enough just to say
26 "each and every charge", it has to be for something. It is not a haircut or for cheese, it is for
27 something and so you have to specify what it is for. Would you accept that?

28 A I am sorry, I am not quite clear what you are asking me. The wording of the Condition
29 refers to each and every charge offered for network access, I believe.

30 THE PRESIDENT: Perhaps if we look at the Condition, which is in various places but in Bundle
31 E, if you have still got that, Tab 12, towards the end on the manuscript p.44 at the bottom.

32 A Is it Tab 12 in the same ----

33 Q No, in Bundle E, where the *PPC* judgment was. At Tab 12 is an extract from the 2004
34 LLMR and towards the end, if you look at the manuscript pages at the bottom, at p.44 ----

1 MR. THOMPSON: Page 494 of the Review.

2 THE PRESIDENT: Do you have that? It is Condition HH3.

3 A Yes, I have that.

4 MR. THOMPSON: It says "for Network Access covered by Condition HH1". Do you see that?

5 A Yes.

6 Q So you turn back to Condition HH1, which I think that is not actually in the decision but it
7 was obviously a relevant provision. It says:
8 "Where a third party reasonably requests in writing network access the dominant
9 provider shall provide that network access".
10 Then it says:
11 "The dominant provider shall also provide such network access as Ofcom may from
12 time to time direct".
13 I do not think that is relevant. I think we are with the first sentence. Would you accept
14 that? So it has got to be a reasonable request in writing for network access?

15 A I would say that these are issues that are outside my expertise and they seem to be questions
16 of legal interpretation of the Condition.

17 Q I am not sure that that is correct because you have made these points repeatedly in your
18 report.

19 A But the paragraphs you referred to, I was not giving my own personal professional opinion.
20 I was in that first role I explained at the start. I was reporting what Ofcom said and I think it
21 says very clearly that that was Ofcom's view and it gives the references in the Determination
22 where Ofcom set that out.

23 Q Can we look at BT17, Tab 3, which may give us some guidance as to what all this means? I
24 am sorry, I have given you the wrong reference. I am terribly sorry. My BT16 and 17 are
25 all in one file. Is that right? Do you have that in the same ----

26 A No.

27 THE PRESIDENT: No, BT17 Tab 3 is the contract ----

28 MR. THOMPSON: Yes, that is correct. I am sorry, I have for some reason ----

29 A It says "Contract Form - BT Backhaul Extension Service".

30 Q You will see in the right hand column under the heading "Signature", where it says
31 "Signature":
32 "I/we apply for the BT Backhaul Extension Service subject to the current Contract
33 Conditions for Backhaul Extension Services [reference to a website] which I/we
34 accept."

1 Would you accept that that was a reasonable written request for a service, Mr. Myers?

2 A Again, that's not an issue on which I would have a view.

3 Q I think there is a limit to how self-denying you can be. You have to understand these

4 documents in order to express any kind of view on this matter?

5 A I would be requesting advice from one of my Ofcom lawyers if I was in doubt about the

6 legal interpretation or the legal implication of a document such as this.

7 A Yes. I am simply asking you whether that it is a written request for a BES service. Would

8 you accept that?

9 A That's what I understand it to be, but I'm not in a position to say.

10 THE PRESIDENT: We can all see it is a request for BES services.

11 MR. THOMPSON: If we turn to the next tab, you will find the contract, and you see that is a

12 contract for BES services - do you see that?

13 A Yes, I see that.

14 Q If you turn through to clause 2, you will see clause 2.1:

15 "This Contract begins on the date that the Contract Form is accepted and signed by

16 duly authorised representatives of BT and the Communications Provider and shall

17 continue thereafter until terminated in accordance with this Contract."

18 Do you see that?

19 A Yes.

20 Q I think that is what the lawyer would call an "evergreen contract" - would you accept that

21 characteristic, it does not stop unless somebody terminates it?

22 A That's what I understand from those words, yes.

23 Q Then 2.7 relates to the minimum period:

24 "If the Communications Provider terminates this Contract during a Minimum

25 Period, other than because BT has breached this Contract or increased its charges

26 or has materially changed the conditions of this Contract to the Communications

27 Provider's detriment or because the Contract is terminated under Force Majeure,

28 the Communications Provider must pay BT the rental and other charges for the

29 remainder of any Minimum Period at the rate in force at termination or as

30 otherwise provided in the Openreach Price List."

31 Do you see that?

32 A Yes.

33 Q That does not mean you cannot terminate within the minimum period, it just sets out some

34 financial consequences, if you do, you have to pay effectively the full year anyway - do you

1 see that?

2 A Yes.

3 Q You understand that BT's case is that what condition HH3.1 is concerned with is the charges
4 for the BES or WES service - you understand that is what BT's case is. It is not for the
5 components, it is for the overall service, so the BES 100 or the BES 1000. You understand
6 that is what BT's case is?

7 A Sorry, you used the word "components", what do you mean by "components"?

8 Q For example, Mainlink, a connection service, an access construction service, if that is such a
9 service, but BT says that those are not what HH3.1 is concerned with. HH3.1 is concerned
10 with the overall charge - do you understand that?

11 A Yes, I understand that's BT's argument, but I think the use of the word "components" is
12 confusing because BT defines "components" and it combines those components to build up
13 the costs of services, and services will include connection which would itself have
14 underlying network components beneath it. I understand in broad terms BT's case on this
15 point.

16 Q Ofcom, in its opening, put the matter rather differently, and I think you have the transcripts
17 of the opening. It is day 2, p.2, and Mr. Saini says this:
18 "So we say whether one considers a BES or WES circuit as a whole, whether one
19 considers connection, whether one considers rental, or whether one considers
20 mainlink, all of those items, together or separately, fall within the definition of
21 network access. Another way of putting it is that items which amount to network
22 access will be necessary for access to a network but may not be sufficient."
23 Is that how you understand it?

24 A I think so, yes.

25 Q I would just like to ask you what you say is necessary for an AISBO service, whether we
26 can focus on what it is that Ofcom was thinking about. We did not find that particularly
27 clear. On the face of it, a BT circuit is not necessary for an AISBO circuit. All these CPs
28 could perfectly well start self-supplying. That is something you do deal with in your
29 discussion on connections and rentals. Is a BT service necessary at all for a wholesale
30 AISBO service?

31 A For a wholesale AISBO in general?

32 Q Yes.

33 A Again, I think I can think I can comment on the economic market definition. The market
34 definition for the AISBO market would include both circuits supplied by BT, and circuits

1 supplied by other CPs, either to themselves or to other CPs.

2 Q Likewise, even if one looked just at BT Ethernet services, not all of the services that have
3 been identified would be necessary for a BT circuit - for example, Mainlink might or might
4 not be necessary, excess construction might or might not be necessary. There are a range of
5 things that might or might not be necessary for an AISBO service - is that not correct?

6 A Yes, that's right, some of these different services or elements can be purchased in variable
7 proportions, and in some cases they wouldn't be part of a circuit that a CP purchased.

8 Q Then if we come to the core service itself - I think you were here for Mr. Harman's cross-
9 examination, and there are, I think, three elements that he identified as the core capital costs,
10 the electronics, the duct and the fibre - would you accept that?

11 A Yes, those would account for a substantial proportion of the costs.

12 Q In principle, those capital costs could be borne upfront, somebody could just buy them
13 outright, whether from BT or somebody else - you would accept that?

14 A Well, I think there's a distinction between those different costs elements. As I understand it,
15 the electronics is typically provisioned circuit by circuit, so that cost is incurred at the point
16 at which a connection is made or related to the connection of that particular circuit. As
17 regards duct and fibre costs, these are generally shared across a very wide range of services,
18 and whilst there may be occasions when new duct or new fibre is installed for provision of a
19 particular circuit, as I understand it, the norm would be that these ducts and fibre costs are
20 incurred perhaps many years in the past, or a number of years in the past, and shared across
21 a large number of services.

22 Q In principle, given there is evidence that build or buy is one of the options, presumably if
23 you build then you largely incur the capital costs upfront?

24 A Yes, indeed. If you're building and - well, it depends on what you're building. If a
25 communications provider is building new duct then that would clearly be incurred at that
26 point. Again that may well be shared, or intended to be shared, across a wide range of
27 services. In other cases, they may not need to build new duct. It depends on the
28 circumstances.

29 Q Then looking at the other end of the telescope you do not have to incur any of the capital
30 costs upfront, you can, in fact, rent them and pay the depreciation charge or the rental
31 charge over the period of the circuit. That would be an alternative pricing model, you
32 simply for the service over its length, over its lifetime?

33 A Just to clarify, are you suggesting a pricing model where there is no connection charge and
34 just an ongoing rental charge?

1 Q Effectively, either no or very little?

2 A Yes, because of course if there was connection charge that would obviously be incurred
3 upfront by the CP.

4 Q Yes, but the capital costs of the electronics, the duct and the fibre could be incurred over the
5 lifetime of the circuit? That would be a perfectly viable pricing model. You might or might
6 not like it from a regulatory point of view, but it would be perfectly possible?

7 THE PRESIDENT: When you say "the costs incurred" as opposed to the costs being billed, the
8 customer being charged for them, that is slightly different. When the expenditure is
9 incurred and how it is priced ----

10 MR. THOMPSON: Yes, it could be rented off BT in principle at least with a minimal upfront
11 charge and charged over the lifetime of the circuit?

12 A Yes, indeed, just to clarify, in the light of the President's comment, yes, I think you did refer
13 to incurred, but obviously the costs, the electronics costs, for example, would be incurred
14 upfront. It would be possible to recover that cost over the period for a rental charge, in
15 which case it would be recovered over a number of years on circuit.

16 Q That was really our difficulty, because it appears that none of the charges or services on
17 which Ofcom relies are, in fact, necessary because either they could be provided by
18 somebody else or they could be provided upfront or they could be provided over the
19 lifetime. It did not seem to us to be a clear criterion for the scope of the condition. Would
20 you accept that?

21 A I'm not sure I really fully understand exactly the point that Mr. Saini was putting or whether
22 there was a context around it. If you put to me specific propositions about upfront versus -
23 costs being recovered upfront or over time, I think we have gone through those, and
24 elements that may be purchased or not purchased. The further point you're inviting me to
25 comment on, I don't feel I have a view on that.

26 THE PRESIDENT: I think that is really a submission, is it not?

27 MR. THOMPSON: Yes, I asked the questions and ----

28 THE PRESIDENT: It is not really for this witness.

29 MR. THOMPSON: The other way it was put was really by the CPs, and that emerged also on day
30 2 at p.74, and this is the cross-examination by Ms Rose of Mr. Jones, who is a factual
31 witness for BT. I do not know whether you were present for the factual witnesses?

32 A I was present for some of them. I believe I was present for this witness.

33 Q And what Ms Rose is putting to Mr. Jones is that, taking a WES 100 as an example, there
34 are a number of different discrete services that are being provided and some customers need

1 | them and some do not and that rather goes to the "necessary" point. You will see Ms Rose,
2 | first of all, says, "The customer does not obtain the service of Mainlink, do they?"
3 | Mr. Jones agrees? The second customer has got Mainlink, the third excess construction, the
4 | fourth one out of hours installation, and the fifth one some form of migration charge - do
5 | you say see that?

6 | A Yes.

7 | Q As we understand this line of examination, the suggestion seems to be that HH3.1 applies to
8 | all these discrete services, viewed separately. Is that Ofcom's understanding or not?

9 | A That is a legal interpretation, but it's my understanding that that is Ofcom's interpretation.
10 | But that's not a matter I would have been directly involved in as an economist.

11 | Q We have looked at what BT appears to have put forward its contract for, which was a
12 | contract for a BES 100 service. We are not aware of any requests in writing for all these
13 | other bits and pieces. Is that something that, so far as you are aware, Ofcom has
14 | considered?

15 | A Sorry, has Ofcom considered?

16 | Q Applying condition HH3.1, looking for reasonable requests in writing for these services,
17 | and we see only a request in writing for a BES 100 service. Is that something, as far as you
18 | are aware, that Ofcom has ever considered?

19 | A Sorry, I am not sure, I don't know. Economically speaking I would say the form of a
20 | contract itself does not necessarily specify precisely economically what the services are.
21 | The services may be more granular than the way they're expressed in a particular contract.

22 | Q Can we look at something quite specific which you do talk about, which is the minimum
23 | term. Would you understand there to be any need to request rental services outside the
24 | minimum term in writing, or would the matter simply roll on from month to month? We
25 | looked at the contract; it is an Evergreen contract.

26 | A That's about the interpretation of the legal contract, so again I wouldn't claim any expertise
27 | on that, but that is my understanding based on the clause you showed me.

28 | Q Can we look again – do you still have the conditions out, Mr. Myers?

29 | A Yes.

30 | Q It is tab 12 of core bundle E, condition HH4. Are you familiar with the concept of a
31 | reference offer?

32 | A Yes.

33 | Q Do you see under 4.2 there is an obligation to include at least the following:

34 | "(a) a description of the Network Access to be provided, including technical

1 characteristics (which shall include information on network configuration where
2 necessary to make effective use of Network Access);
3 (b) the locations of the points of Network Access;
4 (c) the technical standards for Network Access (including any usage restrictions
5 and other security issues);"

6 Are you aware of Ofcom ever requiring BT to provide a reference offer, for example for
7 excess construction charge services or transfer services?

8 A I don't have any knowledge on that question.

9 Q But they do have reference offers for the BES service, do they not?

10 A As I understand, yes.

11 Q In fact, there is an obligation at 4.4 to "publish a Reference Offer in relation to any Network
12 Access that it is providing as at the date that this Condition enters into force". Again, that
13 was simply in relation to BES and WES services, and not to all these other bits and pieces,
14 was it not?

15 A I don't know.

16 THE PRESIDENT: Are you involved at Ofcom in monitoring?

17 A Sir, I wouldn't be involved in this aspect of either the legal specification of these conditions
18 – I might sometimes comment on those but I wouldn't be involved in the implementation or
19 monitoring of them, except in perhaps unusual circumstances where there was a specific
20 economic issue that arose.

21 MR. THOMPSON: I would now like to turn to the history of the condition and Ofcom's policy
22 between 2004 and 2009. That is something you deal with at some length on pp.20 to 28 of
23 your statement. First of all, the 2004 Market Review which is core bundle E tab 12. I think
24 we just need to look at section 7. You deal with it quite quickly at paras. 46 to 49 of your
25 statement.

26 THE PRESIDENT: BT17 can be put away, I think.

27 MR. THOMPSON: I will come back to it.

28 A Yes, and which paragraph?

29 Q It is p.167, manuscript p.17.

30 A Yes, I have p.17.

31 Q If we start at 7.52 in the middle it says:

32 "Under the cost orientation obligation, BT will be required to provide wholesale
33 AISBO services at cost oriented prices, ...

34 7.54 As BT has been identified as having SMP in this market, the availability of

1 wholesale AISBO services at cost oriented prices would help to ensure that the
2 resulting competition in the retail leased lines markets and other downstream
3 markets should lead to lower prices."

4 Would you accept that there the market definition is clearly wholesale AISBO services and
5 the concern is excessive pricing on that market?

6 A The concern is excessive pricing in that market. I am not sure what you mean by "on that
7 market". The concern would, in my view economically speaking, relate, or could relate to,
8 excessive pricing on individual prices within that market where those individual prices were
9 economically meaningful. As I say, that's an economic interpretation of the concern.

10 Q There is nothing about that in this passage, is there, and in particular at 7.68, if you jump on
11 to that. You specify the concern:

12 "BT, as it has SMP in this market, has the ability to price above the competitive
13 level, so as to have adverse consequences for end users of public electronic
14 communications services."

15 That is simply the wholesale AISBO market as a whole; there is no indication of any sub
16 market, is there?

17 A I see the words. I'm just saying that my economic understanding of the nature of the
18 concern would relate to, or could relate to, individual prices being at an excessive level, and
19 not only the entirety of all the prices in the market at an excessive level, if that's what you
20 mean by "on the market". I'm still not quite sure I understand what you mean by "on the
21 market" as opposed to "in the market".

22 Q I think you probably heard the exchanges I had with Dr. Houpis. I was not proposing to go
23 back over those again. What I was putting to him is that excessive pricing is for the service
24 as defined, not for some subset or component service.

25 A My economic view on that would be that that is one potential concern, but there could still
26 be concerns about excessive pricing of individual prices within that market, where those
27 prices are economically meaningful.

28 Q I think that probably is a matter for legal rather than economic --

29 A As I say, I'm only giving an economic view, not a legal view.

30 Q Can we now turn briefly to the Energis Determination. I think you were not involved in
31 that. It appears in bundle BT14 tab 39. That is simply for dates. You will see on the first
32 page that the case was opened on 23rd July 2003 and closed on 3rd September 2004. Do you
33 see that, Mr. Myers?

34 A I'm sorry, where is that?

1 Q At the start of tab 39.

2 A I am in the wrong tab. Tab 39. Yes, I see that.

3 Q You will see that it's a case that opened on 23rd July 2003 and closed on 3rd September 2004.

4 So it was one of those cases that in fact did last more than four months, and where Ofcom

5 found there were exceptional circumstances arising out of the 2004 Market Review. Is that

6 something you know?

7 A As I say, I don't recall this case, but I can see from the dates that that's more than a four

8 month period.

9 Q We will get into this in more detail. You can see the scope of disputes is stated in various

10 places in this document. For example, on the third page the scope of the dispute:

11 "To determine whether BT should be required to offer and provide interconnection

12 variants of the following retail SHDS products"

13 And then 12 products including various LES services. So it was a parallel exercise to the

14 AISBO issues that arose in the 2004 Market Review. Do you see that?

15 A Yes.

16 Q If one then turns to tab 41 p.3 para.1.2. First of all, perhaps on the first page you can see

17 that this was published on 3rd September 2004, so two or three months after the LLMR

18 2004. Then Ofcom says:

19 "In line with its conclusions in the recently published review of retail leased lines,

20 ... Ofcom has determined that a wholesale variant of BT's retail SHDS products

21 falls within the alternative interface symmetric broadband origination market

22 identified in that review."

23 So it was self-consciously parallel to the 2004 review. So you see that?

24 A Yes.

25 Q Then at 2.3 to 2.7 Oftel and then Ofcom summarises the position that I think we have just

26 been discussing about the disputes and the extension of time. There was a complication

27 about transitional provisions. Then at 2.7:

28 "The relevant market definitions and access obligations relating to the products

29 requested by Energis were being considered by Oftel in its review of retail leased

30 lines ... The ongoing market review led Oftel to conclude that the circumstances

31 surrounding this dispute were exceptional and that, pursuant to Section 188(5) of

32 the Act, Oftel need not resolve this dispute in four months.

33 2.8 Oftel advised that it intended to wait until the conclusion of the market

34 definitions and access obligations in the leased lines market review before seeking

1 to resolve this dispute."
2 So the two were intertwining, do you see that?
3 A Yes.
4 Q Can I just briefly show you (I think you will say this is a matter of legal submission and that
5 is fine, but I think it is a matter the Tribunal will want to see in due course) at 3.3 through to
6 3.17 there is a discussion of network access, and in particular at 3.5 there is reasoning in
7 relation to products requested by Energis, so these are the wholesale products equivalent to
8 those we are concerned with in this case. Ofcom concludes that they fall within network
9 access because they fall within Section 151(3)(b)(2) of the Act. I do not think we need to
10 worry about that level of detail.
11 So far as you are concerned, I think the only question is that there is no reference here either
12 to this necessity argument of Mr. Saini, or to sub products of the kind that Ms Rose was
13 pursuing with Mr. Jones.
14 THE PRESIDENT: I do not see how Mr. Myers can answer that question - "there is no reference
15 here" - he would have to read this through. He is not familiar, particularly, with this
16 document. If there is no reference there and you have read it through, and you may well be
17 right, then you can make that point to us in due course, but you started out saying you are
18 worried about time so you need not waste time making points like that through Mr. Myers.
19 MR. THOMPSON: I think the only other point in Energis, given that indication, is the
20 Determination itself which one finds on p.21. You will see para. 1 lists six products, and
21 then para. 2 says: "The charge for the network access products listed in para. 1 of this
22 Determination should be reasonably derived" and then the familiar wording "from HH3.1".
23 Again, there is no reference to sunk products, it is simply the charges of those six products,
24 is that not correct?
25 A Again, I am not sure I have a view on exactly how this Determination should be interpreted,
26 but I see the words.
27 Q Can we move to a different topic, namely the contacts with BT over the period, including
28 the Thus dispute. For those purposes BT16 and 17 are probably the most useful places to
29 look. Can I ask you first of all about Mr. Jones' statement, which is in bundle 17, tab 1. I do
30 not know if you have seen Mr. Jones' statement before, but you know who Mr. Jones was?
31 A Yes, I have read this. I think I read it when it was submitted.
32 Q Can I take you to para. 48, p14, please? By way of context, you see in para. 45 Mr. Jones
33 describing the meetings between Ofcom and Openreach between 2006 and 2009. Then at
34 45 he says that they were roughly monthly with Karen Wray, and Karen Wray met more

1 frequently. At para. 48 it says:

2 "It felt to me at the time that Ofcom's focus was primarily on implementing and ensuring
3 compliance with the EOI requirements in the Undertakings so as to achieve the market
4 development it wanted. The impression I got was that that Ofcom did not want to set out
5 any hard and fast rules on cost orientation, so as to avoid any obstacles to one of its primary
6 objectives. What I mean by this is that, as far as I was aware, Ofcom did not indicate that
7 there was any absolute test or benchmark for cost orientation in relation to any product.
8 Instead, there were a number of different factors to take into account when discussing and
9 setting prices, including cost orientation and differential pricing across the products in the
10 Ethernet portfolio."

11 First, I think it is right to say there was no express guidance around the 2004 market review,
12 or you may say you do not know this, in the Energis Determination as to how cost
13 orientation was to be assessed. Would you accept that there was no express guidance in
14 either of those documents?

15 A That may well be. I am not sure I am in a position to confirm it without receiving those
16 documents.

17 Q Would you accept the last two sentences of Mr. Jones' statement?

18 A Sorry, do you mean in para. 48?

19 Q Yes?

20 A I am not in a position to comment on this. I don't believe I was involved in any of these
21 meetings. I certainly wasn't involved in Ofcom's work on implementing the EOI
22 requirements in the undertaking, so I think I just can't comment.

23 Q Yes, given that answer I think I will go straight to the Thus complaint, which is at bundle
24 16, tab 8. Presumably you are familiar that there was such a complaint? I think you said
25 you were not directly involved in dealing with it?

26 A That's correct.

27 Q So that is dated 11th May 2007, and that is addressed in Miss Wray's statement, which is at
28 tab 1 of bundle 16, and I draw your attention in particular to paras. 52 and 55. If I just give
29 you the context, that goes back to 44. You will see that there was a complaint from Thus,
30 which is referred to in paras. 44 and 45 and then there is a reference to a s.135 request, dated
31 5th June 2007, and we will look at that in a moment. What Miss Wray says by way of
32 general comment is at para. 52 and 55. First, the information she provided and the basis on
33 which it was provided, and then a meeting on 12th June - you may want to look at both
34 those paragraphs.

1 THE PRESIDENT: You would like Mr. Myers to read para. 52 and what, through to 55?

2 MR. THOMPSON: I am conscious of the time, but yes, 52 through to 55.

3 THE PRESIDENT: This was not challenged, of course, this statement. It is unchallenged

4 evidence.

5 MR. THOMPSON: It is really just to get your bearings, Mr. Myers?

6 A (After a pause): Yes, I have read those paragraphs.

7 Q Then if we look at the detail of what happened, we can see that at tab 10. You will see it is

8 5th June 2007 and Ofcom is sending a formal notice under s.135 of the Act. Over the page

9 you see the specified information, in particular paras. 4 to 6 and we see that Ofcom is asking

10 for calculations demonstrating how BT's current charges for each and every WES and

11 WEES product implies that BT's ex ante cost orientation obligation posed under the June

12 2004 LLMR. The same in 5, and then the same in 6. So in each case Ofcom is asking in

13 reference to the WES and WEES products.

14 THE PRESIDENT: The charges for each product, yes.

15 MR. THOMPSON: Yes. They put it by reference to the individual products and not in relation to

16 the sub-products. So in the same way as BT says, it is in relation to each and every product.

17 THE PRESIDENT: Well, it is BT's charges for each and every product.

18 MR. THOMPSON: That is right. (To the witness): Do you see that?

19 A I see the words here, yes.

20 Q If you then turn to tab 12, I think there was a draft sent out and then the formal - because on

21 24th May, so before the formal request, Miss Wray has commented on the request and at

22 point 2 Miss Wray says: "I have already discussed the intent behind questions 4, 5 and 6

23 with Graeme", who was an official, I think, of Ofcom, Mr. Hodgson.

24 "I understand that these questions are intended to be used to demonstrate understand that

25 these questions are intended for Openreach to use to demonstrate compliance with HH3. At

26 this stage Ofcom do not have in mind any specific expectations of data type that will be

27 provided in response."

28 Then there is a point of detail about the timing. So it is clear that BT understood that this

29 was the way that Ofcom was interpreting HH3 and that there was nothing specific Ofcom

30 required, no specific guidance as to what Ofcom required for the purposes of HH3. Would

31 you accept that?

32 A I don't think I'm in a position to comment on what BT understood. I see the words on the

33 page, I am not sure whether you are asking me to make an inference from them.

34 Q It is an exchange with Mr. Davies and Mr. Hodgson summarising a discussion, is it not?

1 THE PRESIDENT: Mr. Myers can read this, like we can all read it, Mr. Thompson, and see what
2 he said. He was not involved, Miss Wray does not say he was involved in any of these
3 discussions. I do not see what evidence Mr. Myers can give on this either as a witness of
4 fact for Ofcom, or still less as an economic expert. What is the point of asking these
5 questions?

6 MR. THOMPSON: Sir, the point essentially relates to what BT knew or could have known when
7 setting these prices in 2006/07 given that Mr. Myers clearly places a premium on the issue
8 of legal regulatory certainty, as he said at some length in relation to the FAC and DSAC
9 point.

10 THE PRESIDENT: You have his agreement that that is important. What BT could or should
11 have known is a matter for you to submit to the Tribunal. You might want to take us to any
12 of these documents you think relevant, but I do not think Mr. Myers can give evidence
13 either on what BT should have known, which is argument, or you did ask: is he aware of
14 any guidance, and he said "No", and that would not be necessarily his department. No
15 guidance has been put in evidence, and no doubt it would have been if there was, so there
16 we are.

17 MR. THOMPSON: (To the witness): Can I just take you to one more document before we leave
18 this, which is the response which BT in fact make, which is tab 13. Page 1, this is a letter
19 from Miss Wray to Mr. Hodgson manifesting understanding.

20 "The information request order we have supplied is to be used in order to assess BT's
21 compliance with Ofcom's SMP condition HH3. It is for this purpose the information is
22 provided."

23 Do you see that?

24 A Yes.

25 Q Then there is a lengthy attachment and, in particular, at p.5, under Question 6, in response to
26 the general question about compliance, do you see under that: "Each of the charges
27 published...", etc., and then in the middle of the paragraph it says:

28 "When LRIC costs are calculated (see spreadsheet titled Unit Financials - LRIC),
29 ROCE over 5 years is lower than that allowed by Ofcom. To achieve this would
30 require a further increases to rental prices".

31 So BT is giving information about "ROCE over 5 years". Do you see that?

32 A Yes.

33 Q And likewise when one turns into the detail you see, at p.13, this is the Ethernet Pricing
34 Paper which starts at p.9, and at 13 there is explanation of price movement.

1 A I am sorry, where is that? I do not seem to have numbering on it. No, I do actually.

2 Q I am sorry, it is KW13, it starts at 12 "Financial Impact".

3 A Sorry, yes, I do have it now. Yes.

4 A So there are three price movements described.

5 A I am sorry, where is that?

6 Q It starts at the bottom of 12, "... three main adjustments carried out".

7 A Yes.

8 Q You will see various movements and then underneath it says:

9 "The rebalancing carried out now means that prices more closely match to the costs of

10 providing services with all variants being profitable over 5 years".

11 Then:

12 "This difference is reasonable as this is not a cost plus regulated product".

13 So that is how BT was looking at it. Then at 15, under the heading "7 Regulation":

14 "Ethernet prices are subject to cost orientation principles and do not require Ofcom

15 authorisation. However, pricing of the Openreach Ethernet portfolio is seen by

16 Ofcom as one of the key factors in the effectiveness of the Undertakings which is

17 based on the access/backhaul component policy. There have been a series of meetings

18 with Ofcom over the course of the review to share and discuss the findings at each

19 stage including considerable discussion on the incentives for a CP to go down the

20 WES component route versus WEES. This has led to a wider policy debate over

21 incentives and the right backhaul structure/model going forward which will be

22 progressed outside these price changes. There is a risk therefore that Ofcom may wish

23 to make some changes downstream.

24 The agreed focus of the price review has been to refresh Openreach pricing to ensure

25 consistency with cost orientation principles going forward and separately to mitigate

26 the impact on the existing base where possible, e.g. 18 month moratorium on 10 MB

27 circuits".

28 So would you accept that this is evidence of ongoing discussions in mid-2007 between

29 Ofcom and BT about BT's pricing and how it was to be rebalanced in relation to Ethernet?

30 A I see it refers to discussions or involvement of Ofcom but I am not in a position, I think, to

31 comment any further as I was not involved in any of these interactions.

32 Q Fine. Then if you just turn to Tab 17 you will see where it all ended up. This is dated 10th

33 July 2007 and after the meeting which Miss Wray talks about, which is at Tab 15, which I

34 do not need to detain you with, and then the middle paragraph ends:

1 "Having considered the THUS complaint carefully, we consider the issues raised are
2 likely to be dealt with in the LLMR".

3 So as at July 2007 Ofcom was effectively putting off any ruling on cost orientation until
4 2008. Would you accept that?

5 A I am not sure that I am in a position to comment on exactly what this means.

6 Q Can we look at Bundle BT33 Tab 2. This is the document appended to BT's Reply.

7 A BT33?

8 Q BT33 Tab 2, yes.

9 A I am sorry, I have an extract from a BCMR consultation.

10 Q Yes, it is a slightly unusual document. I do not know whether it is something within your
11 knowledge, but what seems to have happened is when the consultation started for the 2008
12 Review Ofcom included an annex relating specifically to AISBO pricing. Do you recall
13 that?

14 A I was not involved with this at the time but I have looked at this annex.

15 THE PRESIDENT: So this is an annex to the consultation, is that right?

16 MR. THOMPSON: Yes. It was issued ----

17 THE PRESIDENT: Or an annex in the consultation.

18 MR. THOMPSON: -- in January 2008.

19 THE PRESIDENT: Yes.

20 MR. THOMPSON: At 12.1 it says:

21 "The purpose of this annex is to set out a high level comparison of the price of BT's
22 wholesale Ethernet services with the Ofcom's preliminary assessment of the cost of
23 delivering those services".

24 Then at 12.2 and 3 it summarises the THUS complaint and Ofcom's reaction. You will see
25 at 12.3:

26 "We decided to open a full investigation because we considered the issues raised in
27 the complaint were likely to be dealt with in the LLMR".

28 Then at 12.4 Ofcom seems to be finding that the THUS complaint was not well-founded, in
29 the first sentence. Do you see that?

30 A Yes, based on the work performed to date. Yes.

31 Q Then there are some general remarks about concerns that Ofcom did have and then the
32 matter is dealt with at some length, but the passage I would like to take you to is 12.21.
33 You will see that it is under the heading "Ofcom analysis", which starts at 12.17. So in
34 12.17 there is a significant market power finding in the AISBO wholesale market and

1 alluding to cost orientation. Then 12.18 they are saying the RFS do not contain the level of
2 detail required. Then there are some adjustments at 12.19 and 12.20, and then at 12.21,
3 which is the passage I wanted you to look at in particular, where Ofcom says:

4 "For this particular exercise we confined ourselves to comparing costs prepared on a
5 fully attributed costs (FAC) basis with individual service prices. We therefore did not
6 attempt to obtain an incremental ('floor') and standalone cost ('ceiling') information.
7 In principle a range of prices could be consistent with BT complying with its cost
8 orientation obligations, with the FAC being only one such value".

9 What I am going to ask you, as at January 2008 was that the best guidance BT had as to
10 compliance with cost orientation, that there were various tests that could be applied and that
11 Ofcom had not reached a concluded view? Would that be a fair summary?

12 A Again I am not sure I am in a position to -- I would have to review all the relevant material.
13 My understanding was this issue was dealt with in the *PPC* judgment. I may be wrong on
14 that but that was my understanding, where there were discussions about the 2001 guidelines
15 and various other documents.

16 Q Yes, but in relation to AISBO this is actual evidence about Ofcom's position and I am
17 asking you whether you agree with it or not?

18 A I am sorry, I did not think you asked me whether I agree with what is here. I thought your
19 question was, was this the best guidance that BT had.

20 Q On the AISBO market.

21 A On the AISBO market.

22 Q This is a specific publication relating to AISBO.

23 A So it may be but I am not in a position, without knowing what other documents there may
24 be, to know for sure whether that is the best guidance.

25 Q But you are not saying there is anything wrong with this document?

26 A No.

27 Q It is an Ofcom document?

28 A I am not saying that what is said in 12.21 is either incorrect or different from what, having
29 been at Ofcom at the time, Ofcom, I think, would have thought about the role of floors and
30 ceilings.

31 Q It is not just about floors and ceilings. It is about individual FACs and what information
32 Ofcom had and really how far Ofcom was pushing this specific market. That is what this is
33 all about, is it not?

34 A So I would say that this paragraph is consistent with my understanding of the role of floors

1 and ceilings and the role of FAC. I am not sure whether you are asking me to comment
2 beyond that.

3 Q I think I have put the point to you, Mr. Myers, that this is the best guidance that Ofcom was
4 offering in relation to the AISBO market at this time, was it not?

5 A As I have said ----

6 THE PRESIDENT: Mr. Myers says he cannot comment ----

7 A It may be I am just not ----

8 THE PRESIDENT: -- without checking everything else. Would that be a convenient moment to
9 take a break? We did start at 10.00. We must take a 10 minute break, so we will come back
10 at quarter-to.

11 (Adjourned for a short time)

12 Q Mr. Myers, could you take BT5, please. I think you said you were not directly involved in
13 the 2008 Review, but obviously you have familiarised yourself with it for the purposes of
14 these proceedings - is that right?

15 A Yes, to some degree, clearly there's an awful lot of detail in it.

16 Q Yes, I was not proposing to go into that level of detail, otherwise we could be here for some
17 months. Can I take you, first of all, to p.184, para.8.30, it is just to orientate ourselves as to
18 what this was. This was a complete Review, new market definitions, new SMP findings
19 and new conditions - that is right, is it not?

20 A Yes.

21 Q The 2004 conditions were all repealed with effect from 8th December 2008 - that is right, is
22 it not?

23 A As I understand it, yes.

24 Q One sees that in formal terms at p.364, annex 8 to the Review, and you see the heading:
25 "Revocation of notifications, identification of certain markets, the making of
26 market power determinations, the setting of SMP service conditions, and the
27 setting of Directions under SMP service conditions."
28 So this was a whole new regime under this direction - is that how you understand it?

29 A Yes, a new set of market definitions, SMP and SMP remedies, yes.

30 Q If you turn to p.365, para.2(d), there a specific market definition "up to and including one
31 gigabit" AISBO services - is that right?

32 A Yes.

33 Q Then if you turn on there are market power findings at 3 - do you see that?

34 A Yes.

1 Q Then if you turn on to 12 on p.368, there appears to be a typographical error because it says
2 24 June 2003, whereas I think it should be 2004, but it says:
3 "The Notification and SMP Conditions set out in Annex D of the 'Review of retail
4 leased lines, symmetric broadband origination and wholesale trunk segments
5 markets' ...
6 I think that is the LLMR 2004 -
7 "... and any subsequent modifications to the SMP conditions set by those
8 Notifications or any Directions under these SMP Conditions shall be revoked by
9 this Notification when it takes effect under sections 48 (1) and 79 (4) of the Act."
10 Do you see that?
11 A Yes.
12 Q Then over the page you will see that it was signed by Gareth Davies, Director of
13 Competition Policy, on 8th December 2008 - do you see that?
14 A Yes.
15 Q If we now look at the AISBO market, we can take it quite briskly, if you turn right back to
16 the beginning there were a market definitions made, and in particular at 1.11, if you turn
17 over to p.5, you will see, "Low bandwidth AI services at speeds up to and including
18 1Gbit/s" - do you see that?
19 A Yes.
20 Q Then at 1.28 to 30 ----
21 THE PRESIDENT: That is the retail market, is it not, and then 1.14 is the wholesale market?
22 MR. THOMPSON: Yes, the specific wholesale markets ----
23 THE PRESIDENT: Paragraph 1.11 is the retail market.
24 MR. THOMPSON: Yes, and then the wholesale product markets are identified at 1.14 and then
25 1.28 to 1.30 - is that correct?
26 THE PRESIDENT: Yes.
27 MR. THOMPSON: So there was a different market definition and a different remedy on the
28 newly defined low bandwidth AISBO market, both cost orientation and cost control. That
29 is right, is it not? One finds at that 8.291 on p.238?
30 A Yes, a charge control.
31 Q It says: "... in principle be subject to a charge control" and then at 3.01 to 3.04 there is a
32 rather more lengthy discussion of cost orientation concluding that at 3.07 pp.240 to 243 and
33 then over the page to 244 there is detailed discussion of cost orientation and the basis for the
34 application, in particular 3.04 there is a discussion of cost orientation on 243. Just to close

1 this off, so that is the reasoning there. I do not think we need to go into any detail about it.
2 Then if one turns back to para.1.51 p.12 you will see that this was not the end of the story.
3 1.51 says:

4 "Our charge control proposals are the subject of a separate consultation document,
5 which is being published alongside this Statement."

6 So on 8th December 2008 the 2004 conditions were repealed, the cost orientation obligation
7 was varied and imposed on the newly defined market, is that right?

8 A Yes, that's my understanding.

9 Q And the decision in principle was taken to bring in cost controls and another consultation
10 document was issued on that subject, is that right?

11 A It's a charge control. You said cost control; it is charge controls.

12 Q I hope that a new document has been added to your additional documents bundle 2. There
13 has been some re-numbering. I hope it is at tab 38.

14 THE PRESIDENT: The charge control consultation?

15 MR. THOMPSON: Yes. That is also dated 8th December 2008. May I turn you through to p.7
16 you should see para.1.20 and there is reference to bringing the current charges in line with
17 an efficient level of costs at the end of the control. Then:

18 "In cases where prices at the start of the control are materially out of line with costs
19 there may be an argument for making one-off adjustments to these charges to bring
20 them more in line with the underlying costs of provision."

21 Do you see that?

22 A Yes.

23 Q Then 1.21 there is reference to a number of adjustments made effectively voluntarily by BT.
24 Do you see that?

25 A Yes.

26 Q Then at 1.24-125 Ofcom sets out its general position. So:

27 "The effects of the BT price changes is to decrease current AI basket revenues by
28 around 30%. These proposed price adjustments are expected to be implemented
29 fully before the charge control comes into effect and our proposals have been
30 developed on that assumption ... Our provisional view is that given the scale of the
31 proposed price reductions Openreach should not be required to make any further
32 one-off changes when the charge controls are introduced. Prices for services in the
33 AI basket should not then increase in nominal terms between the implementation
34 of the controls and 1st October 2009 following which the RPI minus X formula

1 should apply. Thirdly, the prices of all the services in the AI basket should be
2 brought within the DLRIC clause and DSAC ceilings within 12 months of the
3 implementation of the charge control."

4 What I want to put to you, Mr. Myers, is that we have seen that the last complaint was
5 closed on the basis that the issues would be addressed in the 2008 Market Review. Did you
6 see that? That was the basis on which it was closed.

7 A Yes.

8 Q We have seen a consultation document setting out Ofcom's provisional position on cost
9 orientation issued in 2008. Do you recall that? We looked at that just before. You
10 remember Annex 12?

11 A Yes.

12 Q Would you accept that the purpose of these changes, partly voluntarily by BT, partly by
13 Ofcom, was Ofcom's way of dealing with cost orientation, was it not? That was the way
14 that Ofcom was proposing to deal with this issue?

15 A I don't think I'm in a position to comment on that. I think I would probably need to review
16 other bits of the parts of the document.

17 Q Can I now take you to some more general topics that you address in your report.

18 THE PRESIDENT: May we put BT away?

19 MR. THOMPSON: We can now go back to Mr. Myers' evidence. Mr. Myers, you will recall that
20 in relation to the FAC/DSAC proposal of Sky, one of the four reasons you give for rejecting
21 it is that it would be contrary to the principle of legal or regulatory certainty. Do you recall
22 that?

23 A Yes.

24 Q One finds that in paras.76 to 79 of your report. In 76 you say:

25 "In addition to any legal questions on the validity of such an approach a number of
26 years after the 2004 LLMR decision was made [and one might add, several years
27 after it was repealed as a gloss] (on which I do not comment), accepting such an
28 approach would be contrary to regulatory certainty and in my view it is likely to be
29 contrary to the long-term interests of competition and consumers, as I explain
30 below."

31 Do you remember that?

32 A Yes.

33 Q Then at the end of 79, after your very long discussion, you quote a passage from the
34 Decision saying:

1 "It is therefore important that we follow the approach which BT and the industry
2 could reasonably have understood we would take, unless there is good reason as to
3 why we need to depart from that approach."

4 When you say "BT and the industry could reasonable have understood", when are you
5 talking about? Are you talking about the time when BT set its prices? For example, 1st
6 January 2006, or some other time? What do you understand Ofcom to mean by that?

7 A I think I should look at the paragraph in context. Where is the Determination?

8 THE PRESIDENT: Core bundle B p.111.

9 A Thank you.

10 MR. THOMPSON: 9.149:

11 "In this section we explain why the approach advocated by TTG and Sky is not
12 only contrary to that set out by the CAT in the PPC Judgment, but is also contrary
13 to that which BT could have reasonably expected us to adopt during the Relevant
14 Period."

15 So that is the period of the dispute, but presumably it is not over the whole period; it must
16 be the period when BT set its prices, must it not? For example, the fact that it may have
17 known something on the last period would not be good enough; they must have known it
18 when they set their prices. Is that not right?

19 A Yes, so para.9.150 is about why regulatory certainty can affect investment and competition
20 and that would have been contemporaneous with the prices that we are looking at.

21 THE PRESIDENT: You are saying it is when the prices are being set?

22 A Yes, that's correct.

23 MR. THOMPSON: I think you will recall Dr. Maldoom's evidence in his first report at core
24 bundle D tab 3 paras.24 and 25. Dr. Maldoom summarises the effect of HH3.1 at 24 and
25 then he goes on:

26 "However, no specific cost test is defined within the cost orientation obligation
27 (Condition HH31.). The issue of how common costs might be recovered across
28 different services is left open. The time profile for recovering the cost of assets is
29 unrestricted, other than through the requirement that asset returns are 'reasonable!'"

30 That is all correct, is it not?

31 A Are you asking me for a legal interpretation of the condition, or an economic view?

32 Q I am saying does HH3.1 specify the time or the test or the nature of the test that is going to
33 be – that is an opinion that Dr. Maldoom has put forward as an economist and I am asking if
34 you agree with him.

1 A It seems to me that Dr. Maldoom is commenting on the interpretation of the condition
2 which I wouldn't propose to do.

3 THE PRESIDENT: What he is saying is that the condition does not specify DSAC for example.

4 A In terms of the words in the condition, I agree DSAC is not a concept that's specified in the
5 words of the condition itself.

6 MR. THOMPSON: And the timing is not specified?

7 A Yes, I recall there is no comment on timing.

8 Q Even Ofcom has not said: what did you charge Sky on 1st January 2008 for that particular
9 BES circuit which, on one reading one could do. But any level of aggregation, there is
10 nothing in the condition about it, is there?

11 A Aggregation? Are you asking me about aggregation?

12 Q Ofcom has taken it on an annual basis to compare revenues to costs.

13 A Oh, aggregation across years, is that your question?

14 Q It is actually individual years. You have compared individual revenues to individual costs
15 across the entire product, have you not, for BES 100 rental for example?

16 A Yes, so Ofcom did a year by year comparison of revenues and costs.

17 Q For particular disaggregation, but aggregated across a year?

18 A Yes.

19 Q And there is nothing about that in HH3.1?

20 A It is not explicit in the wording of the condition.

21 Q Do you say it is implicit in the wording?

22 A I am not commenting on whether it is implicit. I have no view on whether it is implicit.

23 Q I think you are agreeing that it is not in the condition.

24 THE PRESIDENT: Well, Mr. Myers has been quite careful. He says it is not express and he
25 cannot comment on the proper interpretation.

26 MR. THOMPSON: (To the witness): Do you understand BT's case which is that it will be
27 contrary to the principle of legal certainty for Ofcom to apply a methodology that was not
28 clear when the price was set. That is our point on this. Do you understand that is our point?

29 A Yes. I mean obviously there are issues about questions of exactly what legal certainty
30 means, but at a general level I understand.

31 Q So to take a concrete example if Sky purchased a BES 100 service on 1st January 2006 you
32 have to understand the cost methodology that Ofcom would have applied if it had asked BT
33 to justify the charges levied on 1st January 2006, and to show that it was clearly stated to BT
34 at that time. That is the point - you understand that?

1 A I am sorry, could you repeat the point?

2 Q You are imagining BT pricing a service to Sky on 1st January 2006 and what you need to
3 know is what was clear to BT when it imposed that price on 1st January 2006. Do you
4 understand?

5 A Sorry, you say "what you would need to know is what BT understood", is that your ----

6 Q That is the relevant question for the purposes of legal certainty, do you understand?

7 A If you tell me that's what legal certainty means then I don't have a view on exactly what it
8 means.

9 Q I think that is what you said yourself at the time - the relevant time is when the charges were
10 settled?

11 A I talked about regulatory certainty, and it is an overlap concept in terms of legal and
12 economic.

13 Q All right, well call it "regulatory certainty". The relevant date is when the price is settled?

14 A Yes, I think it's about what BT either knew or could reasonably have been expected to
15 know.

16 Q If we turn to the present FACs, which we have looked at, it is clear that BT and Ofcom were
17 discussing all this between 2006 and 2007 and that in May/June 2007 BT sent a lot of
18 information to Ofcom, specifically in relation to this condition, including pricing papers
19 setting out its approach. We have looked at that, have we not?

20 A We have looked at various papers, yes.

21 Q And in response Ofcom did not offer any guidance at all as to whether that methodology
22 was acceptable or not, did it?

23 A That's my understanding.

24 Q Do you think BT could have guessed from Ofcom's behaviour whether or not the approach
25 was acceptable to Ofcom as at the middle of 2007?

26 A Which approach?

27 Q The approach that BT set out in the detailed response to the questions arising out of the
28 Thus complaint?

29 A Sorry, just to clarify, do you mean - there were various aspects, were there not, there is a
30 comment about looking at ROCEs over five years, is that the point you were putting to me?

31 Q Yes. Could not BT have known whether that was acceptable to Ofcom, given that it closed
32 the case?

33 A So on the basis of the particular correspondence you have taken me to, as you have already
34 said, there was no specific guidance put forward by Ofcom. Whether BT could have known

1 from other documents, or from the meaning of the condition I don't know, I don't have a
2 view on it.

3 Q It does not seem that whoever wrote annex 12 was any the wiser because they said that it
4 was all very uncertain. We can see in para. 12.21, we looked at it ----

5 A But my understanding of annex 12 is that it looks at one year's worth of data, one year's data
6 and it commented about looking at it on an FAC basis and commented that it wasn't floor
7 and ceiling information.

8 Q Yes, and then they concluded: "In principle the range of prices could be consistent with BT
9 complying with its cost orientation obligations ----"

10 A Yes.

11 Q "-- with the FAC being only one such value". Is that clear as to what BT were supposed to
12 do as at January 2008?

13 A Perhaps I should just get that paragraph in front of me - where is it?

14 Q BT33, p. 455 of the consultation document?

15 A I think this is clear - it is at least clear to me. This is saying that prices can vary between
16 floors and ceilings and FAC would typically be expected to fall between floors and ceilings
17 but there could be greater flexibility than just the fully allocated cost.

18 Q But it does not say what the range is, it just says "a range" could be consistent with cost
19 orientation?

20 A Since that sentence follows a sentence which says: "We therefore did not attempt to obtain
21 incremental floor and standalone costs ceiling information", the way I am reading this at
22 least the following sentence is referring back to the range between floors and ceilings.

23 PROFESSOR MAYER: Can I just ask in relation to that, is it clear from that, it talks about stand
24 alone cost which, I think as you say in your report is not the same as DSAC, would it be
25 clear from that what the ceiling is in this regard?

26 A I think it probably would have been but there has been some different use of terminology
27 over time. So the "ceiling" was typically used as the shorthand for DSAC. That was Oftel's
28 usage from 1997. In the 1997 guidelines which introduced and described these concepts, it
29 used the word "ceiling" to refer to what later became known as the DSAC. So I think it
30 would have been understood that standalone cost ceiling meant DSAC.

31 MR. THOMPSON: Can you turn to Ofcom's skeleton argument in the skeleton arguments'
32 bundle, tab 4. Page 19 ----

33 A Sorry, I do not seem to have it.

34 Q I am sorry, Mr. Myers. It is a single paragraph, I do not know if someone can provide Mr.

1 Myers with para. 57. (Same handed)

2 THE PRESIDENT: Somebody is helpfully handing it up.

3 MR. THOMPSON: It is p.19, para. 57. Under (ii) it says:

4 "BT was under an obligation to be able to demonstrate that its relevant charges
5 were cost-orientated in compliance with Condition HH3.1. In principle BT could
6 do so by any means that satisfied the terms of Condition HH3.1. Furthermore, if
7 BT was unclear as to whether its proposed means of demonstrating compliance
8 with Condition HH3.1 was likely to satisfy Ofcom, it was open to BT to seek
9 confirmation at any time. "

10 We have seen the interaction between Miss Wray and Ofcom over a period of a year, and
11 the information that was provided to Ofcom. Do you think it is fair to say that BT should
12 have done more to find out what Ofcom's view was, given that it did provide detailed
13 information in response to Ofcom's specific request?

14 A I am sorry, should have done more to?

15 Q Is it fair to criticise BT given that it gave detailed information to Ofcom on this specific
16 issue?

17 A I think I find it quite difficult to comment on that without being in a position - certainly, as I
18 say, I wasn't involved in any of those discussions, so I think I would probably need to
19 review all the documents and also be aware of any other documents which might be relevant
20 before I was able to offer a firm opinion.

21 Q We will move on if that is the position. Can we now look at two specific issues about legal
22 certainty? First, I am sure you will remember there is the issue of the 2009 charge control,
23 which is at core bundle E, tab 14. You see in 5.90 and 5.94 - I am sure you have looked at
24 them in preparing - p.157 and 158, (pp. 44 and 45 of the manuscript). You set out the
25 approach that you have taken to the issue of connections and rentals and, in particular, at the
26 end of 5.94 you say:

27 "This is not a definitive position in relation to BT's compliance with its cost
28 orientation obligation, but it does reflect our interpretation of the requirement
29 based on the information currently available."

30 By this time we are talking about, I think, July 2009, Ofcom had a great deal of information
31 available about cost orientation, did it not?

32 A It had certain cost information, yes.

33 Q It had all the responses that BT had made to the Thus complaint?

34 A Yes.

1 Q And all the work that it had done for the purpose of annex 12 of the consultation document,
2 and all the work it had done for the 2008 review and the charge control, it had all that?

3 A Yes, and there is a significant amount of cost information and revenue information in that,
4 yes.

5 Q So against that background, do you think this was making it clear that Ofcom would take
6 the approach that it now adopts to the issue of connections and rentals? Was that made
7 clear to BT in July 2009?

8 A I think as I have said before, I didn't work on this document. It is just that you used the
9 word "you" talking to me about this document, and I wasn't involved in this document, so I
10 have no insight into exactly what was going on. I only see the words in the statement, as
11 others can. I find it quite difficult to see exactly what this means. On the one hand there is
12 a heading to para. 5.94 which says: "Our starting charge adjustments are without prejudice
13 to BT's cost orientation obligations" and then there is the sentence you pointed me towards.

14 Q Does that not make it clear that at that stage Ofcom's view was that you should do a three
15 year average aggregation of connections and rentals. That was the clear position that
16 Ofcom was publishing, was it not?

17 A That's not clear to me, but, as I say, I don't have its insight into what lay behind these words.
18 I'm aware that Ofcom in the Determination commented that this was not intended to comply
19 with cost orientation. That's a comment I think I refer to in my witness statement, but I
20 don't have my own view on whether that's the case or not.

21 Q The other point really arises most clearly out of Article 13.3 of Access Directive which
22 Ofcom refers to in the passage we looked at in the skeleton argument that we have just been
23 looking at, and that is at tab 1 of this same bundle. Would you turn to p.15 of the Official
24 Journal, do you see the point about the burden of proof?

25 A Sorry, which ----

26 Q It is towards the left hand side of p.16, Article 13.3, "Where an operator has an obligation" -
27 do you see that?

28 A Yes, I see that.

29 Q And the point that Ofcom is fond of is the fact that the burden of proof rests on BT. The
30 provision goes on:

31 "For the purpose of calculating the cost of efficient provision of services, national
32 regulatory authorities may use cost accounting methods independent of those used
33 by the undertaking."

34 So the effect of that is that Ofcom is not bound by the approach that BT takes. It can take a

1 different approach - that is correct, is it not?

2 A Yes, that seems to be what this says.

3 Q And that is what has happened in this case. BT, as you said in examination in chief with
4 Miss Gallafent, certain adjustments were made by Ofcom to BT's prices after the event?

5 A Sorry, to BT's costs - costs in the RFS, yes. That's correct, there were a number of
6 adjustments to the published RFS data.

7 Q Yes. Would you put your mind back to our example of BT pricing on 1st January 2006,
8 how could BT know whether Ofcom was going to change its costs and, if so, what changes
9 it was going to make? How could BT know that?

10 A I think it would be reasonable to expect that BT would know that, given the basis on which
11 those adjustments were made by Ofcom. So a necessary condition for Ofcom to make an
12 adjustment in the framework it set out in the Determination was that there was either an
13 error or an obviously inappropriate methodology. I would have expected BT to expect that
14 if it made errors or used obviously inappropriate methodologies that adjustments would be
15 made.

16 Q Did Ofcom consider what BT could have known in 2006, or did it just consider what it
17 thought was the right answer in December 2012?

18 A When deciding on the cost adjustments?

19 Q Yes.

20 A I haven't commented on the cost adjustments in my witness statement, so I'm not sure ----

21 THE PRESIDENT: Just to be clear, if I may interrupt for a minute, are you asking now about the
22 particular adjustments that were made, such as transmission costs, or are you asking about
23 use of more fundamental points, such as use of DSAC as the benchmark, or aggregation of
24 cost years, because I think they are slightly different points?

25 MR. THOMPSON: Yes, they are, we can take them in stages.

26 THE PRESIDENT: I think you will probably need to separate them out.

27 MR. THOMPSON: In terms of the general methodology that was adopted, and we have taken
28 one example, the approach to connections and rentals, I put it to you that it was not made
29 clear, for example on 1st January 2006, that this would be the approach Ofcom would take,
30 and I am not quite sure what your answer is. I put it to you on those general issues it was
31 not made clear?

32 A Sorry, in January 2006, did you say?

33 THE PRESIDENT: I think that was just an illustration. When BT set its prices at the time, you
34 have agreed, and it is common ground for everyone, that regulatory certainty is important,

1 BT should reasonably have known what it should do. What is being put to you is on what
2 basis is it said that BT should reasonably have known that it should look at costs for
3 connections separately and costs for rentals separately, as opposed to in aggregate. That is
4 the question, I think.

5 A As I understand it, one of the arguments being put forward on the other side is that the
6 wording of the condition made it clear. I think I report that Ofcom's view, in my witness
7 statement, in the section dealing with connections and rentals, I think that would be
8 potentially the basis. As I say, that is not a matter I have - that seems to me the
9 interpretation of a legal condition, but that's an argument I understand Ofcom made in the
10 Determination and perhaps in its defence as well.

11 MR. THOMPSON: The other point was that there have been a lot of detailed discussions which
12 are still going on about how particular costs should be treated and the mistakes that were
13 made and things of that kind. Do you say that BT should have anticipated all those
14 discussions when it was pricing, for example, in 2006, and it should have known how
15 provisioning costs, for example, would be treated when it was pricing in 2006?

16 A Well, I do say that I think BT either should have avoided errors or obviously inappropriate
17 methodologies, or expected that errors of obviously inappropriate methodologies would be
18 adjusted.

19 Q How would it know which ones were going to materialise?

20 A Because there were errors or obviously inappropriate methodologies. Are you suggesting to
21 me that if BT made decisions - let us take the case of errors - BT made decisions on the
22 basis of errors, that it's reasonable to rely on the data that includes the errors for the purpose
23 of justifying BT's charges? I'm not sure if that's what you're putting to me, but if it is then it
24 doesn't seem to me that that would be very sensible, and it seems to me that BT should
25 expect that, if it makes errors, they would be corrected.

26 Q We are looking at the position going forwards, and Ofcom is saying, "Come and justify that
27 price", that is pretty much what happened in 2009, then BT puts it forward, Ofcom accepts
28 it or does not accept it. If it does not accept it and it says, "No, the answer is this, so change
29 your price". Now we are thinking of something much more difficult. BT made some
30 decisions in 2006, and I am asking you how on earth it could know that in December 2012
31 Ofcom would say this or that about provisioning costs? It is just impossible, is it not?

32 THE PRESIDENT: I think what Mr. Myers is saying is, one, if BT made a mistake in 2006 in its
33 costs BT should have known that when Ofcom came to look at it it would correct that
34 mistake, and that would be reasonable for BT to have known. That is point one. Point two,

1 if BT did its cost allocations on - I think his words were - obviously inappropriate
2 methodologies, BT should reasonably have known in his view that when Ofcom came to
3 look at it it might reject an obviously inappropriate methodology and substitute one that was
4 appropriate. That is at the general level. Now on provisioning costs, and if we look at that
5 specifically, then one has got to ask, "Is that a case of error or is it a case of obviously
6 inappropriate methodology?" If it is then we have the answer, but it may be that you will
7 want to look at that and say what is obviously inappropriate about it on the specifics.

8 MR. THOMPSON: I think for present purposes it is probably ----

9 THE PRESIDENT: On the general I think Mr. Myers has answered why BT should have known
10 that and expected that.

11 MR. THOMPSON: As in previous areas, I think we may be moving to an area of submissions. I
12 am not proposing to take it any further.

13 THE PRESIDENT: Maybe that is something that Mr. Read addresses, the adjustments, I do not
14 know.

15 MR. THOMPSON: (To the witness) Can I move on to a different topic, which is flexibility in
16 pricing. You will recall that in addressing the Houpis test one of your principal arguments
17 is to emphasise the benefits of pricing flexibility and the value of leaving it to a supplier to
18 determine the structure of its charges, and if one turns to para.87 of the statement ----

19 THE PRESIDENT: That is bundle?

20 MR. THOMPSON: Bundle D/13, your statement, Mr. Myers, para.87, p.38. As I understand it,
21 you are saying that price signalling is good because it gives appropriate indications to the
22 market. So you are in favour of flexibility in pricing - is that right? You make the point a
23 number of times. For example, at 122(b) you refer to the concept of "Ramsey pricing" in
24 favour of flexibility, which I take it to be BT's flexibility, and then at 126 you quote from
25 the Determination that it is appropriate to allow the firm flexibility to set prices to reflect
26 demand conditions. At 129 you express concerns that Dr. Houpis's approach may result in
27 insufficient pricing flexibility to pursue an efficient structure of charges, and at 131 you
28 refer to the benefit of a regulated firm being allowed greater price flexibility to set its
29 charges. Do you see that?

30 A Yes, there's a number of different - those are generally about flexibility but there are some
31 specifics, and perhaps it's worth making the point that what's appropriate is likely to depend
32 on the specific market circumstances. I think the different paragraphs you referred to talk
33 about some different circumstances. For example, para.87 is primarily talking about a
34 market at an early stage of development, whereas para.131 is, or at least the first part of that

1 is talking about a more mature market.

2 Q Yes, you are basically saying it is a good thing to leave it to the market and to have some
3 price signalling and price flexibility, and I think Ramsey pricing is the limit of that
4 approach, I think it was said it is the "gold standard" by one of the previous witnesses.

5 A So whether it is a good thing to leave it to the market, as you put it, depends somewhat on
6 the circumstances, but typically it will be desirable in some circumstances to leave it to the
7 market, as you put it. Ramsey pricing is primarily a retail concept, but it is defining
8 economically and allocatively efficient retail prices. In the case of wholesale prices such as
9 this there are some further complications because what matters is not just the price signals
10 that those wholesale prices imply for the retail level, but also decisions at the wholesale
11 level in terms of choice between inputs and entry, for example. So there is a fairly
12 complicated set of considerations, but flexibility, as I say, can often be a desirable thing.

13 Q I would like to contrast that to what you say at the end of your report where suddenly
14 flexibility and pricing link seems to be a bad thing. At 285(c), for example, under the
15 heading "Fixed proportions", you say:

16 "Where CPs purchase services in varying proportions it is important that each
17 charge is individually cost orientated because the prices will generally provide
18 economically meaningful signals for potential purchasers in their decisions on
19 services to purchase and investment decisions about self-provision or entry.

20 Aggregation would allow BT to charge a high price for one service and a low price
21 for another, which would disadvantage those that bought relatively more of the
22 high-price service, and all CPs would face distorted price signals."

23 Is this not the very same flexibility that you were praising earlier in your report?

24 A No, it is not the same. This is essentially, I think it might have been the first of the three
25 issues you put to me about which charges should be cost orientated at the start of this cross-
26 examination. That is what the first sentence is dealing with. It is talking about where there
27 are economically meaningful price signals. There would still be significant flexibility for
28 BT over where that price was set under cost orientation, under Ofcom's view of cost
29 orientation, because it could be set at least between the DLRIC and the DSAC and
30 obviously there would also be non-mechanistic application of those tests. So looking
31 distinctly at, for example, connections and rentals, still provide BT with significant
32 flexibility and it is not just the flexibility between DLRIC and DSAC. I think you also need
33 to take into account the fact that BT is choosing the cost allocations, subject, of course, to
34 the test we talked about errors or obviously inappropriate methodologies. So that seems to

1 me to provide very substantial flexibility for BT.

2 Q It is just the same issue about -- that arises in Ramsey pricing just the same. You are not
3 following your costs, you are following the demand conditions and you are setting flexible
4 prices. There is nothing about these prices being excessive, is there? It is just you are
5 saying now it is bad to have flexibility.

6 A But when it talks about a separate price being economically meaningful, what that would
7 imply, and I think I develop this later on in the witness statement, is that where a price is set
8 above the appropriate measure of costs that could be considered an excessive price where it
9 is an economically meaningful price.

10 Q If it is excessive.

11 A Yes, indeed.

12 Q But if it is not excessive it is the same virtuous situation that you describe earlier in your
13 report, is it not?

14 A But you are putting to me an inconsistency and I do not see any inconsistency because the
15 approach that Ofcom adopted allowed BT substantial pricing flexibility.

16 Q I was not going to go to it but perhaps we should go to it. Paragraph 8.57 of the
17 Determination, Core Bundle B.

18 THE PRESIDENT: Page 69.

19 A Thank you.

20 MR. THOMPSON: It is an argument that is deployed in relation to connections and rentals, but it
21 is a general point about pricing flexibility, is it not? That if BT charges a high price for
22 Service A related to costs and no price for Service B, you give pricing signals to the
23 purchasers of A and B. That is what it is saying, is it not?

24 A That is not what it is saying. It is suggesting that a high price relative to costs for A and a
25 low price for Service B relative to costs again, I think it is suggesting that that would be
26 undesirable and that seems to me consistent with the DLRIC/DSAC range that will apply.
27 Indeed, I think this is what is meant by the reference to costs here.

28 Q Why is it undesirable in the DLRIC/DSAC range?

29 A Not within the range, no. Not within the range, outside of that range.

30 Q You will recall the discussion I had with Dr. Houpis about the DLRIC/DSAC range, I think,
31 and I put to him the example of connections being set at 4 and rentals at 10, or rentals at 4
32 and connections at 10. That would be very strong pricing one way or the other and, as far as
33 I understand it, you say that would be a good thing, for BT to have that degree of
34 flexibility?

1 A I am sorry, I have not quite understood the example with the numbers.

2 Q You may recall Dr. Houpis ----

3 A I do not recall.

4 Q -- gave evidence that DLRIC and DSAC were a multiple of 2.5 apart, that DSAC was about
5 2 and a half times DLRIC.

6 A So we are saying the DLRIC is 4 and the DSAC is 10. Is that right?

7 Q Yes, and you could set rentals at 4 and connections at 10 or connections at 4 ----

8 A I am sorry, is this the DLRIC for connections and the DSAC for connections or them on an
9 aggregated basis, or what?

10 Q Yes, supposing the DLRIC for each is 4.

11 A The DLRIC for each is 4?

12 Q And the DSAC for each is 10.

13 A 10, right, yes.

14 Q So, as I understand your response to Mr. Pickford, you are saying that is a good thing, that
15 BT could price connections at 4 and rentals at 10, or connections at 10 and rentals at 4.
16 That will be good flexibility?

17 A So that would be flexibility within the range set by DLRIC and DSAC and the general basis
18 on which that range is specified as at least the initial test for cost orientation is that it is
19 desirable. Whether there are further considerations to the case you might need to look at but,
20 yes, in general that is true.

21 Q That would be good because that is leaving it to the market to send signals and all I am
22 putting to you is those are pretty strong signals?

23 A I am sorry, in general that would be desirable. I am not sure what you meant by "pretty
24 strong signals".

25 Q If you set connections at 4 and rentals at 10, or vice versa, that is a pretty strong signal to the
26 market one way or the other, is it not?

27 A I am still not sure ----

28 THE PRESIDENT: Strong signal in what sense?

29 MR. THOMPSON: In the sense that Mr. Myers' view is of economically significant signals.

30 A So, yes, if those separate prices are economically meaningful then, yes, those ----

31 Q But if BT goes one way or the other ----

32 A -- those two sets of prices would be sending different signals. If there was a reasonable
33 basis for those then that could be efficient. It kind of depends a bit on the circumstances.

34 Q All I am saying is that in the FAC/DSAC part of the forest you think that is a good thing,

1 because that is the point you make in response to Mr. Pickford's clients.

2 A Yes.

3 Q So I am now saying why, in the cost orientation part of the wood, do you say that that is a
4 bad thing?

5 A I do not say it is a bad thing. I am really failing to understand your point. Perhaps I have
6 missed your point, because the same range between DLRIC and DSAC would apply under
7 separate assessment and, of course, I think you will have seen from my witness statement, I
8 do not say that separate assessment is definitively the right way. I actually say from an
9 economic point of view there are arguments either side, either for separate assessment or
10 aggregation. But on the basis of separate assessment, there is a similar flexibility between
11 DLRIC and DSAC.

12 PROFESSOR MAYER: Is your point, just so I understand it, that in the example being given in
13 neither case are the connections or the rentals violating DSAC so that, as far as you are
14 concerned, you believe that flexibility is desirable?

15 A In general, yes. In general. As I say, there may be additional considerations in a specific
16 case but in general that would be the case.

17 MR. THOMPSON: Can we move onto the specific issue of connections and rentals? You may
18 recall that I put it to you at the start that there will be three issues: Issues of scope, issues of
19 compliance and issues of repayment. BT relies on the issue of connections and rentals of
20 each of those three levels. Do you understand?

21 A Yes.

22 Q Would you accept that there is ample evidence that the CPs are sophisticated buyers whose
23 purchasing decisions are based, first of all, on their own or their retail customers' needs and,
24 in particular, their duration of their circuits and, secondly, on the whole life costing or NPV
25 assessment, on the relative merits of sole supply or purchase from one person or another.
26 That is quite a long question but you understand what I am getting at? That they look first
27 of all at what they need, so if they are a BES provider they look at that project; if they are a
28 WES provider they look at the needs of their customer, and they look at what is being
29 offered over the relevant period. So if it is a three year back-to-back deal with their
30 customer they look over three years. You would accept that?

31 A Yes.

32 Q As we have seen, BES and WES contracts are rolling contracts, are they not? They are
33 taken out and they go on until somebody terminates it?

34 A Yes.

1 Q Would you accept that the typical life of a WES/BES circuit is well over a year? In 2009
2 you clearly thought three years was the average.

3 A Just to clarify, Ofcom used a three year figure in the 2009? I was not involved in that
4 Review. But, yes, from the evidence I have seen the typical duration of circuit is longer
5 than one year.

6 Q Yes, and in those circumstances the minimum term is likely to be irrelevant to most CPs
7 most of the time. Would you accept that?

8 A I can see that it may not be of the utmost importance but it obviously goes slightly to a
9 question of flexibility for the CP; how important that is, in other words, by which I mean
10 that whilst I think you pointed out to me earlier that a CP could still terminate a contract
11 within the one year minimum, but there would be some termination charges or something to
12 be paid.

13 Q I think what would happen is that the CP would have to pay the rental charge as if they had
14 kept it for a year.

15 A I see. So even if the CP expected the circuit to last for significantly longer than one year,
16 the fact that there is effectively this one year minimum term is still relevant. How important
17 it is, I think the CPs would be in a much better position to judge.

18 Q Can I look at 293a of your statement, Mr. Myers?

19 A Yes.

20 Q You say:

21 "Whilst the two charges are only ever useful if they are bought in combination in the
22 initial minimum contract period (typically the first year that a circuit is rented), in
23 subsequent periods they are not bought in combination as only the ongoing rental
24 charge is paid and not the one-off, upfront connection charge".

25 I must say I do not really understand that statement because surely you buy the circuit and
26 you use it for however long you use it. It does not make any difference to the first year.

27 A I think it builds on exactly what we have just been discussing in terms of the minimum
28 contract term. When a CP is taking up that contract it is making a commitment to pay the
29 connection charge and to pay the first year rental, either because it retains a circuit for one
30 year or, if it terminates early, it pays the remaining first year rental. So it is making that firm
31 commitment and it cannot get out of that commitment, as I understand it from the way the
32 contracts works. For any subsequent year's rental it may expect to take the circuit beyond
33 that first year but, as I understand it at least, it is not making a contractual commitment to do
34 so. So, for example, it could terminate the contract at the one year point without any

1 penalty payments, even if that was not what its initial expectation was. So I think there is a
2 distinction between the minimum contract term and the rest of the life of the circuit.

3 Q That is not really right, is it, because you just take out the contract and it lasts until it stops.
4 There is no magic about a year. If you stop after a month, it stops; if you stop after five
5 years, it stops after five years.

6 A I think there is a distinction which is when you take out that contract you are committed to
7 paying the connection charge and the first year rental. That is the distinction between the
8 first year rental and the subsequent year rental.

9 Q At 293d you say:

10 "... the first Harman report does not provide the evidence to answer the points raised
11 by Ofcom...".

12 And then:

13 "No evidence has been provided that customers of WES/BES services have a
14 preference for a balance of prices involving the rental charge above DSAC, or that a
15 price above DSAC at the wholesale level for the WES/BES services is necessary to
16 achieve the benefit that is suggested".

17 I think you were present when Mr. Harman gave his evidence, and he gave really emphatic
18 evidence that, all things being equal, the CPs would prefer low connections on the basis, as I
19 understood it, that BT would then have to fund the upfront expenditure. Would you accept
20 that in general terms, that, from the point of view of a CP, a low connection charge is a good
21 thing because BT bears the capital cost, if one puts it crudely?

22 A So it changes the nature of the risk for the CP because, agreeing with you, the initial charges
23 the CP is paying, that it is committed to pay, are lower and so perhaps it increases its
24 flexibility, so I can see that that is one of the effects. I am not really sure that I have seen
25 evidence from the CPs about what they prefer and I could see that different CPs might be in
26 different positions. So I think I understand the consideration you are talking about. Whether
27 that applies overriding any other considerations and applies to all CPs, I am not really sure I
28 have seen any evidence on that.

29 PROFESSOR MAYER: Could I just ask on that, Mr. Harman's point, as I understood is, was
30 mainly that if more of the weight is placed on the rentals than connections you reduce the
31 present value of the charges by deferring some of the charges into the future. Do you think
32 that that is a justified case?

33 A As far as I understand it, I think that depends on what particular form of aggregation is
34 being used. If there is aggregation across the life of each circuit, and that aggregation was

1 done without discounting or without taking account of the costs of capital – and I think Mr.
2 Holt's point seems to stand in terms that it would be at the lower NPV, but there are other
3 types of aggregation being put forward and I haven't worked through whether the point
4 would still stand in those. It is not obvious to me that it would, although that may be the
5 case. So, going back to your point about if the NPV is lower would the CPs prefer that? I
6 can see that again it clearly has an advantage for a CP, but the balance of prices may also
7 matter to the CP, depending on the nature of the decision they are making, what their
8 alternatives are in terms of self-provision for example, or the nature of the relationship of
9 the products they are providing to the retail customer. So again, it seems to be a relevant
10 consideration under some circumstances, but there may be other factors as well.

11 MR. THOMPSON: Two examples. If a CP's cost of capital was higher than BT's, then
12 presumably it would prefer BT to bear the capital costs?

13 A I am sorry, I am just reflecting on it. (Pause) Yes, that sounds right to me.

14 Q Likewise, if the CP was capital constrained for some reason because it was expanding
15 rapidly, then it would be good if BT bore the upfront costs and the CP simply paid the rental
16 over a period when hopefully its business would be thriving?

17 A Yes, again that does sound like a set of circumstances where the CP might prefer that, yes.

18 Q Can I ask you about something else, which is 299b, again it is about the minimum rental
19 period, about half way down you say:

20 "Therefore, beyond the minimum rental period the CP may make a series of
21 decisions over time whether to continue renting the circuit from BT or to cease it
22 and put in place alternative arrangements."

23 What do you mean by alternative arrangements?

24 A So I think what I meant was either, for example, self-supply, or obtaining similar wholesale
25 services from another CP, or perhaps finding an alternative way of providing the circuit,
26 perhaps using wireless technology or just a different technology entirely.

27 Q Yes, and presumably each of those would involve the same equation we were talking about
28 at the beginning, upfront costs and then an ongoing cost. Is that not right?

29 A May do. I mean, there may be exceptions to that, but I can see some of those situations
30 would involve that. There are circumstances where the balance between the up front and
31 the on-going would be of importance and make a difference in terms of the economic price
32 signals.

33 Q Can you think of any circumstance in which if you were going to change from BT you
34 would not either have to bear the costs of building the circuit yourself, or the connection

1 charge levied by whoever else – Virgin or someone?

2 A So that, then, depends on the level of the connection charge that Virgin levies, for example.

3 Q Exactly.

4 A Maybe they would not levy a connection charge; maybe they would.

5 Q Yes. You say then that BT's current rental price is the relevant price signal. I am just
6 asking if that is right.

7 A There are two sides of the equation. There is the on-going costs if the CP chooses to remain
8 renting the circuit from BT, and that is going to be compared against the cost of the
9 alternative. In terms of the cost for continuing to rent from BT, it is simply BT's rental price
10 that would be relevant, not the connection charge that was paid in the past. So for the BT
11 cost side of that equation, as it were, the costs paid to BT, the charges to BT, it is just the
12 rental price that would be relevant. That is the point I was making.

13 Q Yes, but as an economist is that the right approach? Imagine you are talking about new
14 house prices or new car prices. Do you discount stamp duty, or depreciation in the first year
15 for people who have already got a house or already got a car? Surely the pricing is the new
16 entity, is it not?

17 A The relevant price signal is the relative prices of the price for continuing in this case the
18 circuit or whatever the product is versus the price of moving to an alternative. To send the
19 right price signals for that you would only want to include in this the BT rental price at a
20 price that reflected cost. So you are comparing two prices. For the BT price side of that
21 you would only want to include the rental price, because the connection charge is not
22 relevant.

23 Q Still, when you are looking at your competitive options: like, I have a house and I am
24 thinking about buying another house, obviously there would be a cost involved in that, but
25 you would still look at the price of the other house, do you not?

26 A I am agreeing with you for the cost of a new house; you want to include all the costs that
27 you incur for the new house. But if you are making a decision whether to move, in terms of
28 the cost of your existing house, you would only want to look at the forward looking costs,
29 the costs that you would continue to incur. So you wouldn't take account of costs that you
30 had incurred in the past but you wouldn't expect to incur in the future for the purpose of that
31 comparison.

32 Q Yes, but if you are thinking of your alternative arrangements, then obviously you would
33 think about the costs of those alternative arrangements, just the same as if you were thinking
34 about the new house, you would think about the cost of that house, would you not?

1 A As I say, there are two prices that you would be comparing: the price of the new house and
2 upfront costs you would need to incur for the new house (or the new circuit or circuit from
3 an alternative supplier). Yes, you would take account of those. But for the existing house
4 or circuit you would only want to take account of the ongoing costs/prices which, for a
5 circuit would only be the BT rental.

6 Q If you are considering changing, then the alternatives are relevant. If you are just trundling
7 along then you are still under the same regime you were at when you bought the thing in the
8 first place?

9 THE PRESIDENT: Mr. Myers is saying considering changing, he is agreeing with you that the
10 billed out charge of the alternative is relevant, but what you are doing is making a
11 comparison and the other side of the comparison (or equation, as he put it) will be only the
12 BT rental and you will not be interested then in the BT connection charge you paid one or
13 two years before. That is what he is explaining.

14 MR. THOMPSON: I had hoped to finish connections and rentals by lunchtime. I think I will not
15 quite make it unless we sit a little bit late. We got a slightly late start.

16 THE PRESIDENT: How much more?

17 MR. THOMPSON: I have probably got another ten or 15 minutes.

18 THE PRESIDENT: I think it is better we come back at 2 o'clock.

19 MR. THOMPSON: I should say I have also got something on repayments. I hope I will not take
20 too long.

21 THE PRESIDENT: Yes, as long as, with Mr. Read, you finish by 4. We will return at 2 o'clock.
22 Mr. Myers, I think you know well, but I should remind you, you cannot discuss the case,
23 your evidence with anybody. The weather, nothing else.

24 Adjourned for a short time

25 THE PRESIDENT: Yes, Mr. Thompson?

26 MR. THOMPSON: Mr. Myers, we were in mid-flow with the topic of connections and rentals.
27 Could I ask you to turn to para. 301? As I understand it, you are considering that
28 aggregation of connections and rentals could lead to a false negative which you describe
29 twice in the sixth line as a "wrong conclusion". Do you see that?

30 A Yes.

31 Q What I want to ask you, is there anything wrong with that approach to compliance? For
32 example, if we took the approach that was adopted in the 2009 leased lines charge control,
33 are you saying that that would lead to the wrong conclusion?

34 A Sorry, the approach in the 2009 calculation of the starting charge adjustments?

1 Q Yes, so you are taking the connection charge and aggregating it over three years?

2 A So I am commenting simply on the economic issues, and the point I am making here is that
3 there is potential for that approach to lead to economic distortions, both in terms of the
4 initial purchase decisions and subsequent decisions, the rental charge, or the balance
5 between connection and rental charge as the case may be, may affect those decisions and
6 where those individual prices are not cost orientated, that can cause economic distortions.

7 Q Yes, you are going a bit further than that, you are saying it is a wrong conclusion?

8 A No, sorry, that is simply a definition of a false negative. The false negative would be a
9 wrong conclusion.

10 Q If we take a simple example. You remember Mr. Harman's DSAC at 10, a connection rental
11 at 10, DSAC at 10 for rental, so both at 10,10, and connection set at 7, and rental set at 11,
12 11, 11. You imagine somebody who buys on the basis of 7, 11, 11, 11 and retains the circuit
13 for three years. They thought it would cost 40 and it did cost $40 - 7$ plus 3×11 or 4×10 ,
14 both cost 40. So are you saying that somehow it would be a wrong conclusion that that
15 person got what they paid for?

16 A Yes, well, I am saying that could result in an economic distortion and that arises because the
17 rental charge is above the DSAC, and what that means is in the initial purchase - taking just
18 to start with the initial purchase decision - that means that longer duration circuits are priced
19 too high, relative to those costs. Therefore, that could lead to the wrong decision. So, in
20 other words, the very initial decision by the CP to purchase a circuit on the expectation that
21 it would take it for three years might be a distorted decision, or there might, as it were, be
22 other CPs who would have taken a circuit for three years but did not do so because of those
23 prices.

24 Q It might be a good thing because of desirable pricing flexibility, but ----

25 A But in terms of whether these DLRICs and DSACs are well-founded, that goes beyond the
26 flexibility and it raises the risk of those individual prices which are economically
27 meaningful in their own right to some extent. It means that economic distortions can arise
28 from that. I mean I understand there are ----

29 Q But I know I have fixed the figures, but on this ----

30 A Taking your figures I would say there is scope for economic distortions on those figures,
31 and the reason is - I think it is probably worth just elaborating this point - the question of
32 whole life costing for me actually is not really the deciding issue in terms of aggregation or
33 disaggregation, and perhaps I should just explain why. We can clearly think of examples in
34 other cases of other purchase decisions CPs would make, where they would do whole life

1 costing of services together which clearly should not be aggregated for the purpose of cost
2 orientation. Perhaps a simple example of that would be, in the *PPCs* case, trunk and
3 terminating segments. If a CP was considering purchasing a PPC with a trunk segment as
4 well as a terminating segment, I would expect it to engage in whole life costing across that.
5 That is a relevant consideration when one thinks about the nature of the decision but it does
6 not of itself, mean that there is not scope for economic distortions because there is the
7 potential for the circuit to be bought without the trunk segment in that case, that individual
8 price is economically meaningful.

9 The case here is different from that and it is essentially the reason why my view is actually
10 there is merit on the arguments on both sides of this debate, and it is essentially because
11 connections and rentals has an element of fixed proportions, this minimum contract duration
12 - the first year rental and the connection - but it also has the element of variable proportions
13 both in terms of the initial decision, duration of the circuit and subsequent decisions, and it
14 is the fact that it contains both elements of fixed and varied proportions which actually, in
15 my view, means that there are arguments either side of this debate in terms of the nature of
16 the potential for economic distortions.

17 Q Yes, thank you. The *PPCs* example you gave is an interesting one, it goes back to the issues
18 we were talking about at the beginning, because the example you give is where, as indeed
19 the passage we looked at in *PPC* shows, and Ofcom had looked at this market and had
20 defined separate markets, and it was for that reason that it was wrong to look across the two
21 markets. That is what was happening in *PPC*, was it not?

22 A Well, that was one of several reasons, actually from the economic point of view that
23 different market definition is perhaps a reflection of the characteristic I am talking about but
24 there is a different point. I think it would be wrong to say that it is the market definition
25 itself that means that. If we take, for example, services in the Ethernet market, we have
26 mainlink as well as the connection and the rental. Again, I would expect CPs to engage in
27 whole life costing across that. But, in my view, economically, even though they are all
28 within the same economic market it would be wrong to aggregate mainlink because it
29 essentially does not have this fixed proportion element, it is variable proportions. The CP
30 can decide to purchase a circuit with or without mainlink, and that seems to me clearly
31 suggesting that separate price of mainlink is economically meaningful and therefore it
32 should not be aggregated.

33 Q Just going back to my example, I think you would accept that on Ofcom's approach in 2009
34 they would have accepted that the CP had paid 40 and it had cost 40 and everything was

1 fine because they would have averaged the connection over the three years?

2 A Yes, I think that's right, if Ofcom in that case looks at it over a three year period.

3 Q Whereas you are saying now that was wrong and that it was right for a CP in that situation
4 to recover 3 because he had overpaid 1 for his rental for three years. He bought on the basis
5 it would be three years, it had been three years, he bought on the basis it was 40, he paid 40.
6 You say that was wrong and he should get three back, is that right?

7 A I don't definitively say it was wrong because, as I have set out, I think, in my witness
8 statement I recognise there is merit on both sides of this argument, and it seems to me to
9 turn on the evidence of which of the distortions that would be caused either by separate
10 assessment, or caused potentially by aggregated assessment, which of those is greater. So I
11 don't take a definitive view that it is definitively wrong, but I do say it is potentially wrong
12 for the purpose of cost orientation because the rental price is individually economically
13 meaningful in a set of circumstances, and that still applies whether or not there is whole life
14 costing going on.

15 Q We can get dazzled by the numbers, but I will give you one more example. Suppose
16 somebody had bought for two years, they had expected to pay 29, 7 plus two 11s, but it
17 turns out that DSAC is 30, 3 x10s, so they have actually paid less than they expected. On
18 Ofcom's view they would still get two back?

19 A Sorry, can I clarify? So that the two year circuits, 7 is the connection charge?

20 Q Yes.

21 A And the 11 is the rental charge in each of the two years?

22 Q Yes.

23 A And, sorry, the DSACs are?

24 Q Still 10?

25 A Still 10, right. Yes, that is overpricing rentals because it is pricing the rental in excess of the
26 DSAC of rental. Perhaps there is a slightly more profound point here about the nature, the
27 derivation of the DSAC test. The DSAC test, as we know, is a pragmatic alternative to
28 combinatorial testing, and it is designed to be a test that applies at the level of individual
29 services. That is the nature of the rationale for the DSAC test. Therefore, if we are
30 considering services which are separately economically meaningful, and as I think I have
31 said, connections and rentals is a bit of a mixed case but taking the case where they are
32 considered separately economically meaningful, it would actually be inappropriate given the
33 nature of the DSAC test to try and offset a price below DSAC on one service, against a
34 price above DSAC on another service. That seems to me to conflict with the nature of the

1 derivation of DSAC and its rationale which, as I say, is all about trying to derive a test
2 which applies at the level of individual services without the need to apply combinatorial
3 tests.

4 Q You say when you come to think about whether these characters should get more money
5 they have bought on the basis of it costing 29, it did cost 29 but when you look behind the
6 costs it should have cost 30, and you say that as a matter of discretion they should get two
7 back?

8 A I don't say it should have cost 30, because that assumes it's correct, or appropriate for BT to
9 price every service up to DSAC. That does not seem to be right. It has the flexibility to do
10 so but it does not have the obligation or the requirement to do so. I think it goes back to the
11 points we have just been discussing, which is that my point is that the initial set of price
12 signals, which the CP face, for its initial purchase decision, were distorted price signals,
13 because the rental price was above the DSAC. It does not seem to me that the fact the CP
14 engages in whole life costing corrects that distortion. It is a decision that the CP makes in
15 the face of that distortion, but it does not remove the distortion.

16 Q You say, quite positively, that there were these distortions, can I just be clear about what
17 you do or do not say. For example, at 324, the first sentence: "Ofcom did not engage in
18 such balancing of economic effects in the Determinations" and if you then turn back to the
19 end of 293, p.108 you say this:

20 "Given that there are arguments in both directions and there is an absence of clear
21 evidence on the empirical relevance or relative importance of the potential
22 distortions, it is a matter of judgment which approach would give rise to a greater
23 risk of economic harm to consumers or competition (...) In my view an *a priori*
24 case could reasonably be made to justify a conclusion either in support of the
25 proposed aggregation or separate assessment."

26 You make a lot of evidence-based assessment of other issues, but this seems to be just a
27 straw in the wind. Is there any evidence for your position that you have just set out?

28 A I identify, as some other experts have, the scope, the potential for distortions, for distorted
29 price signals. On evidence, my very point is that I don't think I have the evidence to know
30 how important that distortion is or indeed how important the potential - the potential
31 distortions are from a separate or disaggregated assessment where I also recognise there's
32 the potential for distortions but I haven't seen the evidence to show how important those
33 distortions actually are or were.

34 Q Yes, so that goes back to why you made some emphatic remarks just now and why you say

1 that the aggregation is a wrong conclusion at para.301. There is no evidence for that at all?

2 A My emphatic remarks were in relation to the scope, the potential for distortion. The
3 emphatic remarks were about the nature of the price signals being distorted. That's
4 distortion, that we talked about, of the rental price being above DSAC. My point on
5 evidence is, yes, there was a distorted price signal, but sometimes distorted price signals
6 matter a lot and sometimes they don't matter very much, depending on more specific
7 circumstances, and it is that on which I say I haven't seen clear evidence.

8 Q You do not know which?

9 A Yes, that's right.

10 Q At paras.294 and 295, pp.108-109, you deal with Mr. Harman's comments on cost
11 allocation, and at 295 you in particular look at the position in relation to the first Harman
12 report. Then you say this:

13 "For simplicity, I abstract from such detail and any associated practical
14 implementation issues. If it were decided that connection and rental charges
15 should be aggregated, the appropriate approach to implement aggregation might
16 depend on the specific rationale that was considered most important as well as
17 practical issues about the available data."

18 I did not find that a particularly clear statement, and I wondered what you meant by that.

19 A As I recall - this isn't something that I have looked at in any great detail, I have to say - the
20 first Harman report discusses three different approaches to aggregation and, as I understand
21 it, there's been a fourth one commented on in a subsequent report by Mr. Harman, which is
22 about aggregation within the minimum contract period. As I understand it, there are four,
23 and there may be others but there seem to be at least different approaches to aggregation on
24 the table. I have not particularly focused on the differing characteristics of those, which
25 would be more appropriate, and given that there would be a choice that would need to be
26 made between those four, I think my point, depending on the specific rationale, is that if it
27 was concluded that the appropriate approach was to aggregate connections and rentals there
28 would be some reasons on which weight was placed in order to reach that conclusion. I
29 don't necessarily have anything particularly specific in mind, but I could see that that might
30 guide you or imply that one of the four methods of aggregation was more appropriate than
31 the others.

32 Q Thank you. You will recall that there is this issue about the electronics costs and whether
33 90 per cent of the costs could go across from connections to rentals. So far as I understand
34 it, you have basically accepted that, in principle, that is correct. You will recall Ofcom

1 allowing BT to transfer the electronics costs across in one of the later years?

2 A Yes, I agree that there is a legitimate - in terms of these allocation decisions for BT to make,
3 there is a legitimate choice about whether to allocate these electronics costs to connections
4 or to rentals.

5 Q That is not merely some issue about allocation of fixed or common costs, that is a real
6 uncertainty about LRIC or DLRIC for connections as against rentals. It is the actual
7 difference between the underlying costs, is it not?

8 A But it's not an uncertainty for BT, which seems to be the person in point, because it's BT
9 that is choosing these cost allocations. It is choosing them for the purpose of deriving
10 DSACs. My understanding of the way the regime operates is that the DSACs are to be
11 used, and BT understands they're to be used, for the purpose of assessing cost orientation.
12 So, in fact, the party that shouldn't have uncertainty about this question of whether
13 electronics is allocated to connections or rentals is BT, because they're the one that make the
14 choice, and as long as they avoid an error or an obviously inappropriate methodology - and I
15 think we have just discussed that I don't think and Ofcom didn't take the view that it was
16 obviously inappropriate whether you allocated those to connections or rentals - then that's a
17 decision within BT's control to decide where they should allocate that cost for the purpose
18 of the DSAC and cost orientation.

19 Q Yes, but if we just go back to our 10, 10, 10 example, it presumably follows that the
20 connection DSAC could be 1 or it could be 10, if 90 per cent could shift across?

21 A It could be, and that would be BT's choice in the first instance.

22 Q And the rental could be 10 or it could be 13, or indeed the rental could be 1 and the
23 connection could be 37, if the figures are that flexible?

24 A I don't think the figures are that flexible. We've talked about 90 per cent, but my
25 understanding of that 90 per cent is that if electronics costs when they were allocated to
26 connections, 90 per cent of the connection cost was the cost of the electronics or
27 thereabouts. There are some costs, it seems to me, which contribute to rental which should
28 not be recovered through connection charges. I don't think that it's infinitely flexible, but I
29 do agree from my understanding of the nature of these costs that BT has very substantial
30 flexibility making legitimate costs allocation decisions about how they allocate costs
31 between connections and rentals, and electronics is a clear example of that.

32 PROFESSOR MAYER: Can I just ask a question at this stage in regard to that. On p.99 in
33 para.285(b), you do say:

34 "Connection and rental charges have different costs associated with them ..."

1 and you in particular refer to duct and fibre as being components that cannot be simply
2 reallocated between the two. Do you have any sense as to the proportion of costs that
3 would fall into that category of being clearly identified with either connection or rental?

4 A Yes, those costs - just to clarify, these costs of duct and fibre I think are more clearly
5 identified with rentals. I'm not sure I had a specific figure in mind, but my understanding is
6 that duct and fibre costs are a substantial proportion of the costs of these circuits.

7 MR. THOMPSON: I was, in fact, going to take you to 285(b), because I think certainly one of
8 the issues that Ofcom raises is a need for certainty under the RFS, and I think that is part of
9 what you were talking about just now, that BT should not be allowed to take a different
10 approach for the purposes of the RFS and for the purposes of compliance. I think that is the
11 point that is being made, that that should not be allowed?

12 A Well, I think that would, as it were, be a starting position, but I think, applying the
13 framework - it seems to me that effectively what's being suggested is an adjustment to the
14 RFS. So there is a framework for considering whether adjustments to the RFS are
15 appropriate, about whether there is an error or an inappropriate methodology. I haven't
16 exhaustively considered this issue as to whether an adjustment along these lines would be
17 appropriate, but, on the face of it, whether this cost is allocated to connections or rentals,
18 either of those decisions is reasonable and therefore neither would be obviously
19 inappropriate.

20 Q I was going to ask actually the simpler point, which is that the approach, for example, that
21 Ofcom took in 2009 does not involve any tinkering around with the RFS, does it? It is
22 simply aggregating the connection and the rental charges over three years. That is not
23 tinkering around with the RFS, that is just a calculation, is it not?

24 A Tinkering around with RFS - in 2009, I'm not sure exactly what data Ofcom used and
25 whether that involved any adjustments from the RFS, but to the extent the connection figure
26 was from the RFS and the rental figure was from the RFS, yes, they just aggregated those
27 two over considering a three year circuit. My observation on Ofcom's approach is for the
28 purpose of the connection and rental issue, as regards the aggregation or separate
29 assessment issue, it is not tinkering with the RFS either. There's an RFS figure for
30 connection and there's an RFS figure for rental and, subject to other potential costs
31 adjustments, Ofcom has taken those figures.

32 Q Yes, so you are just adding up two numbers in different ways. It is not changing the RFS?

33 A Yes, neither approach is changing the RFS. Sorry, perhaps I could just clarify. Neither
34 approach is changing the numbers in the RFS, but it depends on the effect of the

1 aggregation, it's changing the nature of the test. The points I made earlier about if it's
2 considered appropriate, if the aggregate system is right then that is entirely reasonable, there
3 is no problem with that. However, if separate assessment is appropriate, disaggregated
4 assessment, then there is a problem, the points I made before about offsetting a price below
5 DSAC on one service against above DSAC on another service which, under separate
6 assessment, would not be appropriate.

7 Q Can I now just turn briefly to the issue of repayments. I think you accepted at the beginning
8 of our discussions that the question of whether BT is charged above DSAC and whether it is
9 compliant is a different question from whether BT should be required to pay money to one
10 or more of these CPs. You accepted those are distinct questions?

11 A I understand that those are distinct questions, yes.

12 Q The latter one is a discretionary decision taken in December 2012 taking account of a range
13 of factors - that is correct, is it not?

14 A Yes.

15 Q I think one of them, which I think is the one you put at the front, is the impact on the
16 compliance incentives of BT to make such a payment?

17 A Could you tell me where this is in my witness statement? I'm sure I could find it, but ----

18 Q Your discussion of repayments is actually quite short. It is at paras.236-241, it is the end of
19 the discussion with Dr. Maldoom?

20 A Yes, I have that.

21 Q You identify a wider range of factors. I put to you, first of all, the compliance incentives of
22 BT. Secondly, there could be issues about the incentives of the CPs to bring or possibly
23 delay disputes. That could be a possible factor you might take into account?

24 A Yes, I agree that's a possible factor.

25 Q Adverse effects on the regulatory regime, if you either gave money to people who had not
26 suffered any loss or if you used dispute resolution to reopen past transactions which would
27 be contrary to the principle of legal certainty, would it not?

28 A Well, I don't think I'm in a position to comment in relation to legal certainty, but taking at
29 least the first part of your proposition, if there are other factors which were decided had an
30 adverse effect on the regulatory regime, then I agree that would be relevant. I don't
31 particularly comment on the specific propositions of such effects that you put forward.

32 Q If we look at 81(b) on p.36, this is in a different context, but you do say:

33 "Retrospectively clawing back those profits therefore not only undermines future
34 efficiency incentives in the market where the claw back is employed, but may also

1 have a broader effect across other markets where similar price cap mechanisms are
2 employed."

3 So you do take into account these sort of effects in deciding what to do or not to do?

4 A Yes, I believe I accepted that in my previous answer. This is a specific example relating
5 specifically to price caps, but there is a wider principle that can apply in other
6 circumstances.

7 Q You were involved in *PPCs* and I do not know whether you were involved in the
8 assessment of repayments in that case, but you may recall that initially it was said it was to
9 be a hard discretion or an all or nothing discretion. Do you recall that issue?

10 A Yes, I was not involved in that part of the analysis but I do recall that point.

11 Q Can we now look at CB-E Tab 9 and then Tab 11?

12 A Tab 9, did you say?

13 Q Yes.

14 A And, I am sorry, what page or paragraph?

15 Q Towards the end. It is paras.336 and following, and, in particular, 338.1:

16 "Such discretion as Ofcom has under section 192(d) is a hard discretion confined to
17 requiring Ofcom to follow through on the conclusions it has drawn pursuant to the
18 dispute resolution process".

19 Do you see that?

20 A Yes.

21 Q That is the position that Ofcom took in the Court of Appeal, and one finds that at Tab 11. If
22 you turn to p.19 and para.83, and you will see it says:

23 "It is common ground Ofcom has a discretion in the exercise of its powers under
24 s.190. I do not accept Mr Saini's submission that the discretion is an 'all or nothing'
25 discretion... [which I think is the same as the hard discretion]: that is to say, in the
26 case of excessive charging, either Ofcom must order repayment of the entire
27 overpayment or it must decline to make any order for repayment. The statutory
28 language does not expressly or impliedly require so extreme and inflexible a
29 position".

30 If you turn back to the beginning of the clip, you will see that this was 27th July 2012. Do
31 you see that?

32 A Yes.

33 Q So the question is, when you issued the provisional conclusions and in the work up to 27th
34 July 2012, am I right to assume that you were looking at this as an all or nothing matter, that

1 you were not really looking at the discretionary factors?

2 A I am afraid I do not precisely recall and, as I say, I would not have been centrally involved
3 in that aspect of the repayments. So my role would have been, where there were economic
4 issues that arose in terms of the appropriate legal tests that were decided, then I would have
5 been commenting on those. I am afraid in relation to your specific question, I do not recall.

6 Q You do not recall whether you were asked to do any work on the economics of repayments?

7 A At the provisional conclusion stage?

8 Q Before July 2012.

9 A I am afraid I do not have a precise recollection of whether I did or did not.

10 Q You may recall that I had some discussion with Dr. Houpis about this, about the overall
11 nature of the economic and regulatory incentives for Ofcom. Do you remember that?

12 A Yes.

13 Q Would you accept that the most direct compliance incentive of Condition HH3.1 would be
14 enforcement action by Ofcom during the period when the Condition is in force, so between
15 2004 and 2008 in relation to the first Condition?

16 A When you say "most direct", perhaps you could just explain what that means?

17 Q It might help you to look at the cases on which it was imposed. That is at BT3 p.94. If you
18 start at p.89, you will see that Chapter 4 is called "Approach to regulatory remedies", and
19 this is the LLMR 2004. Then at 94 it says: "Need for remedies to be incentive compatible".
20 Do you see that?

21 A I am sorry, which paragraph is that?

22 Q 4.37 and 4.38. It says:

23 "The fourth principle requires remedies should be designed, where possible, so that
24 the advantages to the dominant communications provider complying with them
25 outweigh the benefits of evasion".

26 Then you go on:

27 "The remedies imposed by Ofcom clearly give incentives on dominant
28 communications providers to comply with them. Failure to comply with the
29 conditions in Annex D or the Directions in Annex E could result in the offending
30 communications provider facing fines under the Communications Act".

31 That is the incentive you identified when you set the condition in 2004. Do you see that?

32 A Yes, I see that.

33 Q I think you are aware, and it is a point I put to Dr. Houpis, that BT also faces compliance
34 incentives under the Enterprise Act, the Competition Act, both from public enforcement and

1 civil enforcement?

2 A Yes, I am aware of those points at a high level. I do not have any detailed understanding of
3 them but, yes, I am aware of them at a high level.

4 Q Why did Ofcom not mention any of those factors in the Decision?

5 A Those would not have been areas within my responsibility because they would have been
6 questions of legal interpretation or which parts of the regime were most relevant, rather than
7 a question of economic analysis.

8 THE PRESIDENT: I think what is being put to you is that if the relevant factors to the Decision
9 are incentives on BT to comply and, indeed, accepted incentives for CPs to bring or delay
10 complaints, if one then thinks, "What are the incentives on BT?", there is the legal regime
11 which you are advised on by others, but then the incentive effect is partly an economic
12 consideration, is it not?

13 A Yes, I agree with that and my understanding is, on the disputes, there is no financial penalty
14 faced by BT whereas what is being suggested here is under enforcement there is the
15 potential for financial penalties, I think, if that is right. If that is correct? By which I mean
16 going beyond just repayment of the overcharge, an additional amount. So those would have
17 different incentive effects if they were implemented. I agree with that.

18 MR. THOMPSON: Yes, and that they have been enforced between 2004 and 2008 and I think
19 you will accept that there are penalties up to 10% of turnover, so they are not insignificant
20 penalties. So those were the incentives that have been identified by Ofcom itself when the
21 condition was imposed. I am just asking why you did not mention that in assessing the
22 economic incentives for complying for BT.

23 A I think whilst there may be different economic implications of these different legal routes, I
24 do not have any expertise on how they fit together; when it would be more appropriate to
25 use one rather than the other. I could see that economic issues might come into that in terms
26 of some of these incentive effects. I do not recall having any discussion along those lines,
27 but beyond that I do not think I am really in a position to comment any further.

28 Q We have looked at the position over the period of years, including the response to the THUS
29 complaint when BT gave Ofcom very considerable information about its pricing and Ofcom
30 closed the file and then repealed the condition. Why was none of that taken into account in
31 relation to repayments? Why did you ignore Ofcom's own role in this?

32 A As I recall, that is commented on in the Decision. That is not a part of the Decision that I
33 had a key role in so I am not sure I am in a position to elaborate beyond what is in the
34 Decision.

1 Q Can we now look at 15.63?
2 A Of the 2004 ----
3 Q Of the Determination itself. You make a great deal in your statement of Ofcom taking an
4 evidence-based approach generally.
5 A Yes, I think that was -- Yes, I do not dispute that although I think most of that was in the
6 context of the compliance question but, yes, I did.
7 Q That is the point I was going to come to. When it comes to the separate question of
8 repayment, all we find is these four sub-paragraphs which do not really contain any
9 evidence or reasoning at all. I accept there is some cross-referring but there is no separate
10 analysis at all, is there?
11 A By "separate analysis", if you mean were some of these issues considered differently for the
12 purpose of repayment than compliance then my reading of these paragraphs is that they
13 were not considered differently. I need to understand why it was thought they should be
14 considered differently for the purpose of repayments compared to compliance.
15 Q You have accepted it is a completely different question. The ----
16 A But that does not -- I am sorry, I interrupted you.
17 Q The repayment question is a discretionary question for Ofcom in December 2012. The
18 compliance question is looking back in time about what BT knew or should have known in
19 2006, and they are completely different questions.
20 A I accept they are distinct questions. I am not sure that makes them totally different, in other
21 words that some factors relevant to one may be relevant to the other, but I agree they are
22 distinct questions. My point was in relation to these specific considerations, I was not clear
23 how these should be considered differently for the purpose of repayments compared to
24 compliance. I accept the possibility, because they are distinct questions, that there might be
25 such an argument. I am not aware of those arguments of how these things should be
26 considered differently. If you put to me a reason why they should be considered differently
27 I may be able to comment on it.
28 Q Then finally in relation to 15.63.4:
29 "We consider that in this case, where we have found that BT has overcharged in
30 breach of an SMP condition, it is appropriate to require the repayment of the amount
31 of the overcharge, even if the disputing CPs may have passed on that charge to their
32 customers".
33 That is just a completely unreasoned statement, is it not?
34 A Unreasoned?

1 THE PRESIDENT: That is a conclusion effectively, is it not? One has to start at 15.59 and read
2 down to put that question fairly as to how Ofcom reached that conclusion.

3 MR. THOMPSON: If there is any reasoning that supports that then this would be a good moment
4 to identify it, but it appears to be just an unreasoned statement.

5 A Looking at the other paragraphs here, 15.59 seems to be relevant.

6 "We consider that BT should not be left with the benefit of excessive charging in
7 breach of Condition HH3.1".

8 That would seem to be relevant as a reason for the conclusion that is expressed in 15.63.4.

9 Q Does it explain why the money that BT has overcharged should end up with a CP who, for
10 this purpose, must be assumed also to have overcharged? Is there any reason why the CP
11 should have that money rather than BT?

12 A So that seems to me to be a distinct question.

13 Q Yes. I am asking you for the answer.

14 A I was about to give the answer, which is that I agree that this, as set out here – sorry, the
15 reason that BT should not be left with the benefit of excessive charging does not answer the
16 question of whether the CP should receive that money. I agree with that.

17 Q No further questions. I think Mr. Read has some questions for you.

18 Cross-examined by Mr. READ

19 Q Good afternoon, Mr. Myers. I want to concentrate on two areas. Just before the bundles are
20 put away because I suspect one of them I may want to go to straight away. Can I tell you in
21 advance that the areas I want to look at are really the period of 2006/2007 and also Ofcom's
22 approach to the way they have considered the question of overcharging. BT's case
23 obviously is that there is in effect an automated accounting regime that has gone on here.
24 Those are the two areas on which I want to concentrate. I want to start with something I
25 hope we can agree on, which is that I think you accept that there is in essence a time lag
26 involved between firstly when BT notifies its prices, secondly when they come into effect
27 and the charges take place, and thirdly when BT reports at the RFS level. I think we can
28 probably agree upon that. Is that right?

29 A Yes.

30 Q Can I ask you, if you have still got core bundle E up there, to go to tab 12 p.48 in the
31 manuscript bit, p.498 in the original because this is the 2004 Leased Line Market Review. I
32 want you to look at HH5.2. This is the condition that requires BT to give 90 days' notice of
33 any change of charge. You would agree that that is an SMP obligation that BT has to meet.

34 A Sorry, I am just reading it.

1 Q Sorry, I do not want to overly rush you, but I am conscious of the time I have. (Pause to
2 read)

3 A Yes, that's right, it's 90 days, or 28 days depending on --

4 Q If it is a new network access, I agree, but for most of these products they are actually
5 established and therefore if BT wants to change its prices it has to have 90 days' advance
6 notice?

7 A Yes, that's correct.

8 Q We know, because you actually saw it in one of the letters that Ofcom wrote to BT that you
9 were taken to this morning, that in fact Ofcom itself was asking about BT's charges
10 following the 90 day notice period. So it's something that was fairly routinely required, as
11 you would expect if it is an SMP alteration?

12 A Yes, that's right.

13 Q Indeed, we know that there was at least one instance where BT actually tried to lower its
14 prices quicker than the 90 days and objection was taken. I do not know whether you are
15 aware of that?

16 A I do recall that issue, to some degree at least.

17 Q I just want to get the time sequence of this right, because obviously if one is looking at an
18 RFS reporting period of effectively 1st April in one year to 31st March in the next year, it
19 essentially means that the last time that BT can actually change its prices, or notify a change
20 of its prices, to have effect in that RFS accounting year is effectively in December, because
21 if it takes 90 days, by the time you are getting to 1st January, that notification can only take
22 effect after 31st March. You see the time sequence?

23 A Yes. I just want to clarify. I think the point you're making is that if BT notifies a price
24 change in December, that would come into effect 90 days later, which would presumably be
25 during March.

26 Q Yes, during March, but as soon as it gets to the end of December it cannot affect the prices
27 for that RFS accounting period?

28 A Yes, I understand that.

29 Q It means that if BT wants to start changing prices in an RFS accounting year, so in other
30 words from day one of the RFS accounting year, it effectively has to give notification in
31 January in the previous accounting year? It follows, does it not, that if on 1st April I want to
32 change prices as at that date, in order to do it I have to do it in January which means it is in
33 the previous year's accounting year?

34 A Yes. Sorry, I think you're just saying that 90 days before 1st April falls in January?

1 Q Yes.

2 A Yes.

3 Q I am just trying to get the time sequence right. What I now want to do is to really see how
4 this impacts in the chronology of events. You would also, I suspect, accept this but let me
5 put it to you: that BT cannot possibly know what its DSAC figures are likely to be until the
6 end of the RFS accounting year. So in other words, until you reach 31st March BT cannot
7 possibly start doing full calculations of what the DSAC figures are actually going to look
8 like? It follows.

9 A Sorry, it depends what proposition you are putting to me. If you are asking me whether BT
10 knows precisely what the DSAC is for a year, that is in the regulatory financial statements
11 which come out after. If you're asking me whether BT could have any reasonable view on
12 what those DSACs might be, then I think that's a very different question, and I think that
13 would depend on whether the reasons for changes between one year and the next year were
14 foreseeable or not foreseeable. In many cases, changes between years are, to a significant
15 degree at least, foreseeable and in some cases there may be specific reasons why they are
16 not. But as a general proposition I think BT may well be able to form a reasonable view of
17 DSACs from one year to the next.

18 Q Let us just unpick that a bit. Let us take one specific instance. If volumes go radically up
19 towards the end of a year – in other words in the period, let us say, January/February/March
20 of a reporting year – that is going to have a significant effect, is it not, not only on revenues
21 but also on cost allocations, because the cost allocations are based in part on the volumes of
22 sales?

23 A But are you talking about the £million DSAC, or the unit DSAC? As regards the unit
24 DSAC, to the extent that more volume means simply that there is an additional amount of
25 similar unit common cost allocation, then that may not change the unit DSAC very much,
26 but I can see it would change the £million DSAC figure.

27 Q No, it does change the unit DSAC.

28 A I'm not saying it doesn't have any effect, but it seems to me that you would need to look at
29 the sensitivity of the unit DSAC to volumes, and it's less clear to me that the unit DSACs
30 are – I could see they may be affected, but that's an empirical question about the degree of
31 sensitivity.

32 Q I appreciate that you are an economist by background and not necessarily an accountant like
33 Mr. Coulson, but would you accept this: that the way that BT allocates costs in the RFS – in
34 other words, the way that it allocates these big chunks of fixed costs that it has spread across

1 its business – is, to a great degree (not exclusively) dependent upon the volumes in
2 particular product sections? So in other words, if you have a very small number of sales for,
3 let us take an example, BES 1000, it does not suck in a higher proportion of the common
4 costs.

5 A But that is exactly my point. No doubt this is a very simplified and stylised example, but if
6 there is a common cost of 100 and there is volume of 10 of the BES service for example,
7 and a volume of 90 of other services, if you're allocating common costs of one against each
8 of the volumes, then 10 would be attracted to the BES. So the unit element of that common
9 cost would be one. If the volume increased to 20, I guess it would depend perhaps what
10 happened to the other volume. Let me start with the very simplest case which is the other
11 volume actually also goes down by 10, perhaps there is migration from one set of services
12 to the Ethernet circuit, so we are still allocating common costs of one to each unit of
13 volume, so BES is now attracting common costs of 20 but there is volume of 20. So the
14 unit cost is actually unchanged in my admittedly stylised example. So it's because some of
15 these costs follow the volumes that actually mitigates some of the sensitivity of the units
16 cost, but of course there may be other underlying reasons why costs may change.

17 Q You are giving a stylised example there and I may get chance to put to you an actual
18 example in due course. So let us put that question to one side. But you would also agree
19 with this, I suspect, that BT cannot finalise its DSAC calculations until it actually knows
20 what it is that Ofcom is requiring it to report upon in terms of revenues and all the rest of it.
21 You understand that there is a process each year whereby Ofcom consults about the RFS
22 and then issues a statement as to what BT is to do with it?

23 A Yes.

24 Q BT cannot finalise the accounts, can it, until Ofcom has said what it is it wants out of the
25 accounts for that year in its final statement?

26 A I don't understand that. I don't have detailed knowledge of that regime, but I'm not
27 questioning what you say; that may well be true.

28 Q Let me just give you an illustration to put it in context. Can you take bundle DF1. I think
29 we can put away core bundle E now. Have a look at DF1. This is a document that has
30 emanated from Ofcom. Go to tab 8. This is a statement issued by Ofcom in 2007/2008
31 about the explanatory statement and notification on changes to BT's regulatory financial
32 statements. Then if you just look, for example, on p.2 of the actual printed document
33 (which I think is p.4 in), the table.

34 A Yes, I see the table.

1 Q You can see there the type of changes that Ofcom is talking about that BT has to implement
2 in its RFS?

3 A Yes, I see that.

4 Q Again, I do not want to take you into areas if you do not have the expertise on this, but it
5 would be a fair point, would it not, to say that until BT has actually seen what requirement
6 Ofcom is imposing on it, it cannot finalise the RFS accounts?

7 A Yes, I can see that.

8 Q Can I ask you to put that bundle away. I want to explore with you the context of 2006/2007.
9 I think we agreed through the time chronology that I put to you that if BT wanted to start
10 influencing prices between 1st April 2006, when the 2006/2007 accounting period starts, it
11 would have to notify prices, take a decision about prices in January 2006. You would not
12 disagree with that on the time lag.

13 A I think I've got it. Just to confirm. January 2006, 90 days after that is March or April, 1st
14 April which is the start of the 2006/2007 financial year, yes.

15 Q And could you take, please, BT 11 tab 27 - BT's RFS for 2004/2005, do you see that?

16 A Yes.

17 Q Those were published in the latter part of 2005, and when BT first had the opportunity to
18 influence the year 2006/2007, i.e. in January 2006, this is the only information it would
19 have had available to it. You would agree with that?

20 THE PRESIDENT: When you say "the only information it would have had available"?

21 MR. READ: From the RFS, sorry, I should have put the qualification on from the RFS.

22 A Yes, I believe that is right. Is your point simply that there would not have been a later year's
23 RFS available?

24 Q At that stage, yes?

25 A Yes.

26 Q If we go to p.118 we can see the level of reporting that BT was required to report at. On the
27 right hand side you will see the floor, which is the DLRIC floor in the parlance we have
28 been using, and the ceiling is the DSAC ceiling, is it not?

29 A Yes.

30 Q And the single element that it is reported at is short haul data services - do you see that?

31 A Yes, I see that.

32 Q And we know that this is the right market because if we look at the top it has: "Alternative
33 interface symmetric broadband origination". At that stage, and at that level of reporting -
34 and I will come back to the level of reporting in a minute - we can see that BT's pricing fell

1 below the DSAC ceiling, did it not? Because if we look towards the left hand side there is
2 the amount, which is £100 million, and then over on the right hand side the ceiling, £130
3 million. Do you see those figures?

4 A Yes, I see those figures.

5 Q So when BT first start setting prices in January 2006 or could first influence prices in
6 2006/2007 the information in the RFS demonstrated that it was still below the DSAC
7 ceiling?

8 A It demonstrates that in aggregate the revenue was less than the DSAC. It doesn't
9 demonstrate anything either way, at a level below that complete aggregation.

10 Q But this was the level at which Ofcom wanted BT to report at, is it not?

11 A Well, sorry, again, as you may be aware, this is not directly my area of responsibility.
12 Perhaps you could just put the question again?

13 Q Yes, let us explore it a little bit. Could you take vol.BT3? This is the start of the Leased
14 Line Market Review Statement, which in fact continues in another volume, but this is the
15 page we actually need. I wonder if you can go to para. 10.2, which is on p.251 of the
16 statement. So this is being said in the context of the very situation where condition HH3.1
17 has been imposed on BT, and this is what Ofcom is also saying at the same time about cost
18 accounting and accounting separation conditions. So 10.2 making it clear that Ofcom
19 considers it is appropriate to impose cost accounting and accounting separation obligations.
20 10.3:

21 "The processes of cost accounting and accounting separation are complex,
22 covering issues such as cost attribution methodologies, accounting standards, audit,
23 transparency, disaggregation ..." etc

24 Then perhaps if we look over the page at para. 10.10, p.252 Ofcom says the reason why
25 they are imposing this, maintaining the appropriate cost accounting systems, is to
26 demonstrate that the obligations of cost orientation and, for BT, the charge control, are
27 being met. So we see the cost accounting obligations being imposed on BT are being
28 imposed specifically for cost orientation, do we not?

29 A Sorry, this says that: "BT and Kingston should maintain appropriate cost accounting
30 systems".

31 Q Yes?

32 A Are you referring to the cost accounting systems, or are you referring to the format of the
33 RFS?

34 Q Well, you are quite right to draw the distinction because, in fact, the directions relate to not

1 only what BT produces in the RFS, but also the level of data that they are required to keep
2 for the purposes of their accounting systems. You would agree with that, would you?

3 A I don't have the knowledge of that.

4 Q But if we look at 10.13 we see Ofcom saying in terms:

5 "In order to demonstrate cost orientation of a service or product, it is necessary for
6 the dominant provider to establish cost accounting systems that capture, identify,
7 value and attribute relevant costs to its services and products in accordance with
8 agreed regulatory accounting principles, such as cost causality. A key part of this
9 process is the stage which identifies those parts of the underlying activities or
10 elements that directly support or are consumed by those services or products.

11 These elements are referred to as network components."

12 And that is actually picking up on the point you made earlier to Mr. Thompson, that
13 components have a specific term in the regulatory context when you are looking at the RFS?

14 A Yes, that is right.

15 Q Now, I am afraid I am going to have to take you to another bundle, can I ask you to go to
16 BT10, tab 26, which is actually a statement that went hand in hand, which is the statement
17 of Ofcom that imposes the regulatory reporting obligation. So, tab 26 in other words is
18 what we saw in the Leased Line Market Review, this is the process by which Ofcom
19 imposes those cost accounting requirements. If we look at para. 3.22, which is on p.13 you
20 can see that Ofcom is stating in terms:

21 " that the level of detail set out for BT in the April consultation is appropriate for
22 the reasons set out in that consultation, i.e. that the level of detail is necessary in
23 order to ensure that BT is meeting its regulatory obligations regarding cost-
24 orientation, no undue discrimination and price controls. "

25 So we see Ofcom there are indicating that the level of detail they are imposing in this
26 accounting obligation statement is actually specifically there in order for BT to ensure that
27 BT is meeting its regulatory obligations, do you see that?

28 A Yes.

29 Q If we go on in the document to annex 2, we see the notification to BT of the condition under
30 86. Schedule 2 sets out a number of terms about it, and when one gets to p.48 we actually
31 see the specific accounting conditions that are imposed upon BT. If we look at OA2 on
32 p.48 we can see that Ofcom can make such directions as they consider appropriate in
33 relation to BT's cost accounting system. You see that?

34 A Yes.

1 Q And the directions are in fact contained in annex 4 which, if we go on to p. 80 there we see
2 the directions. At p.83 we see the list of network components. So that is what you were
3 talking about earlier, network components, and what we have seen being traced through the
4 documents. If we look at 67 we see the component - the single component - in the AISBO
5 market is a generic component: "Alternative interface symmetric broadband origination
6 specific." Do you see that?

7 A Yes.

8 Q So if we come back to where I was, the level of detail that BT was required to keep its
9 accounts and to report on in 2004/05 was a single level, which is reflected in the RFS by the
10 short haul data services elements that are actually listed out there. That is right is it not, it
11 follows from the trail we have been through?

12 A That appears to be the case, I don't have any expertise on those sort of issues.

13 THE PRESIDENT: So in 67 it says "AISBO specific", what does "specific" mean?

14 A No, I am afraid I don't have any knowledge of that.

15 MR. READ: But there is certainly no other network component being reported in the RFS that
16 we have just been looking at?

17 A I don't know.

18 Q So if that was the only level for which Ofcom was requiring BT to account at in 2004/2005,
19 which is reflected in the RFS, would you accept that BT could not be expected necessarily
20 to keep any more detailed disaggregated figures than that?

21 A Does that not depend on other things such as the interpretation of the cost orientation
22 condition because, as I said, this is not an area in which I have expertise, but my
23 understanding is that Ofcom has a contrary argument. I do not place myself in a position to
24 adjudicate between those arguments.

25 Q I do not, obviously, want to spend a great deal of time debating the areas that you are not
26 familiar with, but if we can just put it neutrally you would accept that the only level of data
27 that BT was being asked to report at in 2004/2005 was at this singular short haul data
28 services level?

29 A Sorry, there is the distinction - my point is I don't know the answer to this - but there is a
30 distinction between the cost accounting systems and level of reporting. I have seen from the
31 documents, including the RFS itself, that the level of reporting was for a set of services in
32 aggregate - I am not sure whether that also covers the cost accounting systems or not.

33 Q This is set out in some detail in annex 1 to BT's notice of appeal, and if you have not
34 trawled through that in any great length ----

1 A I have not, no.

2 Q -- I do not think it is really fair to ask you further about that. Just going back to what
3 information from the RFS BT had at the time, you will agree that in January 2006 when it
4 has first got the opportunity to notify its prices that is the single level it has in the RFS?

5 A In terms of RFS data - in terms of published RFS data, yes.

6 Q Perhaps I should take you to this. Would you take BT12 and go to tab 31, we see that that is
7 Ofcom's regulatory financial reporting and audit requirements for 2005/06, and we see the
8 date of that is 16th August 2006?

9 A Yes, I see that.

10 Q Following on from that at tab 31 we see the current costs financial statements for 2005/06,
11 which we published on, I think, 7th September, so about three weeks after that final
12 statement, and if we look at p.129 there we see the information that was available in
13 September 2006. It has now been split by a process through the statement that we have just
14 seen and the consultation before it and it is no longer a single AISBO element but between
15 WES services and BES services. If we look again at the ceiling we can see the charge for
16 the year on the right hand column (it has moved into a different format for this year) for
17 both WES and BES, those charges for the year are below the DSAC ceilings - do you see
18 that?

19 A Can I just clarify, am I comparing for WES 8,051 charge for 13,219 for the component
20 ceiling for WES?

21 Q Yes - in other words, the charge is below the DSAC?

22 A Yes, and 31,804 compared to 51,566.

23 Q Below the 51,000, charge again below the DSAC?

24 A So again obviously this is an aggregate of charges, but, yes, I see that the aggregate of those
25 charges is less than the aggregate of the DSAC.

26 Q Can I ask you to take core bundle B, and go to 13.15. We actually see what Ofcom say
27 about the reports, and as you can see it says in respect of BES, but I think the same is true
28 for WES:

29 "further disaggregated data was published. There were no internal sales. Without
30 detailed financial information it is not straightforward to apportion total revenue
31 and DSAC between services."

32 Then, as you can see, that is what effectively Ofcom attempt to do using some proxies, and
33 at table 13.4 we see the various figures that Ofcom estimate, and again if you look at these
34 disaggregated figures, there is a series of options one could actually use for the DSAC, we

1 see that, in fact, for the Ofcom revenue estimate it looks as though, for the most part, BT's
2 services are under that DSAC ceiling. Do you see that?

3 A I just want to make sure I'm understanding this table. We have an Ofcom revenue estimate
4 column, and then we have three columns with DSAC in them, and these are alternative
5 ways of splitting the aggregate DSAC between the specific BES services. Right. You are
6 asking me about the comparison of the revenue estimate column with all of the three other
7 columns?

8 Q I think the figures probably speak for themselves, and I do not want to take up time, but I
9 am simply making the point that even when Ofcom split it out in this fashion on figures that
10 obviously it did not have, essentially it still ending up with the conclusion that the prices for
11 2005/06 are below the DSAC ceiling. Indeed, that is the reason why there was no
12 overcharge, because even on this methodology Ofcom found that BT was still compliant?

13 A Yes, that's right, Ofcom found there was no overcharge in 2005/06.

14 Q So the consequence of this is that on the data that would have been available immediately in
15 September 2006, BT would have been in the position of thinking that it was more or less
16 compliant, would it not? If you look at all these figures, there is nothing to alert BT to the
17 fact that its charges are looking as though they are going to radically exceed DSAC?

18 A It depends if you're putting to me a simple extrapolation of the prior year. If you're saying if
19 BT compared its charges in 2006/07 with its RFS or rather a split of the RFS by service in
20 2005/06, I don't know, that may be the case, I haven't seen that comparison. Whether there
21 were changes in the costs between 2005/06 and 2006/07 and whether they were foreseeable,
22 obviously I can't recall the extent to which the Determination assesses that.

23 Q One of the things, as you know, that BT has been complaining about bitterly in this case is
24 that whatever may be the position for the years 2007/08 and 2008/09, for the years 2006/07
25 it is wrong now to assess BT with the benefit of hindsight that Ofcom has done without
26 recognising the issues and the problems that BT faced in 2006/07. That is BT's case?

27 A I understand that's BT's case. I also understand that Ofcom in the Decision didn't agree with
28 that case.

29 Q Can I turn to another issue with you now, because obviously you cannot take it any further,
30 because you basically do not know the level of detail or disaggregation that BT was being
31 asked to keep accountable because, as you have accepted, that is the first time you have
32 looked at that - that is right, is it not?

33 A Yes.

34 Q Can we look at another problem then. Can we look at the DSACs for 2006/07. I am going

1 to ask you to now go to BT7, tab 11. These are the RFS ----

2 A I am sorry, which tab was it?

3 Q Tab 11. These are the RFS for 2006/07.

4 A Yes.

5 Q Can I ask you to look at p.39, which contains the figures, the splits, for this period. Can I
6 first ask you to look at WES 10 rental, and if one goes across one sees that the unaudited
7 LRIC ceiling is given as 53,33.03. Do you see that?

8 A Yes.

9 Q And if one looks at the FAC one sees it is 5,014.99 - do you see that?

10 A Yes.

11 Q The figure, if my arithmetic is correct, means that DSAC is about 6.3 per cent above FAC?

12 A Yes. I haven't checked that percentage, but yes, I can see it.

13 Q It looks about right though, does it not?

14 A Yes, it does.

15 Q You have got a 300 difference over a 5,000 FAC figure?

16 A Yes.

17 Q If we look at WES 100 rental, we see that the figures are 565.29 and 5097.45. Do you see
18 that?

19 A Yes.

20 Q Again, my estimate of that it is about 11 per cent difference - in other words, the extra 580,
21 or whatever it is, over the 5,000 figure for the FAC is around about 11 per cent?

22 A Right.

23 Q I think you would accept, would you not, that that is a very low FAC to DSAC ratio? It is
24 not what you would normally expect the DSAC to be above FAC, you would expect it to
25 have higher headroom, would you not?

26 A Yes, it would be certainly more typical for there to be materially more headroom.

27 Q If one goes on and looks at the BES figures, and if one takes in particular the BES 100
28 rental, one sees the DSAC for that is 5,072.76, but the FAC is 5,302 - do you see that?

29 A Yes.

30 Q That is a result that you would not expect at all, is it, DSAC being below FAC?

31 A Yes, that's unusual, yes.

32 Q If you look also at BES other bandwidth rentals, you can see that that is 5223 and the FAC
33 is 5340.37. So again it is DSAC below FAC, which really just should not happen, should
34 it? You should not be having DSACs below FACs unless something very, very weird is

1 going on?

2 A Well, I certainly agree it's unusual. It's an issue that was addressed in significant detail in
3 the Determination, where I think it's explained that it can arise where different allocation
4 methods effectively are being used between the derivation of the FAC figures and the
5 derivation of the DSAC figures?

6 Q Yes, but that point was being made in a different context, was it not, because it related to the
7 .C.L methodological change that BT was suggesting should be made because in effect what
8 had actually happened was that these figures must have been wrong as a result of that
9 because you would not expect DSAC below FAC?

10 A So BT's argument during the administrative stage was that the fact that there were examples
11 of DSACs below FACs meant that the DSAC figures must be wrong, and Ofcom considered
12 that in significant detail. It is Section ----

13 Q Section 12, I think it is.

14 A 12, thank you, of the Determination, and Ofcom concluded that it did not agree with BT and
15 it decided that was not the case, that there were still sufficient reasons for using the DSAC
16 data, although it did point out some issues and some failure to follow cost causation in those
17 numbers.

18 Q Because what you would normally see, and we can see this on p.40 for the previous year's
19 accounts, because p.40 is in fact the statement for the services year ended 31st March, and
20 again it is not split up in that detail but it is splitting out WES and BES. You can see that
21 you get what you might call the "normal" scenario of a quite low LRIC floor, a FAC
22 substantially in the middle at 7,000, and then LRIC ceiling, a DSAC, at 13,000, and that is
23 what you would normally expect?

24 A Yes, it is more normal for FAC to lie within the range between DLRIC and DSAC.

25 Q I think in the original *PPC* case there was actually a graph that actually showed the way you
26 would normally expect these things to go, in that the more you disaggregated things the
27 most you would expect that in fact you would have a wider variation between DSAC and
28 FAC and DLRIC, and indeed between SAC and pure LRIC.

29 A Yes. Just to make sure that I have recalled the same diagram you are describing, this says
30 about how if you look at any of these cost measures at the level of BT as a whole they are
31 all going to be the same. Standalone cost for BT as a whole is the same as the incremental
32 costs for BT as a whole and the fully allocated costs as a whole, but if you look at a more
33 disaggregated level then there is likely to be a departure between those cost measures.

34 Q Yes, I think in fact we might be able to have a look at that in a moment. What I would like

1 you to look at is para.14.65 in the Determination. Do you see that?

2 A Yes.

3 Q At 14.65.1 it is stated that BT has not:

4 "demonstrated that its unit DSACs were lower than it reasonably expected when
5 setting charges for 2006/07".

6 But looking at the figures we have looked at in the RFS, they are quite low, are they not,
7 compared to what you would expect given that you would expect a much higher headroom
8 between DSAC and FAC?

9 A So they are generally lower than you would normally expect compared to FAC for that year,
10 when that FAC information was not available contemporaneously with the setting of prices?
11 I am sorry, you are putting to me a comparison between DSAC and FAC in the 2006/07
12 RFS, which was not published until - I am sorry, what date was it - September 2006? Is that
13 right?

14 Q Yes, that is absolutely right. It is September 2007.

15 A So, I am sorry, wasn't there some further evidence on what DSACs could be forecast based
16 on ----

17 Q Yes, there is and we will come to that in a moment.

18 A The Coulson report on which I commented.

19 Q If you just look at the RFS itself, it is suggesting that in fact DSACs may well have been
20 lower than anyone would have anticipated because you would not expect them to be below
21 or very close to FAC.

22 A But you seem to be applying hindsight there. Again it is a matter of the question you are
23 putting to me. If you are putting to me, at the time that BT set its prices, it would not have
24 had the 2006/07 RFS, whether that was the FAC information or the DSAC information.

25 Q But the information it did have in its RFS suggested that for the previous two years it had
26 been compliant, did it not, because that is what we have seen from the 2004/06 and
27 2005/06?

28 A For 2005/06, yes. For 2004/05 we just looked at the aggregate of all the services. What that
29 does not address is what might have been reasonably foreseeable in terms of changes in cost
30 between 2005/06 and 2006/07.

31 Q Can we now turn to the question of forecasts?

32 THE PRESIDENT: Before you leave that, I think what is being put, Mr. Myers, is that when it
33 set its charges for 2006/07, based on what it then had, it would not have expected what
34 emerged, when you then got eventually the RFS for 2006/07, namely that on a number of

1 services the DSAC was unusually below the FAC.

2 A It would not have expected that. Whether that is something on which BT relied, given that
3 it did not have the FAC information for 2006/07, I do not know. I do not see how it could
4 have relied on that given that it did not have that information at the time it set those prices.

5 MR. READ: No, but when Ofcom considered the question of whether BT should be found to
6 have been in breach of the cost orientation obligation and when it was ordered to make the
7 repayment, Ofcom did know those figures and it knew that those figures looked rather
8 peculiar, did it not?

9 A It did but also Ofcom concluded that the figures were fit to be used, the DSAC figures for
10 2006/07 were fit to be used in the context for the purpose of assessing cost orientation, and
11 BT's charges were a very long way above them, and in para.14.65.1, which I think you
12 pointed me to, it refers to DSACs lower than it reasonably expected. That is obviously a
13 slightly different question from looking at the outturn. I do not see that the outturn
14 definitively answers the question of what BT might have reasonably expected.

15 Q We can debate what the Decision actually says but I am conscious of the fact that I am
16 probably going to overrun 4 o'clock already, so I do not want to take any more time on that
17 point. Can we look at forecasting, because you accept, I think, that Ofcom recognised,
18 when it imposed the SMP condition in July 2004, that the Ethernet market, the AISBO
19 market, was nascent -- that is the phrase that gets used -- did it not?

20 A "Relatively immature" is the phrase that I recall but, yes, I do not disagree with "nascent". I
21 am not drawing a clear distinction between "nascent" or "relatively immature". Both may
22 well have been used.

23 Q If it is nascent, there are going to be problems, are there not, in the likely take-up of the
24 product because the whole thing is nobody quite knows what is going to happen. It is not
25 like a stable product where you do not know what elements are going to be taken up or not
26 taken up.

27 A Yes, there may be some significant potential for forecast error, which is a point, as I recall,
28 Ofcom accepted in the Decision.

29 Q We have had the debate already, but if volumes drive the actual cost allocations in ways that
30 are not dependant solely upon a revenue volume/linear graph, if there are other things going
31 on then that could affect the costs as well?

32 A So the costs might be affected and the costs forecasts might be potentially affected in terms
33 of potential for forecast error. I think the point Ofcom was making in relation to evidence
34 was that BT did not provide, during the administrative phase, any forecasts of DSACs for

1 2006/07 which it used when it set its prices. At least that is one of the points I think Ofcom
2 was making.

3 Q Is that actually true because perhaps the easiest way of doing this is to take Mr. Maldoom's
4 first report, which is in Bundle D, which should be in the same bundle as your statement,
5 and if you go to Tab 3, which is his first report, and go to p.50, one sees at para.145-146 he
6 is referring to a number of pricing papers about forecasts. Do you see that?

7 A Sorry, is that a volume forecast or a cost forecast?

8 Q He seems to be talking about volumes.

9 A Volumes, all right.

10 Q "For future years, WES forecasts were simply on the basis of advice from 'product
11 managers'. The pricing paper also note that there was little basis to verify the
12 forecasts".

13 Then:

14 "The pricing papers of 2004, 2005 and 2006 suggest that, once established, WES was
15 expected to grow significantly. BES, on the other hand, was not. Both pricing papers
16 OPG 22/2006 and WPAG 8004/05 suggest that BT was expected to have low volumes
17 for the subsequent five year periods".

18 Do you see that? So those pricing papers, and, as I say, I have not got time to take you
19 through all the pricing papers at length, but those pricing papers, on what Dr. Maldoom
20 said, seem to suggest that there were difficulties in forecasting. Yes?

21 A So, yes, there were some difficulties. Whether they are the precise nature of the difficulties
22 that Dr. Maldoom suggests I do not recall. I would have to review this in detail and also
23 look again at the Determination which, I have said, accepted in general that BT did have
24 difficulties in forecasting volumes in this year.

25 Q Yes, so, for example, if we look at para.10.204 in the Determination we can see that there is
26 specific reference made to BT's pricing papers. Some of it is marked "confidential". But,
27 for example, in para.10.208 we can see a footnote that is not confidential, or rather the
28 footnote reference is not confidential, 552 and there is a reference, and I do not think the
29 pricing paper number itself, which is in 552, can possibly be confidential, but one can see
30 that that is the very OPG 22/2006 paper that Mr. Maldoom was referring to.

31 A Yes, I can see that. I was actually referring to something beyond that, which was Ofcom, as
32 I recall, analysed this issue of forecast difficulties for 2006/07 in Section 14 of the Decision.

33 Q Yes, if we go to 14.63, this may be what you are referring to.

34 A I think I am referring to this section including this paragraph, yes.

1 Q We know, because it refers there in the first sentence of 14.63, to a pricing paper. Again I
2 am not quite sure why the pricing paper itself, the number of it, is confidential. But then in
3 14.63.3 one of the points made is:

4 "The forecasts relate to WES services only - no forecasts are presented for BES
5 services which represent [a certain percentage] of the total revenues".

6 That paper that I have just shown you earlier in para.10.208 in the Decision actually is the
7 BES paper that Dr. Maldoom himself was referring to earlier in his report.

8 A I am sorry, are you saying that the forecast was a BES forecast not a WES forecast?

9 Q What I am saying to you is that even though Ofcom had that relevant paper, it seems to have
10 assumed that it did not have the forecast relating to the BES services but only had the
11 forecast relating to the WES services.

12 A There seems to be a question of fact here. I'm just not clear. Ofcom's understanding was
13 that that forecast related to WES services only. If you're telling me that's wrong perhaps
14 you could show me why it's wrong.

15 Q I am just saying that Ofcom had the pricing paper relating to the BES services.

16 A So if it was a BES pricing paper but the volume forecast was for WES, then I'm not sure
17 how informative that is about BES, because BES and WES are different services used for
18 different purposes, and volume forecasts for one may not apply to the other, and my
19 recollection is that the volumes of the two evolved quite differently over a period.

20 Q You are absolutely right, but the point that Dr. Maldoom is making quite clear in his report
21 (and this is why I took you to the report rather than taking time to go through confidential
22 pricing papers) that they are relating to BES volume forecasts. That pricing paper relates to
23 BES pricing forecasts.

24 THE PRESIDENT: BES volume forecasts?

25 MR. THOMPSON: Sorry, BES volume forecasts, yes.

26 A Sorry, I'm a bit confused. Are you telling me that 14.63.3 in the Determination is factually
27 incorrect?

28 Q Yes, that Ofcom actually had the pricing paper which gave Ofcom the volumes for the BES
29 services.

30 THE PRESIDENT: I am sorry, I think on something like that you do need to show Mr. Myers the
31 paper and not take it through Dr. Maldoom. It may be confidential but I think we just have
32 to look at it.

33 MR. READ: The only problem is the way these bundles have been put together – go to BT18 tab
34 17. Sir, the slightly odd thing about this is the pricing paper itself does not appear to be

1 marked as confidential.

2 THE PRESIDENT: Well, it is your paper and your client's paper. If it is confidential you can tell
3 us and we will treat it as confidential. Is this the full --

4 MR. READ: Unfortunately, I do not think it is because if you go to Annex A p.3 you see the
5 supporting documents. I do not think the supporting documents have made it into the
6 bundle.

7 THE PRESIDENT: If there is a point on this, it may be that the sensible thing is to provide the
8 document (because this seems to be a factual point) and let Mr. Myers look at it overnight
9 and ask a question on it in the morning when he has had chance to look at it. He obviously
10 may never have looked at it, or certainly has not looked at it for quite a while and we have
11 not got it. So for all those reasons.

12 MR. READ: Sir, I am extremely conscious of the time I am taking.

13 THE PRESIDENT: We can park that and if you can, and if you want to ask about it, get a copy
14 of it.

15 MS GALLAFENT: Sir, I wonder if I could just ask some clarification. The reference in Dr.
16 Maldoom's report to which I understood the question was being derived, is to pricing code
17 for OPG 21 2006, but the paper we have just been taken to is 22.

18 MR. READ: No, it is para.146 of Dr. Maldoom's report where he is specifically dealing with the
19 BES papers which is OPG 22 2006. One relates to WES, one relates to BES.

20 THE PRESIDENT: yes, the one that is referred to in 14.63 (which is the point Ms Gallafent is
21 making) is OPG 21 2006.

22 MR. READ: Yes, and then they go on to say that there was no forecast volumes for the BES and
23 that is where we got into looking at pricing paper OPG 22 2006. But, as I say, if we park
24 that and perhaps I can try to sort it out.

25 THE PRESIDENT: Yes, give references. Presumably the other one is the one at tab 16?

26 MR. READ: Yes.

27 THE PRESIDENT: One can see that one of them is WES and one of them is BES.

28 MR. READ: I am just acutely conscious of the time, sir, so I think if I can park that, then I will
29 move on.

30 THE PRESIDENT: Yes. Mr. Read, how much more have you got?

31 MR. READ: I am tempted to say a lot, but I will try to cut it down as much as I can.

32 THE PRESIDENT: What we will do is we will sit until 4.45 but we want to give Mr. Myers a
33 short break.

34 MS ROSE: I am sorry to interrupt, but that will put me in some difficulty because I am meeting

1 my daughter at a tube station at 5 o'clock.

2 THE PRESIDENT: Yes, you are not asking any questions, I appreciate, but you need to know
3 what is said.

4 MS ROSE: No, but my juniors are not here either.

5 THE PRESIDENT: You will see the transcript. Is it essential that you are here to listen?

6 MS ROSE: I am in your hands.

7 THE PRESIDENT: Obviously, you would be excused. You can clearly leave, as you need to do,
8 but we certainly want Mr. Read to finish. It is just a question of seeing what the answers
9 are, is it, Ms Rose? If you have to read the last few pages of the transcript, I would have
10 thought that would cover your position, would it not? Of course, you can be excused to
11 leave. But I think it is right that Mr. Myers should have a short break. Yes, Mr. Pickford.

12 MR. PICKFORD: Sir, I am sure you will recall that part of today's time was allocated to Sky and
13 TalkTalk to ensure that we had adequate time, combined with today and tomorrow. In so
14 far as we overrun with BT, we respectfully ask that we can have that time made up
15 tomorrow.

16 THE PRESIDENT: We will consider that at the end of today. We will just rise for ten minutes.

17 Adjourned for a short time

18 MR. READ: Mr. Myers, can I now go to an illustration of 2006/2007. Can I ask you to look at
19 BES 1000 connection services? Let us start at the table in the Determination at core bundle
20 B, and table 13.10 first of all, on p.254. This table shows the figures reported in the RFS,
21 do you see that. If we look at BES 1000 connection, which is about a third of the way down
22 - do you see that?

23 A Yes.

24 Q You see there is revenue of £8.7 million, and DSAC of £6.4 million?

25 A Yes.

26 Q It is a matter of arithmetic, but if you take the excess of the revenue over the DSAC it is
27 about 35 per cent higher than the DSAC?

28 A Yes, that looks about right.

29 Q So on the RFS when this was reported, and as you have rightly observed, this is reported
30 after BT has already set its prices for that particular year, on the RFS figures there is about a
31 35 per cent excess of revenue over DSAC. Then I suspect you have gone some way further
32 on to table 13.37 I think it is, which after the adjustments Ofcom made we see the figures
33 for BES 1000 connection are slightly different, because the external DSAC I think has gone
34 down significantly and the revenue for the BES 1000 connection has remained the same?

1 A Yes, the revenue has remained the same in both the FAC and the DSAC have gone down
2 significantly.

3 Q And that is as a result of Ofcom's cost adjustments?

4 A Yes.

5 Q And if we go to table 14.13 on p.379 we see that figure has gone up from what would have
6 been 135 on the RFS figures to 222 per cent. I am looking at the 2006/2007?

7 A Yes, 222 per cent revenue as a proportion of DSAC.

8 Q It is fair to say, is it not, and you touched on this with Mr. Thompson earlier, that the
9 adjustments that Ofcom made were effectively made clear in the 2009 Leased Line Charge
10 Control. Perhaps I ought to take you to that and just explore that a little more. If you go to
11 BT7. I am sorry to keep moving around the bundles, but it is the only place where the full
12 document is listed out, and if you go to tab 12 and p.97 we see the adjustments that are
13 being made to the cost baskets, do you see that, table 4.2 on p.97. Do you see that?

14 A Yes.

15 Q And we see there are a series of amendments made to the RFS?

16 A Yes.

17 Q And we can see, for example, there are payment terms, exclusion of 21CN, and in the case
18 of TISBO, because this is the TISBO price cap, regulatory asset value and holding gains. If
19 I can just explore very briefly with you one of those payment terms, just to see how it
20 works, if you go to para. 4.135, p.108, and which is referenced in the table?

21 A Yes.

22 Q This is essentially an adjustment to reflect the fact that Ofcom thinks that BT gets paid for
23 effectively late paid debts should be adjusted to effectively the contractual terms rather than
24 as BT were saying to reflect their actual experience of dealing with customers?

25 A I would need to review this text to confirm that. Do you want me to do that?

26 Q The only point I am trying to make from this, Mr. Myers, is that obviously when you were
27 dealing with Mr. Thompson earlier, the point he was putting to you is that BT could not, in
28 2006/2007 for example, have actually understood that these adjustments were necessarily
29 going to have to be made to their RFS, because they only find out the conclusions about the
30 adjustments in the 2009 leased line charge control?

31 A But the point I made before which I will perhaps reiterate here, is that if this is one of the
32 adjustments that Ofcom made, which accounts for part of or some of the cost difference
33 between the unadjusted and the adjusted RFS for BES 1000 connection then Ofcom would
34 have come to the view that the treatment of payment terms in the RFS, as published, was

1 either an error or obviously inappropriate. I think if it was in error or obviously
2 inappropriate then, as I say, you should expect it to be adjusted.

3 THE PRESIDENT: Just help me, table 4.2, this RFS it is not regarding the AISBO services, is it?

4 MR. READ: No, but I showed this just in order to draw attention to the basis upon which the
5 change was made and, in particular para.4.137.

6 "On the other hand we disagree that the debtors' calculations should reflect
7 disputed invoices, as this would not give BT the correct incentives to minimise its
8 costs."

9 So there is Ofcom, in respect of the TISBO price cap, indicating, considering the changes as
10 to whether or not the incentives should be made, and then at table 5.2 on p.149 one then
11 sees Ofcom adopting the same approach to the AISBO cap, which is then reiterated at para.
12 5.71 at p.153?

13 A And are you saying the same adjustment was made in the Determination?

14 Q And the same adjustment is then made in the Determination.

15 A Where would that be in the Determination?

16 Q That is at para. 13.204. at B, p.280. At 13.204 you can see the payment terms are being
17 discussed and there is an analysis and it is set out. At para. 13.215 in the Determination,
18 they say, on the contrary: "This was consistent with the approach we took in the 2009 LLCC
19 Statement."

20 A Yes, and I think the point I was making that in 13.210 Ofcom reaches the view in the last
21 sentence that without the adjustment BT's numbers, the RFS numbers, would be obviously
22 inappropriate.

23 Q But I am putting a simpler point to you, that this was all being challenged by BT in the 2009
24 leased line charge control. We see that BT is saying that actually you should not be looking
25 at contractual terms, you should be looking at what actually happened on the ground.
26 Ofcom reject that and there may have been fair reasons for rejecting it, they mention
27 incentives as we have actually seen. The point is that up until 2009 it would not have been
28 obvious that that change was necessary?

29 A I am not sure I am in a position to comment definitively on that, but I would observe that
30 Ofcom's view is that the methodology BT used was obviously inappropriate.

31 Q Well, it is a point going to certainty, and I think we have probably exhausted it as far as we
32 can go. But let us return to the BES 1000 connection, if we may. You would accept that it
33 is as a result of those sorts of changes that lead to this not insignificant leap between,
34 effectively, a 36 per cent missing of the DSAC ceiling to effectively 122 per cent missing of

1 the DSAC ceiling in table 14.3. That is what causes those figures to go up so much?

2 A The cost adjustments?

3 Q Yes, the cost adjustments?

4 A Yes, that seems to follow from the numbers you took me to.

5 Q Can I put a further point to you? It is going back to the accounting obligations again. Let us,
6 first of all, look at the Determination itself, because one of the criticisms that is made of BT
7 in para.14.200 is that you would have expected BT to have monitored this cost for the
8 service during the course of the year. If Ofcom - I know I am putting this on an "if" basis
9 because you frankly conceded you do not know enough about the accounting obligations to
10 really give a definitive view - was only requiring BT to report at a much more aggregated
11 level in 2004/05 and 2005/06, it is not obvious, is it, that BT would have been assessing its
12 cost on a more disaggregated basis?

13 A There seem to be at least two things relevant to that. One is the meaning of the condition in
14 terms of this issue of aggregation or individual service assessment, and also potentially the
15 difference between cost accounting systems and level of reporting.

16 Q BT would not need to capture this information on its data, would it, unless it was required to
17 do so by the RFS? It would not actually end up allocating all its fixed costs between these
18 different services unless it was subject to the accounting obligation that Ofcom had imposed
19 upon it?

20 A For the purpose of meeting the reporting obligation, if that reporting obligation was at an
21 aggregated level, it wouldn't need to. Whether it would need to for the purpose of satisfying
22 the cost orientation condition is a different question.

23 Q You are surely not suggesting that if Ofcom have specified the level of accounting
24 information that BT has to keep, the condition itself imposes a greater obligation on BT?

25 A Sorry, could I just clarify. You said the obligation specifies the accounting information that
26 BT has to keep? I thought it was about the level of aggregation of data that BT had to
27 report. Those are different things.

28 Q Yes, they are, and when I took you to the accounting obligations document back in July
29 2004, the point was that it was about accounting separation as well as reporting
30 requirements, and we went through and we saw that the only obligation on BT in 2004
31 related to a single reporting component level?

32 A Yes, I think that's the point I'm making, that that obligation was a reporting obligation, if I
33 have understood it correctly.

34 Q No, no, it goes further than that, Mr. Myers, but if you are not familiar with it then I think

1 we should probably park that subject.

2 Q No, I'm not.

3 Q Can I just ask you to go back to table 14.13, which is p.379. It is quite clear, is it not, that
4 what happens here is that the external revenue remains pretty constant throughout 2006/07
5 and 2007/08 and 2008/09, it drops in 2009/10, and that is to be expected because, of course,
6 the product was coming to the end of its natural life in 2009/10?

7 A I'm sorry, could you repeat that, please?

8 Q Yes, if you look at the table, we can see that average external revenue remains at just over
9 5,000 for 2006/07 and 2007/08 and 2008/09 - you have that?

10 A Yes.

11 Q For 2009/10 it drops, and I was simply making the point that the reason why it drops is
12 because it has effectively come to the end of its product life which you may or may not be
13 able to comment upon?

14 A I'm not able to comment on that.

15 Q But what puts BT in breach in 2006/07 on Ofcom's view is that the 5,200 revenue has
16 exceeded by, on Ofcom's figures, 220 per cent the external unit DSAC of 2,338. That is
17 clear from the figures, is it not?

18 A Well, I think the excess is 122 per cent, but yes.

19 Q Yes, 122 per cent, quite right. But the point is that what then happens is that it is not that
20 anything happens to BT's prices, it is that over the next few years the external unit DSAC
21 goes up?

22 A Yes, I see that.

23 Q And, as a result, in fact, we can see that not only does the DSAC go down considerably, but
24 even the ROCE goes into negative figures at the end of the period?

25 A Yes, I see that.

26 Q My question is a simple one: why is it that Ofcom does not look at the average over the
27 period? If it did, BT would be compliant for those four years?

28 A As you pointed out, there were things changing over the period. Prices certainly changed in
29 2009/10, there were not such large changes in other years, but as you pointed out there were
30 significant changes in the year by year costs, very significant changes on these numbers
31 between each of the years. I think that would create circumstances - costs circumstances in
32 this case or cost and revenue circumstances in 2009/10, that were very significantly
33 different between each of these years. In that context, averaging runs a significant risk of
34 averaging together two rather dissimilar things and reaching a false conclusion, that

1 conclusion about a false negative conclusion I was being asked to comment on earlier by
2 Mr. Thompson, as a consequence of averaging different things together. Ofcom's approach
3 was a different approach which addressed the same underlying concerns that lead one, or
4 might lead one to - or the argument is made that one should average, which is to look at the
5 year by year costs and invite an explanation of why, in this case, the costs are so different
6 between, for example, 2006/07 and 2007/08 - in other words, look at the specific
7 circumstances. So I would say, therefore, to summarise that, two points: Ofcom's approach
8 by looking at the evidence on a year by year basis addresses effectively the same underlying
9 concern which is the proponents of averaging across years are leading them to that view, but
10 it avoids one of the disadvantages of averaging, which is that it may hide overcharging in
11 one year by combining it with something that's comfortably below DSAC in a different
12 year.

13 Q The reality of all of this is that Ofcom knew quite well, did it not, that BT was not looking
14 at single years when it was making its assessment of cost orientation? Ofcom knew that?

15 A Perhaps you should point me to the reasons why you say that.

16 Q You were shown this morning the material that BT was putting forward to Ofcom in 2007,
17 which showed quite clearly that BT was saying to Ofcom, "We have looked at this over a
18 five year period". Perhaps I ought to take you very briefly to it again. Can you go to BT16,
19 tab 13, p.6. This is one of the pricing papers that BT hands over to Ofcom at the time?

20 A Is that right, it was seen by Ofcom at the time?

21 Q If you go back to the previous page you can see that this is responses from Openreach, p.3,
22 so this material actually being provided in the context that Mr. Thompson took you to this
23 morning.

24 A So this would have been in 2007?

25 Q This actually would have been in early 2007 when BT was conducting ----

26 A The letter seems to be dated June 2007.

27 Q Yes, the pricing paper is earlier, because the pricing paper is being submitted as an instance
28 of showing BT's efforts to be cost orientated?

29 A I understand the pricing paper was earlier. Are you saying that Ofcom had it before this
30 letter or at the time of this letter?

31 Q They had it with this letter, 6th June 2007.

32 A So they had this in June 2007, thank you.

33 Q So 6th June 2007, and if we just look at p.7, for example, it is making absolutely clear that
34 BT is looking at - this is in respect of WES 10 and we will need to come back to that very

1 | shortly, so perhaps we can just see that it is being put on the basis of a five year ----

2 | A I'm sorry, did you say p.7?

3 | Q At the top there should hopefully be a little diagram - do you have that, a little figure?

4 | A Yes.

5 | Q Showing for WES 10 five year view excluding Main Link - do you see that?

6 | A Yes, I see the diagram, I am not sure I fully understand it.

7 | Q I am very conscious of the time, if you go to the next page, p.8, and I just want to pick this
8 | up in WES 10, and we will see WES 10 in a short moment, if you can see:

9 | "Because the impact of the 10MB rental increase affects the existing customer base
10 | who would see an increase in rental charges, a decision to allow an 18 month
11 | migration window for existing 10MB circuits means that they will only pay the
12 | increased rentals on new circuits. During this period prices for 10MB circuits will
13 | be phased in 3 price changes details of which are in the main paper."

14 | If you look at p.13, you can see the first paragraph starting on that page after the 2 and 3:

15 | "The rebalancing carried out now means that the prices more closely match to the
16 | costs of providing service with all variants being profitable over 5 years."

17 | This is the five year period that BT was actually analysing prices on. If one goes a bit
18 | further in this same divider to p.61, this again is material being provided by BT to Ofcom in
19 | 2007 to explain the cost orientation of its prices. Again, we can see quite detailed figures
20 | being set out there for WES 10, WES 10LR, and so on and so forth, and one can see that the
21 | costs are split down not between connections and rentals but the revenues are, which is
22 | perhaps not surprising if BT is billing on connections and rentals, but it is all being done
23 | over a five year period. You see that, the figures, the projections, and everything are being
24 | done over a five period?

25 | A Yes, I see there's years one to five, yes.

26 | Q So if BT has been clearly pricing on the basis of a five year period and if Ofcom in
27 | hindsight is making an assessment of whether or not BT has met its cost orientation
28 | obligation, do you think it is right to exclude looking at and taking into account an average
29 | over a five year period?

30 | A So that seems to turn on the question of whether, if this is indeed was doing consistently,
31 | whether that was a reasonable approach or not, and I would go back to what I said before,
32 | which is I think there were significant problems with trying to assess cost orientation
33 | looking only at the figures over a five year period when circumstances - prices may change.
34 | In the example you showed me costs changed very materially between those five years.

1 That seems to me to be quite problematic to run a significant risk of reaching an incorrect
2 conclusion.

3 Q Where in the condition HH3 does it say the time period over which the cost orientation is
4 going to be assessed?

5 A I was not commenting on the wording of the Condition because I think I agreed earlier that
6 it does not specify a time period. My point was based on an economic analysis, that, based
7 on an economic analysis, I would say that there are significant problems in looking at
8 aggregating over a five year period for the purpose of cost orientation.

9 Q As an economist, are you saying that you would look at single years in isolation?

10 A It depends on the question that one is addressing. If one is looking, for example, at the
11 profitability of a service as a whole in terms of the investment, return, that would be owned
12 on that product over its life, that is clearly a different question. I think what it is appropriate
13 to look at, economically speaking, depends on the question and my previous comments
14 were in the context of my understanding of economic analysis of cost orientation.

15 Q Just leave that bundle out.

16 THE PRESIDENT: Could I just ask, is this being dropped, this paper, on the basis that BT were
17 looking, which was provided to Ofcom, as you pointed out, Mr. Read, were looking at cost
18 orientation over a five year period or just planning their price adjustment over a five year
19 period going forward?

20 MR. READ: I think, Sir, that it is Karen Wray's statement. But if one perhaps goes to p.15 one
21 sees specific mention of regulation being subject to cost orientation.

22 "However the pricing of the Openreach Ethernet portfolio is seen by Ofcom as one of
23 the key factors in the effectiveness of the Undertakings" ... [so that is the equivalent
24 of input undertakings] ... which is based on the access/backhaul component policy.
25 There have been a series of meetings with Ofcom over the course of the review to
26 share and discuss the findings at each stage, including considerable discussions on the
27 incentives for CPs to go down the WES component route versus WEES. . This has
28 led to a wider policy debate over incentives and the right backhaul
29 structure/model...".

30 I think that the point that I am certainly making is that in that context BT was plainly
31 discussing looking at profitability and issues over a five year period and, indeed, if one turns
32 back to p.5 one sees:

33 "Provide any information that BT considers relevant to demonstrating BT has satisfied
34 its ex-ante cost orientation obligation...

1 The charges have been calculated in accordance with the management accounts as set
2 out in the spreadsheet titled *Unit Financials ...*".

3 Those are the ones that we have been looking at.

4 "When LRIC costs are calculated ... ROCE over 5 years is lower than that allowed by
5 Ofcom (11.4%)...".

6 So BT could not have been making it much clearer that, when it was looking at cost
7 orientation, it certainly was looking at a five year period. It is in respect of a specific
8 question that Ofcom itself has asked about BT providing any information as to how BT has
9 satisfied its ex-ante cost orientation obligation. So the point I am putting to you is if Ofcom
10 knew that BT was doing those prices, is it really right for Ofcom to jettison any analysis
11 over a longer period when it comes to reassess whether BT has been in breach in 2006/07 in
12 respect of BES connections, 1000?

13 A So, as I said before, I think that seems to turn on a question of whether or not BT's
14 interpretation was a reasonable or appropriate interpretation, and I do not comment on the
15 appropriate legal interpretation of the condition but, as I commented before, economically
16 speaking I think there are some significant issues in aggregating across a five year period, or
17 averaging across a five year period, when there are very material changes in either revenue
18 or, in the specific case of BES 100, specifically costs between the five years within that
19 period.

20 Q You were involved, were you not, in the *PPC* case?

21 A In the *PPC* case, yes.

22 Q You presumably, I think, were involved in the basis upon which Ofcom reached its decision
23 in that case?

24 A Yes.

25 Q I wonder if you can take Bundle B8 and if you can go to Tab 16, which is BT's 20th April
26 2012 response. Do you see that?

27 A Yes.

28 Q Can you go to p.110? So this is BT's response in this Ethernet case and it is setting out what
29 it sees as the previous approach of Ofcom and the CAT, and then at 299 there is an
30 extensive quotation from the Draft Determination in the *PPC* dispute. Do you see that?

31 A Yes.

32 Q This is what Ofcom is saying:

33 "The DSACs of an individual service can fluctuate from year to year, meaning that an
34 unchanged charge that was below DSAC in one year might be above DSAC the year

1 later. In considering the extent to which we can rely on individual years where
2 charges are above DSAC, it is therefore important to bear in mind that BT sets its
3 charges on the basis of the information that is available to it at the time. Given that
4 the DSACs for the year are only known at the end of the year, BT does not know what
5 the appropriate value will be when setting its charges".

6 Then it goes on:

7 "If charges do not change materially in a year but the DSAC unexpectedly declines, it
8 could be argued that it is unreasonable to consider that this one charge in isolation
9 represents an overcharge.

10 5.7 There may also be accounting treatments of costs that affect the pattern of costs
11 between years. For example, some costs might be expensed in the year in which they
12 are incurred but also yield benefits in other years. In such circumstances revenues
13 might look lower relative to cost in the year in which the costs are expensed and
14 higher in the other years. Considering the comparison between revenue and costs
15 over a period of years reduces the risk of drawing inappropriate conclusions".

16 Then one sees in para.300 the Final Determination being set out there. Perhaps I should
17 also refer to para.5.8 of the provisional Draft Determination, but one can see what is said
18 there. Then in para.300 the Final Determination is set out in the *PPC* case, and I am reading
19 the third paragraph starting in para.300:

20 "For the purposes of resolving the Disputes, for the reasons set out in greater detail in
21 Section 7, we therefore conclude that overcharging has occurred where charges have
22 been persistently above DSAC for the majority of the period (i.e. for at least three out
23 of the five financial years ...). Charges above DSAC for this length of time indicate
24 that BT has failed to take action to alter its charge in light of them being above DSAC
25 and would increase the potential for economic harm.

26 Where charges exceeded DSAC in fewer than three financial years, consideration for
27 specific circumstances is warranted. The relevant circumstances may include:

28 ...

29 (ii) Average charges compared to DSAC across the whole period".

30 So that is plainly what Ofcom thought was the right approach in 2009, is it not? I am sorry,
31 2010.

32 A In 2010. So these are the factors that Ofcom looked at in that *PPC* Determination and one
33 of those considerations was the average charges over the whole period. Then there were
34 these other considerations. I think we should turn to the *PPC* Determination itself because I

1 think we will see from that that these other considerations were much more important than
2 the average charges. In relation to the points at para.5.7 on p.110, that is giving a specific
3 example of a cost that is expensed yield benefits in other years. That is a specific reason for
4 either applying an accounting adjustment or, if that is not done, potentially looking across a
5 number of years, as long as those other years are not too dissimilar. I do not know if such
6 an argument of this type was actually being put forward in relation to BES 1000 connection,
7 for example. I am sorry, I have got two points. I think the first point is that I think it is
8 important to look at the *PPC* Determination. Perhaps you could tell me which bundle that is
9 in? I think it is very important because you are suggesting that Ofcom has adopted a stark
10 difference in approach and my point is that I think there is a very minor difference in
11 approach, and that, for example, Ofcom reached conclusions in the *PPC* Determination,
12 three services where there was a single year of price in excess of DSAC did not constitute
13 overcharging. And Ofcom's reasoning to support that conclusion was not about the
14 averaging of charges over a period. It was based on a year by year assessment and an
15 understanding that the price versus cost comparison in that year might be misleading.

16 Q I will take you to the *PPC* Determination if you want, but can I ask you first just to go
17 Bundle DF2 Tab 12?

18 A Yes.

19 Q This is your statement in the *PPC* case, is it not?

20 A Yes.

21 Q If we go to p.24 of the statement, by para.53, you set out there the position on BT's price of
22 2 megabit trunk services compared to DSAC and FAC, and then we see on the right-hand
23 column you actually have conducted an average, have you not?

24 A Yes.

25 Q So you did in that particular instance conduct an average?

26 A Yes, I entirely agree that in the *PPC* Determination Ofcom reported the average. My point
27 was, I think, to understand the importance of that you need to look at the conclusions and
28 the basis on which those conclusions were reached. I think that we should look at the *PPC*
29 Determination in order to inform that.

30 Q I think it is clear from your Table 2 that in respect of 2 megabit trunk services, which was
31 the only service that Ofcom found overcharging from in the *PPC* Determination -- and that
32 is right, is it not? I know subsequently it has gone on to do others ----

33 A In this *PPC* Determination, yes.

34 Q But in *PPC* the only issue was the 2 megabit trunk. Yes?

1 A Yes.

2 Q And we can see, it is self-evident from that, that with the possible exception of 2004/05,
3 which I do not think there was a finding of overcharging, then every single year, if you
4 looked at trunk alone, was well over DSAC.

5 A Yes.

6 Q So four out of the four years in question were all over DSAC.

7 A Yes, and my point is on this 2 megabit trunk service Ofcom placed weight on the excess of
8 price over DSAC in each of the four years, a year by year assessment, and it reported the
9 average but that did not play a large role in the conclusions. I hope now we can turn to the
10 *PPC* Determination in order to look at the point I was making.

11 Q I am trying to remember where it is in the bundles. No doubt someone will help me. (After
12 a pause): Do you have that?

13 A I do. So perhaps I should explain my point?

14 THE PRESIDENT: I am sorry, we are slightly ----

15 MR. READ: It is ST1-7.

16 THE PRESIDENT: At Tab 27?

17 MR. READ: At Tab 27.

18 A And I am starting at p.107. So Table 7.1 on p.107. That is similar to the table I've just
19 taken you to in my PPC witness statement for a larger number of bandwidths, not just the
20 2Mbit trunk but other services as well. Comparison between BT's revenue and DSAC. So
21 there is a year by year analysis of that for each of the five years, and there is an all years,
22 what the average is over all years. So that is reported in the Determination. In relation to
23 2Mbit trunk where, as you say, Ofcom found overcharging, I said that Ofcom placed weight
24 on the year by year assessment and the fact that price was significantly in excess of DSAC
25 in each of the four years for which Ofcom found overcharging, and it didn't place significant
26 weight I think on the average. If we look at para.7.31, this is discussing three services
27 where charges were above DSAC for one year, and Ofcom concluded that they did not
28 constitute overcharging. That analysis was based on the year by year assessment, and
29 identification of specific reasons, or reason, that applied why in the year in which price was
30 above DSAC there was evidence to suggest that the excess arose from ... costs that year
31 which may not have provided a true picture of underlying costs. So again, it's the year by
32 year assessment that's important to Ofcom's conclusion in the PPC Determination in respect
33 of finding of no overcharging, as well as in respect of a finding of overcharging on 2Mbit
34 trunk. Whilst I entirely agree that the average over the five year period as reported, that did

1 not play a major role in Ofcom reaching its conclusions.

2 Q But it still averaged in the PPC decision, which it has not done in the Ethernet decision.
3 Whatever weight you may place on it, you would agree, would you not, that the one thing
4 that has not been done is any averaging in the Ethernet Determination?

5 A Yes, I agree, averaging across years has not been done in the Ethernet Determination.

6 Q I think that (I am conscious of the time) I am just going to ask you one last question. It
7 relates to WES 10. If I can ask you to go back to the Decision itself and go to p.383. If you
8 look at para.14.213 you can see that four reasons were given in the Provisional Conclusions,
9 the last one of which was that:

10 "BT's charges exceeded DSAC as a result of BT increasing its charges three times
11 for the standard variant WES 10 rentals in June 2007, December 2007 and June
12 2008."

13 I asked you to look at that pricing paper and to note that BT was deliberately introducing
14 staggered pricing in three stages precisely not to jolt the market when it changed the prices
15 in 2007, yes? You remember that?

16 A Yes.

17 Q So do you think it is really a valid criticism that BT in fact changes its prices three times?

18 A I don't think that's the emphasis of the point that's being made here. I think the key aspect of
19 the point that's being made here and is then discussed further in the reasoning beyond the
20 Provisional Conclusions is that an important consideration in Ofcom concluding that the
21 excess of revenue over DSAC in 2008/2009 for WES 10 rental was that that came about as
22 a consequence of BT increasing its prices. I think the number of times it increased them or
23 the pattern by which it increased them is of less importance than the fact that the reason for
24 the failure of the DSAC test was BT increasing its prices to the level it did rather than, for
25 example, as a consequence of the DSAC falling compared to the previous year. We can see
26 that in two pages further on table 14.14. If, in the second row down, the average external
27 revenue, we can see that the 2007/2008 figure is 1,146 and the 2008/2009 is substantially
28 higher at 2,040, whereas in the next row down we can see the unit DSAC is slightly higher
29 in fact but very similar between 2007/2008 at 1,526 and 2008/2009 at 1,581. So the reason
30 why the DSAC test was failed in 2008/2009 was the price increase – or maybe a number of
31 price increases, but the effect of price increases, not a reduction in DSAC.

32 Q We can see from table 14.14, can we not, that BT, for one single year, misses the DSAC
33 ceiling by 29%?

34 A Yes.

1 Q If you looked over the period you would see that DSAC on average was not exceeded?
2 A I agree factually. Sorry, that's my understanding although factually I haven't done the
3 calculation. Sorry, are you going to ask me what the interpretation is?
4 Q The point I was going to ask you is simply this: is BT really in a hindsight investigation to
5 be criticised for missing its DSAC ceiling for a single year as a result of a staggered price
6 change agreed with Ofcom in 2007, particularly when it then brings its prices down and is
7 under DSAC for the following years? Is not this an automated approach?
8 A No it is not, and it is not a hindsight assessment. If you actually look at the analysis that
9 follows this table, as we can see, there's a discussion for example of contemporaneous data
10 unavailable (p.387) and that goes through the information that BT would have had at the
11 time which, at the start of the 2008/2009 period, would have been the 2006/2007 RFS.
12 Then the point is made in 14.236 that BT could have reasonably foreseen reduction in costs
13 between 2006/2007 and 2007/2008, because the 2006/2007 figure included costs of
14 mainlink, not just the costs of WES 10 rental, and those costs of mainlink came out in
15 2007/2008. Then, as we have seen, the DSAC in 2008/2009 is actually very similar to the
16 cost in 2007/2008. So I would entirely disagree with your suggestion this is a hindsight
17 assessment. There is in fact detailed discussion of data that BT had at the time, and what
18 they could have reasonably foreseen. That is in particular in 14.236 and 14.237 where it
19 says that whilst perhaps BT could not have known for sure that its price rises would lead to
20 the failure of the DSAC test, it could have reasonably identified the material risk. Those
21 played a role in Ofcom's conclusion that the failure of the DSAC test also constituted
22 overcharging on the facts in this case.
23 Q Could I ask you one final question. Could I ask you to look at BT33 tab 2, which you have
24 looked at already this morning. Let us have a look at what Ofcom itself was saying on 17th
25 January 2008. Do you see that.
26 A Where?
27 Q It is tab 2. I just wanted to show you the first page which shows you that it is 17th January
28 2008. Do you see that?
29 A Yes.
30 Q Then if you go to paragraph A12.4. You can see this is work by Ofcom on the 2006/2007
31 cost data. The second bullet point:
32 "the current pricing structure for WES/WEES is unbalanced: in general connection
33 charges appear to significantly exceed and some local end rental charges fall below
34 underlying FAC costs;"

1 Then I think if one looks at p.459 table 12.3 we actually see Ofcom's analysis of WES 10
2 and the profitability net of cost of capital. The rentals are in minus, are they not?

3 A My understanding is this is 2006/2007 data? Is that correct?

4 Q That is certainly what they suggest. But, of course, the reason why it is 2006/2007 data -

5 A That's also reflected in Table 14.14 in the Determination where the average external revenue
6 is less than the unit FAC, because this is FAC data, I think.

7 Q But, Mr. Myers, the reason why it is 2006/2007 cost data is because of course we know that
8 the 2007/2008 cost data was not available at this time, was it?

9 A Sorry, there seem to be two points to make. One is I just explained that Ofcom addressed
10 the question of the information that was available and whether BT could have reasonably
11 foreseen the cost reduction between 2006/2007 and 2007/2008, and Ofcom sets out its
12 reasons why it thinks BT could have reasonably foreseen it because it's the taking out of
13 mainlink costs which were bundled in with WES 10 in 2006/2007, coming out in
14 2007/2008. The second point is I think, as I recall, there is explicit recognition by Ofcom in
15 the service analysis of WES 10 rental that BT was indeed earning low ROCE. Indeed, on
16 the numbers in Table 14.14 zero in 2006/2007 and slightly below its cost of capital in
17 2007/2008. The objection I think was not to BT increasing its price at all; it was the extent
18 by which it increased its price, which took it above the DSAC when in Ofcom's view that
19 was, as I said, (whilst BT perhaps could not have known for sure) possible to identify the
20 material risk that its charge would exceed DSAC.

21 Q 14.221 the last sentence says:

22 "As noted above, in our Provisional Conclusions we observed that if BT had not
23 increased its prices from the level in June 2007 then it would have passed the
24 DSAC test for the whole period."

25 A Yes, that's true, and it could have increased it by less than it did, and passed the DSAC test.

26 Q Sir, I am very conscious of the time, and I think I probably need to stop there.

27 THE PRESIDENT: Have you obtained those two pricing papers that you wanted to look at?

28 MR. READ: Sir, I did not get long to look at it over the short adjournment, but I think I may have
29 been putting the question on a slightly unfair basis because I do not think in BT's 20th April
30 2012 response the BES paper was specifically referred to. So although Ofcom had the
31 paper, it was not one being specifically relied upon by BT. Therefore, I do not think it
32 would be fair to Mr. Myers to put it on that basis. It was something I noticed in the
33 Determination, but I think having gone back and reflected on it, it may not be a completely
34 fair point to have been putting against Ofcom.

1 THE PRESIDENT: So you are not pursuing that point?
2 MR. READ: So I am not going to pursue it.
3 THE PRESIDENT: Very well. So you have concluded your cross-examination. We have had a
4 request to add someone else from Frontier Economics to the confidentiality ring. As I
5 understand it, there is no objection to that.
6 MR. THOMPSON: It has been agreed by all parties.
7 THE PRESIDENT: So I shall make that order accordingly. Mr. Pickford you had been promised
8 half an hour today which you have not had so we will start at 9.30 tomorrow. Could
9 someone please notify Ms. Rose of that. Mr. Pickford, as it is at your request, you can have
10 the obligation of giving her that, no doubt, welcome news. You will need to conclude by 3
11 o'clock, Mr. Pickford, so that there can be re-examination and questions from the Tribunal,
12 and that is an outside limit. You are only dealing, as I understand it, with the FAC issue, is
13 that right?
14 MR. PICKFORD: That is not correct, no. I am going to be dealing with the RAV issue as well.
15 THE PRESIDENT: The RAV issue also, I see.
16 MR. PICKFORD: Sir, before we rise, because I was going to get to my feet today I was going to
17 give a clip of documents to Mr. Myers. I have not done so but I am very happy for him to
18 have them overnight.
19 THE PRESIDENT: That is sensible because he can look at them rather than trying to absorb
20 them in the witness box. (Same handed)
21 MR. PICKFORD: Probably if we put them into the AD 2 tab 39
22 THE PRESIDENT: You can keep them out, Mr. Myers, because you can take them home and
23 familiarise yourself with what is in them. So we will resume at 9.30 and take a 15 minute
24 break in the course of the morning to give Mr. Myers a break. As you know, you cannot
25 discuss the case overnight. So 9.30 tomorrow morning.
26 (Adjourned until 9.30 a.m. on Friday, 15th November 2013)