



Neutral Citation No. [2024] CAT 76

Case Number: 1381/7/7/21

**IN THE COMPETITION APPEAL TRIBUNAL**

**19 December 2024**

Salisbury Square House  
8 Salisbury Square  
London EC4Y 8AP

**Before:**  
**THE HONOURABLE MR JUSTICE WAKSMAN**  
**(Chair)**  
**EAMONN DORAN**  
**DEREK RIDYARD**  
**Sitting as a Tribunal in England and Wales**

**BETWEEN:**

**JUSTIN LE PATOUREL**

Class Representative

and

**(1) BT GROUP PLC**

**(2) BRITISH TELECOMMUNICATIONS PLC**

Defendants

and

**COMPETITION AND MARKETS AUTHORITY**

Interested Party

**NON-CONFIDENTIAL REDACTED JUDGMENT**

**Hearing dates:** 29-31 January, 1, 5-8, 12-15, 19, 20-22, and 26-29 February, 1, 4-5, and 18-22 March 2024

**Representation:**

**Ronit Kreisberger KC, Derek Spitz, Michael Armitage, Jack Williams and Matthew Barry**  
(instructed by Mishcon de Reya LLP, Solicitors) for the Class Representative

**Daniel Beard KC, Daisy Mackersie, Natalie Nguyen, Sarah Love and Ali Al-Karim** (instructed by Simmons & Simmons LLP, Solicitors) for the Defendants

**Jennifer MacLeod** (instructed by the CMA Legal Department) for the CMA

## Table of Contents

<b>INTRODUCTION.....</b>	<b>7</b>
<b>BACKGROUND.....</b>	<b>8</b>
<b>THE DAMAGES SOUGHT .....</b>	<b>10</b>
<b>THE CORE ISSUES .....</b>	<b>10</b>
LIABILITY ISSUES .....	10
QUANTUM ISSUES .....	11
<b>THE PARTIES' SUBMISSIONS.....</b>	<b>11</b>
<b>THE EVIDENCE .....</b>	<b>12</b>
LAY WITNESSES .....	12
EXPERTS.....	12
DOCUMENTARY EVIDENCE AND GLOSSARY.....	14
<b>THE LAW – THE GENERAL POSITION .....</b>	<b>15</b>
INTRODUCTION: <i>UNITED BRANDS</i> .....	15
PHENYTOIN .....	16
ALBION WATER II.....	20
LIOETHYRONINE.....	23
HYDROCORTISONE .....	23
OTHER CASES AND MATTERS.....	25
UNFAIRNESS BY COMPARISON .....	26
THE RELEVANCE OR OTHERWISE OF REGULATION .....	28
THE EFFECT AND SIGNIFICANCE OF OFCOM'S 2017 PROVISIONAL CONCLUSIONS AND STATEMENT .....	29
PRICES AND MARGINS ON THE UNDERTAKING'S OTHER PRODUCTS.....	31
BURDEN AND STANDARD OF PROOF .....	31
<b>FACTUAL MATTERS (1): BT'S MARKET SHARE.....</b>	<b>32</b>
BACKGROUND AND THE BASICS OF BT'S PRICING .....	34
LINE RENTAL PRICING .....	35
CALL CHARGES.....	39
ARPU .....	39
GROSS MARGIN.....	41
<b>FACTUAL MATTERS (2): OFCOM AND BT.....</b>	<b>43</b>
BACKGROUND .....	43
2006.....	43
2009.....	44
2013.....	44
2014.....	44
2015.....	44
2016.....	45
2017.....	45
2020 AND 2021.....	48
<b>FACTUAL MATTERS (3): SWITCHING.....</b>	<b>49</b>
<b>FACTUAL MATTERS (4): BT'S PERCEPTIONS AS TO LINE RENTAL INCREASES AND SWITCHING.....</b>	<b>55</b>
INTRODUCTION.....	55
THE IMMEDIATE PURPOSE OF BT'S LINE RENTAL INCREASES.....	55
<b>MARKET DEFINITION.....</b>	<b>59</b>
INTRODUCTION.....	59
THE BASIC APPROACH .....	59
THE SSNIP TEST.....	60
THE CELLOPHANE FALLACY .....	61

PRICE DISCRIMINATION.....	62
THE RELEVANCE OF SWITCHING .....	62
REASONS FOR SWITCHING .....	63
<i>The Possibility of Secular Trend</i> .....	63
<i>Gradual and consistent decline in SFV Customers</i> .....	64
<i>Price Increase in face of declining SFV customer base</i> .....	67
<i>Dr Jenkins' Evidence on Secular Trend</i> .....	67
<i>Dr Jenkins' Event Study on the Commitments Price Reduction</i> .....	68
<i>BT's own perception as to reasons for switching</i> .....	69
<i>Competition from the Post Office</i> .....	80
<i>Conclusion</i> .....	80
SUMMARY OF MR PARKER'S APPROACH .....	80
<i>SPC-Dual play bundle price differential</i> .....	80
<i>Line Rental Price Increases</i> .....	80
<i>Call Price Increases</i> .....	81
SUMMARY OF DR JENKINS' APPROACH.....	81
<i>Switching per se</i> .....	81
<i>Dr Jenkins' Critical Loss Analysis ("CLA")</i> .....	81
<i>Bundles as constraints on SFV Pricing</i> .....	81
ANALYSIS: MR PARKER'S APPROACH.....	81
<i>Mr Parker's use of BT price data</i> .....	81
<i>Mr Parker's SPC-Bundle Price Differential</i> .....	87
<i>Line Rental Price Increases</i> .....	96
<i>Call Price Increases</i> .....	99
ANALYSIS: DR JENKINS' APPROACH .....	102
<i>Switching per se</i> .....	102
<i>CLA</i> .....	103
<i>Bundles as Constraints on SFV Pricing</i> .....	111
CONCLUSION ON MARKET DEFINITION .....	115
<b>DOMINANCE .....</b>	<b>115</b>
THE LAW.....	115
MARKET SHARE .....	116
OTHER FACTORS GOING TO DOMINANCE .....	117
<i>Barriers to Expansion</i> .....	117
<i>The Position of the Post-Office</i> .....	118
<i>Constraints from Bundles</i> .....	119
<i>Price Leadership</i> .....	120
CONCLUSION ON DOMINANCE.....	122
<b>LIMB 1 METHODOLOGIES: DESCRIPTION.....</b>	<b>122</b>
INTRODUCTION.....	122
MR DUCKWORTH'S METHODOLOGY .....	126
DR JENKINS' METHODOLOGY .....	131
<i>Derivation of BT Consumer Common and Incremental Costs</i> .....	131
<i>SAC Combi</i> .....	133
<i>DSAC Cross-Check</i> .....	137
<i>Dr Jenkins' Sensitivities</i> .....	138
<i>Comparative Tables</i> .....	138
<b>REASONABLE MARGIN .....</b>	<b>140</b>
INTRODUCTION.....	140
THE LAW ON REASONABLE MARGIN.....	141
MR DUCKWORTH'S APPROACH.....	141
<i>BT's Reported Margins 2004-2006</i> .....	141
<i>Mr Duckworth's Comparators</i> .....	143
<i>Ofcom's 2017 Provisional Conclusions and a 10% margin</i> .....	145
DR JENKINS' ANALYSIS .....	149
<i>The Upper Bounds Point</i> .....	149
<i>Dr Jenkins' comparators</i> .....	151
CONCLUSION ON REASONABLE MARGIN .....	156
<b>LAW ON COMBINATORIAL AND OTHER TESTING - PPC .....</b>	<b>156</b>

<b>ANALYSIS OF THE RFS METHODOLOGY .....</b>	<b>161</b>
INTRODUCTION.....	161
OBJECTION AS A MATTER OF PRINCIPLE TO THE RFS MODEL AS AN APPROPRIATE WAY OF CALCULATING A COMPETITIVE BENCHMARK AS AT 2009 .....	161
<i>Use of an FAC model.....</i>	162
<i>The Regulatory Purpose of the RFS.....</i>	166
OBJECTIONS TO THE USE OF THE RFS METHODOLOGY IN RESPECT OF THE CLAIM YEARS.....	167
Introduction .....	167
The use of “actual data” .....	167
Legal Certainty .....	169
Use of the CPI Index and reported indirect costs before and as at 2009 .....	169
Indirect Costs Data from 2015/16 going forward .....	172
Particular cost events that might affect common costs .....	176
Changes in call pricing and competition .....	176
Economies of scope and size of common costs .....	176
Economies of Scale .....	177
Different Cost allocations in the claim years.....	178
Likely Size of Common Costs BT Consumer.....	180
CONCLUSIONS ON THE RFS METHODOLOGY.....	184
<b>ANALYSIS OF DR JENKINS’ METHODOLOGY .....</b>	<b>184</b>
INTRODUCTION.....	184
DR JENKINS’ DERIVATION OF THE COMMON COSTS OF BT CONSUMER.....	185
<i>The Relevant Figures.....</i>	185
<i>Dr Jenkins’ Primary Approach.....</i>	186
<i>VULA Margin .....</i>	188
<i>The TSO Cross-check .....</i>	190
<i>Conclusion on BT Consumer Common Costs .....</i>	192
THE SAC COMBI EXERCISE.....	192
Insufficient number of combinations.....	192
The “Number of Lines Error” .....	197
Conclusions on Dr Jenkins’ SAC Combi methodology.....	199
<b>DR JENKINS’ DSAC CROSS-CHECK .....</b>	<b>200</b>
<b>DR JENKINS’ FAC ANALYSIS .....</b>	<b>203</b>
<b>OVERALL CONCLUSION ON THE COMPETITIVE BENCHMARK .....</b>	<b>207</b>
INTRODUCTION.....	207
2015/2016.....	208
<i>The Common Costs Starting Point.....</i>	208
<i>The SFV Services Common Costs Contribution .....</i>	209
<i>Application of Margin.....</i>	211
<i>Resulting Figure for 2015/16.....</i>	211
THE FOLLOWING YEARS TO 2021/22.....	211
OVERALL CONCLUSION ON LIMB 1 FIGURES.....	214
<b>LIMB 2 (1): UNFAIRNESS “IN AND OF ITSELF” .....</b>	<b>214</b>
INTRODUCTION.....	214
<i>The CR’s case .....</i>	214
<i>BT’s case.....</i>	215
<i>The Tribunal’s analysis .....</i>	217
EXTENT OF THE EXCESS .....	217
PROVISION OF ECONOMIC VALUE: (A) GENERALLY .....	218
Introduction .....	218
<i>The Extent or Level of Economic Value Required .....</i>	218
<i>The Relevance of the ability to switch (or not) .....</i>	218
PROVISION OF ECONOMIC VALUE: (B) GIVES.....	219
Onshoring of Customer Call Centres .....	220
Call Protect.....	221
Care Level 2/Fault Fix Guarantee.....	224
Right Plan.....	226

<i>Caller Display</i> .....	227
<i>Other Points about the Gives</i> .....	228
<i>Conclusions on the Gives</i> .....	231
PROVISION OF ECONOMIC VALUE: (C) BRAND VALUE .....	231
<i>Introduction</i> .....	231
<i>What are NPS?</i> .....	231
<i>Use of BT's NPS documents at trial</i> .....	232
<i>Survey Base for NPS documents</i> .....	234
<i>Particular NPS documents</i> .....	235
<i>Conclusions on the NPS documents</i> .....	238
<i>Ofcom Materials</i> .....	239
<i>Introduction</i> .....	239
<i>2016 Switching Tracker Data</i> .....	239
<i>Comparison Documents</i> .....	239
<i>2016 – 2022 Switching Tracker Data</i> .....	241
<i>Analysis</i> .....	241
PROVISION OF ECONOMIC VALUE: (D) ABILITY OF CUSTOMERS TO SWITCH .....	243
<i>Conclusions on Brand Value</i> .....	249
PROVISION OF ECONOMIC VALUE: (E) CONCLUSIONS .....	250
WORKABLE COMPETITION FACTORS.....	250
<i>Introduction</i> .....	250
<i>Price Dispersion</i> .....	251
<i>Cost Efficiencies Dispersion</i> .....	253
EXISTENCE OR OTHERWISE OF EXPLOITATION BY BT OVER ITS PRICE INSENSITIVE CUSTOMERS (“THE EXPLOITATION POINT”) .....	255
<i>Introduction</i> .....	255
<i>Price insensitivity of SFV customers</i> .....	255
<i>BT sought to maximise value from a declining market and regular price increases</i> .....	255
<i>No price competition from competitors</i> .....	256
<i>Conclusions</i> .....	257
DISPROPORTIONATE IMPACT OF PRICE INCREASES ON SFV CUSTOMERS (“THE DISPROPORTIONATE IMPACT POINT”).....	257
PRICE RISE REVENUE USED TO FUND NON-SFV INVESTMENTS (“THE NON-SFV INVESTMENTS POINT”).....	259
LACK OF TRANSPARENCY (“THE LACK OF TRANSPARENCY POINT”) .....	260
<i>Customers</i> .....	260
<i>The Press</i> .....	260
<i>Ofcom</i> .....	261
<i>Conclusions</i> .....	265
EFFECT OF THE EXPLOITATION, DISPROPORTIONATE IMPACT, NON-SFV INVESTMENTS AND LACK OF TRANSPARENCY POINTS .....	265
PRICE RISES DURING PERIOD WHEN OFCOM EXPRESSING CONCERN .....	266
MARKET DYNAMICS .....	268
<i>Migration Intent</i> .....	268
<i>Rebalancing</i> .....	268
<i>Conclusion on Market Dynamics</i> .....	271
THE SIGNIFICANCE OR OTHERWISE OF OFCOM’S 2017 PROVISIONAL CONCLUSIONS AND STATEMENT.....	271
CONCLUSION ON UNFAIRNESS IN AND OF ITSELF.....	273
<b>LIMB 2 – (2) UNFAIRNESS BY COMPARISON .....</b>	<b>273</b>
INTRODUCTION.....	273
COMMITMENTS PRICING.....	274
THE POST OFFICE .....	275
THE PRICING OF BT’S RIVALS .....	275
HPS.....	276
BT’S BUSINESS TARIFF .....	277
CONCLUSION ON UNFAIRNESS BY COMPARISON.....	277
<b>ALTERNATIVE CASE BASED ON LINE RENTAL PRICE ONLY .....</b>	<b>277</b>
<b>OVERALL CONCLUSION ON LIABILITY .....</b>	<b>277</b>
<b>QUANTUM (1): BASIS OF OVERCHARGE .....</b>	<b>278</b>
<b>QUANTUM (2): BUSINESS CUSTOMERS .....</b>	<b>280</b>

INTRODUCTION.....	280
THE EXCLUSION ISSUE .....	280
THE PROPORTION ISSUE .....	283
THE PASS-ON ISSUE .....	286
<b>QUANTUM (3): BT EMPLOYEES WITH GIFTED SERVICES .....</b>	<b>286</b>
<b>QUANTUM (4): DECEASED CLASS MEMBERS.....</b>	<b>287</b>
INTRODUCTION.....	287
THE MORTALITY QUESTION.....	288
THE PERSONAL REPRESENTATIVE QUESTION.....	290
<i>Introduction</i> .....	290
<i>Rate of will-writing</i> .....	291
<i>The 20% adjustment</i> .....	294
<b>QUANTUM (5): INTEREST AND RELATED MATTERS .....</b>	<b>296</b>
INTRODUCTION.....	296
INFLATION.....	296
COMPOUND INTEREST .....	298
CALCULATION OF SIMPLE INTEREST .....	300
<b>OVERALL CONCLUSION .....</b>	<b>300</b>

## **INTRODUCTION**

1. This case concerns a claim against two Defendants, BT Group Plc and British Telecommunications Plc (collectively “BT”). The claim is that BT has abused its dominant position in a telecommunications (“telecoms”) market by imposing unfair prices, contrary to section 18 of the Competition Act 1998 (“the Act”). The claim is brought by Mr Justin Le Patourel as the Class Representative (“the CR”) in respect of approximately 2.3m affected BT customers.
2. The market is concerned with the provision of landline telephone services to residential addresses known as Standalone Fixed Voice Services (“SFV Services”). These are provided in circumstances where the customer contracts with BT for access to the telephone network for voice calls only. The charges consist of a fixed line rental charge and a variable charge for calls made.
3. Within the provision of SFV Services there are, according to the CR, two customer groups. The first consists of Voice Only Customers (“VOCs”). A VOC buys an SFV service and does not buy a broadband service from either the same or any other provider. As at 2019, there were 1.2m such customers, representing about 5% of total residential customers. The second customer group encompasses Split Purchase Customers (“SPCs”). As at 2019, there were 1.1m SPCs. Such customers also take a broadband service pursuant to a separate contract, either with BT or with some other provider. What they do not have is a “bundle”, i.e. a package of telephone and broadband services provided together by the same supplier under one contract. The market for bundles, comprising voice and broadband, and which the CR says is separate from the SPC market, is known in the industry as “Dual Play” (“DP”). There are also several other bundles sold alongside voice by BT and others, including services such as TV, mobile etc.
4. On 15 January 2021, Mr Le Patourel issued a claim form in which he applied for a collective proceedings order (“CPO”) in respect of the claim referred to above. Following a hearing which took place on 24 and 25 June 2021, and a judgment handed down on 27 September 2021 ([2021] CAT 30), the Tribunal made a CPO on 19 October 2021. By that order, and pursuant to section 47B of the Act and Rules 77 and 80 of the Competition Appeal Tribunal Rules, Mr Le Patourel was authorised to act as the CR to continue collective proceedings on an opt-out basis claiming damages for loss suffered by the Class (as defined below). The remedy sought is an award of aggregate damages for the Class pursuant to section 47C(2) of the Act, together with interest, costs and any further or other relief as the Tribunal may think fit.
5. The details of the class and claim period were set out in the CPO as follows:

“The Class shall be defined as: “all persons domiciled in any part of the United Kingdom (except in the **Hull Area**) – or their UK-domiciled personal representatives – who, during the **Claim Period**, bought a **BT Standalone Fixed Voice Service** except for the **Excluded Services** (referred to below as “**the Class Members**”)”, whereby:

(a) **BT Standalone Fixed Voice Service** means any residential landline calling plan service provided by BT, except for the Excluded Services, which (i) includes landline line rental and (ii) has not been sold as part of a bundle with broadband. For these purposes, a bundle refers to a contract, or two or more closely related, linked or interdependent contracts which, individually or together, include and require the purchase of broadband as well as the landline calling plan service.

(b) **Excluded Services** means BT Basic and BT Home Phone Saver.

(c) **Hull Area** means the area defined as the Licence Area in the licence granted on 30 November 1987 by the Secretary of State under Section 7 of the Telecommunications Act 1984 to Kingston upon Hull City Council and Kingston Communications (Hull) plc.

(d) The **Claim Period** means:

(i) for residential BT Voice Only Customers, between 1 October 2015 and 1 April 2018 inclusive;

(ii) for business BT Voice Only Customers, between 1 October 2015 and the date of the Tribunal's final determination of the Claims made by the Sub-class of BT Voice Only Customers or their earlier settlement (or settlement of any part thereof); and

(iii) for BT Split Purchase Customers, between 1 October 2015 and the date of the Tribunal's final determination of the Claims made by the Subclass of BT Split Purchase Customer or their earlier settlement (or settlement of any part thereof)."

6. By the same order, the Tribunal dismissed an application by BT, made on 30 April 2021, to strike out or summarily dismiss the claim. By a judgment handed down on 6 May 2022, the Court of Appeal dismissed BT's appeal against the making of the CPO ([2022] EWCA Civ 593).
7. All the relevant notifications and other procedural steps required of the CR in pursuance of the CPO have been taken.
8. The latest iteration of the claim is to be found in the Re-Re-Re-Re-Amended Claim Form dated 11 December 2023, followed by the Re-Re-Amended Defence dated 15 December 2023 and the Re-Re-Amended Reply dated 21 December 2023.
9. What follows is the Tribunal's unanimous judgment on the substantive claim.

## **BACKGROUND**

10. The immediate background to the making of the claim, and a matter relied upon (among other things) by Mr Parker, the expert economist retained by the CR, who produced two reports in support of the claim, dated 13 January and 26 May 2021 ("DP1" and "DP2" respectively) was a review of BT's pricing for the two relevant groups of customers, namely VOCs and SPCs, by the Office of Communications ("Ofcom"). It is necessary at this stage to give a summary of Ofcom's intervention and the consequences of it. However, there is an issue between the parties as to the relevance, admissibility and (if admissible) the weight to be attached to the Ofcom findings in this regard. The making of the summary below is without prejudice to that issue which we determine later in the judgment.



11. The background to that intervention, so far as Ofcom was concerned, was that when BT was privatised in 1984, it was subject to retail price control, continuing until 31 July 2006, and released from it as from 1 August 2006. However, although BT was released from such price control, it was not fully deregulated because Ofcom still considered that BT had “significant market power” (“SMP”) in the relevant markets. Ofcom therefore still did not permit BT to compete freely within the bundles market. That restriction was removed by Ofcom’s decision dated 15 September 2009.
12. There are various other Ofcom reviews and decisions which followed, and which will be referred to below. However, in its “Review of the Market for Standalone Landline Telephone Services: Provisional Conclusions” dated 28 February 2017 (“the 2017 Provisional Conclusions”), Ofcom set out proposals to address the concerns which it had by that stage about the standalone telephone services market and BT’s pricing therein. These were then open for a consultation period ending on 9 May 2017.
13. At this stage, the proposal to cut the line rental price applied to both VOCs and SPCs, which Ofcom then considered were in the same market.
14. On 24 October 2017 BT put forward a voluntary proposal to Ofcom. This included, for VOCs but not SPCs, a line rental reduction of £7 per month as from 1 April 2018 and thereafter raising the price of calls and line rental by no more than inflation each year. It also proposed an improvement in the information made available to such customers to make them more aware of potential savings. For SPCs, BT proposed to stimulate engagement by issuing an annual statement showing their total spend which should help them consider what alternatives were available for voice-only services in conjunction with broadband services. We refer to the above proposals as “the Commitments”.
15. Following consideration of the consultation responses and further market research, along with BT’s proposals, Ofcom produced its “Review of the Market for Standalone Landline Telephone Services: Statement” on 26 October 2017 (“the 2017 Statement”). This consisted of its final conclusions, together with its 2017 Provisional Conclusions. In it, Ofcom accepted the Commitments in place of making any binding decision of its own.
16. Following a consultation launched in 2020, aimed at reviewing the performance of the BT Commitments to date, Ofcom published its “Statement in its Consultation on Protecting voice-only landline telephone customers” on 25 March 2021 (“the 2021 Statement”). In it, Ofcom accepted a renewed BT Commitment with price increases for VOCs limited to inflation and in any event within a safeguard cap of 2.5% of the price of line rental. This commitment would last 5 years. The existing commitment in respect of SPCs continues as before.

17. It will be seen from the terms of the CPO that the claim in respect of VOCs is for a three-year period, which ends with the commencement of the Commitments on 1 April 2018. For reasons of limitation, that period does not start any earlier than 1 October 2015. The claim in respect of the SPCs runs up until the determination of it by this Tribunal, since they were not the subject of the Commitments.

### **THE DAMAGES SOUGHT**

18. The damages claimed are presently quantified up to 31 March 2022. The total, inclusive of VAT and compensating for inflation, but before interest, is about £1,101m. This is made up of £430m for VOCs and £671m for SPCs. Interest is then claimed on a compound basis up to December 2022, which would increase the total damages claimed to £1,307m. If simple interest were added instead, the total claim would be around £1,278m. There are various significant issues between the parties on quantum.
19. The total number of claimants is a maximum of 3.8m. This will include customers who were in one of the two sub-classes at some point within the relevant claim period, even if they were not customers at the beginning and/or not customers at the end. Of that total of 3.8m, and before any adjustments for death and intestacy and before taking account of any of the other quantum points, 1.8m members of the Class were VOCs and 2m members of the Class were SPCs. The precise number of Class Members for each year, and which members were VOCs or SPCs, is now agreed.
20. There is an alternative claim in damages, which is less than the principal claim. It is based on excessive and unfair prices for access only, i.e. line rental.
21. Although there are two sub-classes, namely VOCs and the SPCs, the CR's claim is in respect of both of them, with no alternative claim for just one of them. In other words, the claim is made on an "all or nothing" basis.

### **THE CORE ISSUES**

22. These are set out below.

#### **Liability Issues**

23. Both sides accept that there are four key stages in the analysis of the CR's claim that BT has abused its dominant position, which can be framed as follows:
- (1) Market Definition: is there a distinct market consisting of the supply of SFV Services only as opposed to some wider market, in particular one including bundles?
  - (2) Dominance: if so, is BT dominant in that market?
  - (3) Excessive pricing (Limb 1): if so, did BT charge prices for its SFV Services to the VOCs and SPCs over the claim period which were excessive?

- (4) Unfairness (Limb 2): if so, were such excessive prices unfair and thereby abusive?
24. It follows that if the answer to any one of those questions is “No”, the CR’s claim must fail.
25. The references to Limbs 1 and 2 are, of course, to the analysis contained in the judgment of the CJEU in *United Brands v European Commission* [1978] 1 C.M.L.R. 429, which the parties described as “seminal”. The case itself is dealt with below. All of the economic experts, as well as the parties’ submissions, addressed these four questions separately, and in that order.

### **Quantum Issues**

26. These are as follows:
- (1) Failure to Mitigate: did the Class fail to mitigate its loss by failing to switch to alternative providers or other suitable BT tariffs, including bundles?
  - (2) Basis of Overcharge: the approach to the amount of overcharge, as a matter of principle;
  - (3) The size of the Class:
    - (a) Business customers who purchased SFV Services: should they be excluded from the Class?
    - (b) Class Members who were gifted broadband: should they be included?
    - (c) Class Members who are deceased without personal representation: it is agreed that they should be excluded from the Class, and the question is how many there are;
  - (4) Interest and inflation:
    - (a) Inflation: should damages be uprated to take inflation into account?
    - (b) Compound Interest: should compound interest be awarded as damages for loss of use of monies?
    - (c) Simple Interest: how much should be awarded by way of simple interest?

### **THE PARTIES’ SUBMISSIONS**

27. The CR and BT each produced detailed opening submissions on 10 and 17 January 2024 respectively (“Openings”) and lengthier, detailed closing submissions on 12 March 2024 with various Appendices (“Closings”). The latter were followed by oral closing submissions. We also have the benefit of two sets of submissions from the Competition and Markets Authority (“CMA”), whom we permitted to intervene, filed on 29 July 2022 (“CM1”) and 14 November 2023 (“CM2”). Counsel for the CMA did not take part in the trial, save to make some brief opening submissions.
28. We should add that, at various stages during the trial, the parties helpfully produced further materials, sometimes in agreed letters and sometimes in the form of further diagrams, tables or spreadsheets.

29. In this judgment, we have not dealt specifically with every single point or argument made by the parties or every single piece of evidence. Had we attempted to do so, this would, in the words of Teare J in *The Suez Fortune* [2019] EWHC 2599 (Comm) at paragraph 26, have resulted in a judgment of “intolerable length”. This is in the context of a case where, apart from the weeks of expert evidence, together with lay evidence, there were in total over 660 pages of detailed written submissions, with over 3,600 footnotes, dealing with references and other matters, and 5 days of closing arguments. While all of that has been considered by us, what we have done in the judgment is to deal with the parties’ key points, and the key materials, on all matters. It is neither necessary nor appropriate to do more.

## **THE EVIDENCE**

### **Lay Witnesses**

30. For the CR, there were no lay witnesses.
31. For BT, there were the following lay witnesses, all of whom gave oral evidence:
- (1) Jonathan Bunt, the present Director of Regulatory affairs for the BT Consumer Business Unit, who has produced 3 witness statements (“WSs”) dated 29 April 2021, 23 February and 3 August 2023 (“JB1, JB2, and JB3”);
  - (2) Margaret Blight, the present Start-up Partnerships Director employed by BT, who produced one WS dated 23 February 2023 (“MB1”);
  - (3) Deirdre Cheek, the current principal of Regulatory Affairs within the Regulatory Team of BT Group. She produced one WS dated 18 February 2023 (“DC1”), and
  - (4) Richard Cackett, the current Director of Commercial Finance at BT Consumer. He produced one WS dated 23 February 2023 (“RC1”).
32. We accept that all the BT witnesses were doing their best to assist the Tribunal. Occasionally, a witness took some time to answer a question or appeared not to be entirely objective, but this is not a case where we would conclude that any witness’s evidence was simply implausible or not credible as a whole. Nor is this a case where some key primary fact turned exclusively or mainly on witness evidence. Where we perceived a difficulty with a witness’s evidence which was relevant, we will refer to it in context, below.

### **Experts**

33. There were the following expert witnesses for the CR, all of whom gave oral evidence:
- (1) David Parker, an economist with the consultancy Frontier Economics Limited and latterly Berkeley Research Group (BRG) which specialise in micro economic analysis. In addition

to DP1 and DP2 (see above), he has produced 3 further reports, DP3, DP4 and DP5, dated 29 September 2023, 10 November 2023 and 8 February 2024 respectively;

- (2) Martin Duckworth, an economist also with Frontier Economics Limited, who has produced reports dated 29 September and 10 November 2023 (“MD1 and MD2”);
- (3) Prof. Graham Loomes, a behavioural economist and Professor of Behavioural Science at Warwick Business School; he has produced 2 reports dated 7 September and 10 November 2023 respectively (“GL1 and GL2”); and
- (4) Jonathan Punter, a consulting actuary with the firm Punter Southall, who has produced 3 reports dated 29 September, 10 November and 28 November 2023 (“JP1, JP2 and JP3”) together with a supplemental note dated 6 October 2023.

34. The expert witnesses for BT, all of whom gave oral evidence, were as follows:

- (1) Dr Helen Jenkins, an economist who specialises in empirical microeconomics, and a partner of Oxera Consulting LLP. She has produced 3 reports, dated 29 September and 10 November 2023 and 11 February 2024 (“HJ1, HJ2 and HJ3”);
- (2) David Matthew, an economist who is Managing Director of NERA Economic Consulting. He has produced 2 reports, dated 29 September and 10 November 2023 (“DM1 and DM 2”);
- (3) Dr Stephan Hunt, an economist and partner at Keystone Europe Limited, a consultancy specialising in microeconomics strategy and technology analysis. He has produced one report dated 29 September 2023 (“SH1”); and
- (4) Bob Scott, an actuary and Senior Partner in Lane Clark and Peacock LLP, a firm of consultants and actuaries (“BS1”).

35. The economic experts produced a joint statement on 15 December 2023 (“the JES”). The behavioural economists produced a joint statement on 14 December 2023 (“the Behavioural JES”), and the actuarial experts produced a joint statement on 15 December 2023 (“the Actuarial JES”).

36. The issues which the various experts evidence addressed are set out in the table below, using the expert’s initials.

Issue	CR expert	BT expert
Market definition	DP	HJ
Dominance	DP	HJ
Excessive Pricing – Limb 1	DP, MD	HJ, DM
Abuse – Limb 2	DP, GL	HJ, DM, SH
Deceased members without PRs	JP	BS

Members with gifted broadband and Business Customers	DP	HJ
--	----	----

37. We did face some difficulties with the economic expert evidence. This is because, in the case of many areas of dispute, the methodologies employed by each of the opposing experts were quite different. Perhaps because of this, at various points each party submitted that the other party's line of analysis should be rejected entirely. As will be seen, for the most part, we did not rule out a line of reasoning as simply illegitimate *per se* but rather took account of possible defects so that our approach then blended the outcomes of the various models so to reach the appropriate outcome. Sometimes, for example with Dr Jenkins, she would produce a set of alternative outcomes or "sensitivities" which represented what, for her, was a more "conservative" outcome than her primary outcome. This, at least, gave us some alternative views to consider. In addition, on occasion, each side's experts would "run" the other side's expert's analysis to see if it altered their outcome or not. Finally, and at our request, both sides produced alternative analyses using different figures for the purpose of the Limb 1 exercise. Here, that produced by the CR contained somewhat more variables than that produced by BT. All of this was useful, but it did not remove entirely the need, as we saw it, to consider outcomes that were not directly the product of either side's approach. This is perhaps inevitable in cases of this kind where sets of figures, percentages and comparisons are so important and which are therefore highly fact and expert opinion sensitive.
38. As for the experts themselves, as with BT's lay witnesses, this is not a case where one side's expert can be criticised as generally lacking credibility or relevant experience. All of the experts, but particularly Mr Parker and Mr Duckworth for the CR, and Dr Jenkins for BT, are highly experienced, both in their fields and in giving evidence to tribunals such as this. On occasion, all of them could be said to have strayed into arguing their case and losing objectivity, or speculating. In general however, the experts did their best to assist us. The economic experts had to deal with our numerous questions for each of the hot tub sessions (which we notified in advance) as well as cross-examination, and the ground they covered was very extensive, as will be made clear below. Their professional and constructive approach to these exchanges during the hearing, even on matters where they disagreed with one other, greatly assisted us in reaching our conclusions on the core economic issues. We should add that we found the JES a particularly useful document.

### **Documentary Evidence and Glossary**

39. As might be expected in a case of this kind there is a substantial volume of documents. Most are BT internal documents. A large number were put to witnesses, but there was a further number which were only referred to in the parties' submissions, principally their Closings. We refer to many

internal documents below, but are conscious of the fact that, on various occasions, both sides referred to them selectively, and we have borne this in mind.

40. The other main repository of documentary references is the material produced by Ofcom. We refer to that, and its significance or otherwise, below.
41. Further, and in the light of the very many technical terms and acronyms used in the evidence and documents, we append to this judgment a Glossary. This is not agreed as such, but it is one which we have derived from the Agreed Glossary dated 13 February 2024; for the most part the changes are to add items or to delete items which are unnecessary.

## **THE LAW – THE GENERAL POSITION**

### **Introduction: *United Brands***

42. Section 18 of the Act provides:

“Abuse of dominant position...

(1) Subject to section 19, any conduct on the part of one or more undertakings which amounts to the abuse of a dominant position in a market is prohibited if it may affect trade within the United Kingdom.

(2) Conduct may, in particular, constitute such an abuse if it consists in— (a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions;....”

43. At paragraph 56 of his judgment in the Court of Appeal in *CMA v Flynn Pharma Ltd* [2020] EWCA Civ 339 (“*Phenytol*”), Green LJ (with whom Sir Geoffrey Vos C (as he then was) and Sir Stephen Richards agreed) said that the starting point for a claim based on unfair pricing is the judgment of the CJEU in *United Brands*., which all parties there described as “seminal”. Paragraphs 248–254 thereof read as follows:

[248] The imposition by an undertaking in a dominant position directly or indirectly of unfair purchase or selling prices is an abuse to which exception can be taken under Article 86 of the Treaty.

[249] It is advisable therefore to ascertain whether the dominant undertaking has made use of the opportunities arising out of its dominant position in such a way as to reap trading benefits which it would not have reaped if there had been normal and sufficiently effective competition.

[250] In this case charging a price which is excessive because it has no reasonable relation to the economic value of the product supplied is such an abuse.

[251] This excess could, inter alia, be determined objectively if it were possible for it to be calculated by making a comparison between the selling price of the product in question and its cost of production, which would disclose the amount of the profit margin; however the Commission has not done this since it has not analysed UBC's costs structure.

[252] The question therefore to be determined is whether the difference between the costs actually incurred and the price actually charged is excessive and, if the answer to this question is in the affirmative, to consider whether a price has been imposed which is either unfair in itself or when compared to competing products.

[253] Other ways may be devised-and economic theorists have not failed to think up several-of selecting the rules for determining whether the price of a product is unfair.

[254] While appreciating the considerable and at times very great difficulties in working out production costs which may sometimes include a discretionary apportionment of indirect costs and general expenditure and

which may vary significantly according to the size of the undertaking, its object, the complex nature of its set up, its territorial area of operations, whether it manufactures one or several products, the number of its subsidiaries and their relationship with each other, the production costs of the banana do not seem to present any insuperable problems.”

44. Both parties, and indeed the Tribunal in this case, have referred to the two questions raised in paragraph 252 of *United Brands* as “Limb 1” and Limb 2”. Limb 1 considers whether the price is excessive and if so, Limb 2 considers whether it is unfair either in itself or when compared to competing products. We noted this at paragraph 25 above.
45. The *United Brands* test has of course been considered in many cases. For our purposes, there are the following key English authorities which all deal with excessive pricing:
- (1) The decision of the Court of Appeal in *Phenytoin*;
  - (2) The decision of the Tribunal in *Albion Water Ltd v Water Services Regulation Authority and United Utilities Water plc* [2008] CAT 31 (“*Albion Water IP*”);
  - (3) The decision of the Tribunal in *Hg Capital LLP v CMA* [2023] CAT 52 (“*Liothyronine*”) and
  - (4) The decision of the Tribunal in *Allergan plc v CMA* [2023] CAT 56 (“*Hydrocortisone*”)
46. We set out below the principal points to be derived from those four cases, making reference to other case-law where appropriate, and then deal with some further, specific matters.
47. Above and beyond stating the general principles which are applicable, we have avoided detailed consideration of particular areas of law where the parties do not appear to be in disagreement. Rather we have concentrated on where they are, or may be.

### **Phenytoin**

48. We deal with *Phenytoin* first, since it is Court of Appeal authority. This was an appeal from a decision of the Tribunal dated 7 June 2018 ([2018] CAT 11) which, in turn, had upheld an appeal from a decision of the CMA which had held that the relevant prices for the drug were unfair and thus abusive. The Tribunal set aside the CMA’s decision. The Court of Appeal dismissed the appeal against the decision of the Tribunal, although on different grounds to those given by the Tribunal, and remitted the matter back to it. The particular issue in *Phenytoin* concerned the correct approach to be taken by the CMA when considering the methodology used to ascertain the competitive benchmark which forms part of the Limb 1 analysis. The Court of Appeal held that when a competition authority is determining a competitive benchmark, there is no rule of law requiring it to use one particular method, which is effectively what the Tribunal had decided. However, even though it had a margin of appreciation to decide what methodology to use, and what evidence to rely upon, where the undertaking said to have abused its dominant position had put forward sound evidence and arguments tending to show that its prices were fair, the CMA was under a duty to



evaluate fairly and impartially all the arguments and evidence advanced. It had not been open to the CMA here to ignore the comparator evidence raised by the undertakings in their defence. So the outcome, so far as the CMA's decision was concerned, was the same, which was that it was wrong.

49. The particular point at issue in *Phenytoin* is not an issue here, but having considered the relevant authorities including *United Brands*, Green LJ made some general observations about abuse of dominant position by reason of excessive pricing as follows:

“97 I would draw the following general conclusions from the case law about the test to be applied: (i) The basic test for abuse, which is set out in the Chapter II prohibition and in article 102FEU, is whether the price is “unfair”. In broad terms a price will be unfair when the dominant undertaking has reaped trading benefits which it could not have obtained in conditions of “normal and sufficiently effective competition”, ie “workable” competition. (ii) A price which is “excessive” because it bears no “reasonable” relation to the economic value of the good or service is an example of such an unfair price. (iii) There is no single method or “way” in which abuse might be established and competition authorities have a margin of manoeuvre or appreciation in deciding which methodology to use and which evidence to rely upon. (iv) Depending upon the facts and circumstances of the case a competition authority might therefore use one or more of the alternative economic tests which are available. There is however no rule of law requiring competition authorities to use more than one test or method in all cases. (v) If a cost-plus test is applied the competition authority may compare the cost of production with the selling price in order to disclose the profit margin. Then the authority should determine whether the margin is “excessive”. This can be done by comparing the price charged against a benchmark higher than cost such as a reasonable rate of return on sales (ROS) or to some other appropriate benchmark such as return on capital employed (ROCE). When that is performed, and if the price exceeds the selected benchmark, the authority should then compare the price charged against any other factors which might otherwise serve to justify the price charged as fair and not abusive. (vi) In analysing whether the end price is unfair a competition authority may look at a range of relevant factors including, but not limited to, evidence and data relating to the defendant undertaking itself and/or evidence of comparables drawn from competing products and/or any other relevant comparable, or all of these. There is no fixed list of categories of evidence relevant to unfairness. (vii) If a competition authority chooses one method (e g cost-plus) and one body of evidence and the defendant undertaking does not adduce other methods or evidence, the competition authority may proceed to a conclusion upon the basis of that method and evidence alone. (viii) If an undertaking relies, in its defence, upon other methods or types of evidence to that relied upon by the competition authority then the authority must fairly evaluate it...

107 Pulling the strands together I conclude that the economic literature supports the conclusions of law that I derive from the case law summarised above (cf para 97). There are many different tests which might be used to determine whether a price is excessive and unfair; there are or may be difficulties with all tests and much will depend upon the availability of evidence and data; all cases are highly fact and context specific; there is a need for competition authorities to be able to intervene ex post in pharmaceutical cases; and, it is economically rational that competition authorities should have a margin of appreciation as to the choice of method and evidence that they seek to rely upon...

125 In my view by the nature of the abuse in issue there needs to be “a” benchmark. But, in the first instance at least, the choice of benchmark is for the competition authority to choose and can be based upon the costs of the undertaking being investigated or it can be based upon comparables such as the prices charged by the same or different undertakings in the same or different geographical markets or indeed any other benchmark or combinations thereof capable of providing a “sufficient” indication that the prices charged are excessive and unfair. It follows from the above that assuming the Tribunal was mandating the use in all cases of a hypothetical benchmark price which did not include the costs of the undertaking or some other benchmark related to the undertaking, then I respectfully disagree with the Tribunal...

154 The concept of economic value is not defined. In broad terms the economic value of a good or service is what a consumer is willing to pay for it. But this cannot serve as an adequate definition in an abuse case since otherwise true value would be defined as anything that an exploitative and abusive dominant undertaking could get away with. It would equate proper value with an unfair price. This is a well-known conundrum in international competition law. The same point was made by the Court of Appeal in *Attheraces* [2007] Bus LR D77; [2007] UKCLR 309, para 205. The issue was first identified in US antitrust and arose from criticisms of the judgment of the Supreme Court in *United States v Du Pont & Co* (1956) 351 US 377 when it attracted the

soubriquet “the cellophane fallacy”. To overcome this in *United Brands* in para 250 the court held that there must be a “reasonable” relationship between price and economic value.

155 The simple fact that a consumer will or must pay the price that a dominant undertaking demands is not therefore an indication it reflects a reasonable relationship with economic value. But a proxy might be what consumers are prepared to pay for the good or service in an effectively competitive market, hence the relationship between the two descriptions of abuse in paras 249 and 250 and the fact that the economic value description is said to be an example of the broader description of an abuse in para 249...

171 First, the Tribunal observed that this [ie economic value] was clearly a legal test. The categorisation of this as a “legal” concept seemingly led the Tribunal to treat economic value as a discrete component of the test in law to be applied. It is “legal” in the strictly limited sense that it has been ascribed a meaning in a court judgment but, at base, it is an economic concept which describes what it is that users and customers value and will reasonably pay for and it arose in the *United Brands* judgment [1978] ECR 207 as an economic description of the abuse of unfair pricing: see the analysis at para 61 above.

172 Second, the Tribunal did not agree with the submissions of all parties that economic value was simply a matter to be taken into account as part of other components of the test. The Tribunal held that it was not part of the “in itself” test but was part of “a more general assessment” (Judgment, paras 427 and 443(6)). I agree with the parties on this. It is evident from the judgment in *United Brands* that the reference to “economic value” is a part of the overall descriptor of the abuse; it is not the test. The test should therefore, when properly applied, be capable of evaluating economic value. So, for instance, as the CMA argues, when evaluating patient benefit it would be possible to measure its economic value in the plus element of cost-plus, or even in the fairness element. Equally, if there is evidence of the prices being charged in relevant, comparator, markets which were effectively competitive then those prices could be capable of acting as proxy evidence of the economic value of patient benefit. In so far as an issue of fact arises which can be categorised as an aspect of “economic value” it needs to be measured and it can be evaluated in various parts of that test. If it is properly factored into “plus” or “fairness” or into some other part of the test, or is reflected in other evidence which can stand as a proxy for economic value, then there is no incremental obligation to take it into account again, as a discrete advantage or justification for a high price. In para 421 the Tribunal states that the analysis of economic value conducted at other stages of the test are “broadly similar” but that there is a “different perspective”. With respect I do not follow this. The analysis of the Tribunal, for instance as articulated in para 443(6) of the Judgment (set out at para 40 above), suggests that it is a requirement discrete from other components of the test to be applied only after all those components have been worked through. But if this were so it would (wrongly) risk compelling a competition authority to double count economic value. In short, economic value needs to be factored in and fairly evaluated, somewhere, but it is properly a matter which falls to the judgment of the competition authority as to where in the analysis this occurs.”

50. Before considering these paragraphs as a whole, something more needs to be said about the reference to “economic value” in paragraph 172. This arose because the Tribunal had found, or appeared to have found, that in addition to undertaking the Limb 1 and Limb 2 exercise to reach a judgment on unfairness, the authority had also to consider, in the round as it were, what the economic value of the product was and whether the price charged bore no reasonable relation to it. See paragraphs 427 and 443 (6)-(8) of the decision of the Tribunal. The Court of Appeal disagreed with that approach. There is no further overarching test concerned with economic value, although it needs to be taken into account somewhere.
51. Without wishing to parse the paragraphs quoted in paragraph 49 above as if they were a statute, it seems to us that they yield the following propositions which are relevant for present purposes and which apply as much to the Tribunal as they do to the CMA:
- (1) To be abusive, the price must not only be excessive but also unfair;

- (2) It will be unfair if the dominant undertaking has reaped trading benefits which it could not have obtained in conditions of workable competition;
- (3) If a price is excessive and bears no reasonable relation to the economic value of the service in question, this is an example of an unfair price. However the lack of a reasonable relation to the economic value of the service is not itself the test; rather, it is an economic description of the abuse. It needs to be considered at some point in the analysis: this could be under the Limb 1 or Limb 2 exercise;
- (4) Where the price is found to be excessive, whether it is unfair will depend on a number of factors including, but not limited to, evidence and data relating to the defendant undertaking itself and/or evidence of comparables drawn from competing products and/or any other relevant comparable, or all of these. There is no fixed list of categories of evidence relevant to unfairness. In particular, if the question of economic value (see below) has not been taken into account under Limb 1, it must be considered as part of the unfairness exercise under Limb 2.

- 52. Interposing there, in our view, both parties here did ultimately seek to take the question of economic value as part of the Limb 2 assessment of unfairness, rather than in the context of Limb 1 excessiveness. (Mr Parker was disposed sometimes to bring it into the question of excessiveness, but we did not agree with this and in any event, it was not ultimately the CR's case.)
- 53. For our part, and notwithstanding the flexibility open to a court or competition authority as to where to take into account the question of economic value, we consider the approach taken by the parties to be a helpful one. This is for two reasons. First, it enables the Limb 1 exercise, complex and challenging as it may be, to focus on the linear process of deciding (a) the relevant competitive benchmark, (b) the excess of the price (if any) over that benchmark, and (c) whether such excess is significant and persistent (for the latter, see paragraphs 54-55 below). One would perhaps hesitate to describe such a process as "mechanical" where the underlying questions can be the subject of hotly contested expert evidence and where they involve various value judgments, and moreover where there is a margin of appreciation afforded, at least to a competition authority. Nonetheless, we consider that it is, from an analytical point of view, "cleaner" and more efficient if the question of economic value can be considered as part of the Limb 2 unfairness exercise which, on any view, is clearly less "mechanical" than the Limb 1 exercise, and where a multiplicity of different factors can be taken into account.
- 54. As for the nature or extent of the excess of price over the competitive benchmark which needs to be shown, in the end, both parties here were content to adopt the expression "significant and persistent".

This expression has its origins in paragraph 56 of the decision of the Court of Justice in *Latvian Copyright* [2017] 5 C.M.L.R. 19:

“It should be emphasised in this regard that, as observed by the Advocate General in point 107 of his Opinion, the difference must be significant for the rates concerned to be regarded as “abusive”. Furthermore, that difference must persist for a certain length of time and must not be temporary or episodic.”

55. It was adopted by the Tribunal in its decision in *Phenytoin*. It was not expressly referred to by the Court of Appeal, no doubt because there was no appeal issue relating to it. We also proceed on the basis that a significant and persistent excess needs to be shown.
56. It also appears to us to be implicit in the judgment of the Court of Appeal in *Phenytoin* at paragraph 97 (vi) that if and when Limb 2 is reached, the Court should balance all the factors involved which go one way or the other, giving them such weight as it considers appropriate, so as then to conclude whether the price was itself unfair. Of course, the very size of the excess can be a factor pointing strongly towards unfairness. On the other hand, it would, in our view, be wrong to approach the Limb 2 exercise as if there were a presumption of unfairness established already by the mere fact that the price was excessive under Limb 1, subject only to any justification which the defendant can establish. We do not see the decision in *United Brands* as directing such an approach, nor do we see why it is necessary. Nor do we see the reference by Green LJ in *Phenytoin* at paragraph 97 (v) to “other factors which might otherwise serve to justify the price charged as fair” (quoted at paragraph 49 above) to mean that there was some presumption of unfairness. All it meant was evidence or arguments pointing towards fairness rather than unfairness. Indeed that is demonstrated by paragraph 97 (vi).
57. The importance of distinguishing between the Limb 1 and Limb 2 exercises was emphasised by Laddie J in *BHB v Chandler* [2005] EWHC 1074 (Ch):
- “51. I do not accept that this supports the proposition advanced on behalf of VCI. On the contrary it appears, particularly from the paragraph 252 of the judgment [in *United Brands*], that all the ECJ was saying was that comparing prices with costs determines the profit margin. Once that has been achieved it is necessary to go on to the next stage to determine whether the price is unfair. What it did not do was suggest that high prices or high margins are the same as unfair prices. Indeed, were Mr Turner right, it seems to me that the law reports would be full of cases where undertakings in dominant positions would have been found guilty of abuse by simply charging high prices. As Mr Vaughan says, the reality is that there are no such cases.”
58. In paragraphs 195 and 208 of *Attheraces Limited v British Horseracing Board* [2007] EWCA Civ 38, the approach of Laddie J in *BHB* on some related issues (although not this paragraph – which was not discussed) was endorsed by the Court of Appeal.

## **Albion Water II**

59. *Albion Water II* was an appeal to the Tribunal from a decision of the Welsh Water Authority that certain charges made by Albion Water for the carriage of non-potable water through a pipeline to a particular water company were not excessive (and therefore could not be unfair) for the purposes of a Chapter II claim. It, of course, preceded *Phenytoin*.

60. As to the most appropriate methodology the Tribunal stated as follows:

“88. Despite the various cases in this area, no consensus has emerged as to what, if any, is the most appropriate method of measuring cost in excessive pricing cases. The ECJ has stated that the “costs actually incurred” must be ascertained (United Brands, paragraph [252]), but there is no rule of law as to how that is to be done: it is a matter of fact, accounting technique and economic assessment. However, community jurisprudence only permits the inclusion of efficiently incurred costs (see Case 395/87 *Ministère Public v Tournier* [1989] ECR 2521, [1991] 4 CMLR 248, at paragraph [42].”

61. It also stated that the relevant costs to be calculated were those which were “reasonably attributable” to the production of the relevant service. See, for example, paragraph 198. Such relevant costs would then be added to a reasonable margin to make up the “competitive benchmark”.

62. As for the extent of any excess required under Limb 1, the Tribunal was prepared to accept, as contended for by the Authority, that the excess needed to be “material” while declining to specify when a particular percentage excess would reach that materiality threshold. It sufficed to say that a price of at least 46.8% above the costs reasonably attributable to the relevant water supply was materially excessive. Ascertaining the extent of the excess involved a “proper degree of discretionary judgment by the decision-maker”. We do not consider that there is any real difference between the threshold of “material” and “significant”.

63. The Tribunal also made the following observations about economic value, summarising what was said in paragraphs 203-217 of the decision of the Court of Appeal in *Attheraces*:

“222. The European Commission (in *Scandlines*) and the Court of Appeal (in *Attheraces*) have both stated that the concept of economic value does not necessarily, or always, imply a cost-based approach, still less according to any particular measure of cost. It is clear that the economic value of a product or service should take account also of relevant “non-cost-related factors”, i.e. factors other than the cost of supplying a product or service but which mean that a product or service has a particular enhanced value from the customer’s perspective...

224...the parties drew the Tribunal’s attention to the passages in the judgment of Mummery LJ [in *Attheraces*] at paragraphs [203] et seq. From these a number of principles emerge:

- (a) Subject to what is envisaged by Article 82 EC, the economic value of a product or service is what it would fetch (paragraph [205]).
- (b) Article 82 and the Chapter II prohibition proceed from the premise that the undertaking has a dominant position enabling it to distort the market in which it operates. Dominance may have the effect of distorting the economic value of the product or service (paragraph [205]).
- (c) It does not follow that whatever price a seller in a dominant position exacts, or seeks to exact, is necessarily an abuse of his dominant position (paragraph [206]).
- (d) The economic value of a product is a different concept from its cost. Although a comparison between price and cost of supply (plus a reasonable return) may be a first step in the analysis of economic value, it is not conclusive on the question of unfair pricing and the existence of an abuse (paragraphs [207], [209] and [213]).
- (e) It is relevant to consider whether the customer’s competitiveness had been, or was at risk of being, materially compromised by the terms of supply (paragraphs [215] and [217])...

225...In our view, the Authority was correct to observe at paragraph 12.61 of the Report that neither *Scandlines* nor *Attheraces* “excludes the possibility that, in the absence of relevant non-cost-related factors, the very excessiveness of a price could be sufficient to establish that the price bears no reasonable relation to the economic value of the product/service being provided.” This approach is also consistent with that taken by the European Commission in *Deutsche Post* (see paragraph [203] above).”

64. We accept that, to the extent that a product or service has a particular enhanced value from the customer's perspective, that is looking at the matter from a subjective (i.e. the customer's) point of view. Indeed, there was some evidence adduced before us on that very question of customers' actual preferences or views in relation to SFV Services.
65. In *Albion Water II* itself, the Tribunal observed as follows:
- “216. The test laid down by the ECJ, like the prohibition in Article 82 itself, contains words – “bears”, “reasonable”, “relation” – which lack precision. Their practical application depends on the legal and economic context. It follows that there is no single correct measure of the ‘economic value’ of an asset such as the Ashgrove system. As the Tribunal has already held in paragraph [310] of the main judgment, and as the parties have accepted in their pleadings, whether a given price bears “no reasonable relation” to its “economic value” is a matter of degree, which involves a considerable margin of appreciation, not least because the concept of “economic value”, and whether the price has a “reasonable” relation to that value, are matters of judgment.”
66. We would agree with that observation.
67. The Tribunal went on to conclude that the extent of economic value contended for by the Authority had not been shown. Rather, it was limited, as follows:
- “249. It follows from the foregoing that the economic value of the services to be supplied in this case was not more, or not significantly more, than the costs reasonably attributable to the service of the transportation and partial treatment of water by Dŵr Cymru, generally and through the Ashgrove system in particular.”
68. In other words, there was no real economic value above the underlying costs of supplying the service.
69. The Tribunal further noted that factors going to the establishment of a dominant position, notably barriers to entry, may well be relevant to determining whether the price was so high as to amount to an abuse. This was particularly true in excessive pricing cases where it was important to distinguish excessive prices which were shielded from effective competitive pressure, as opposed to temporarily high prices which were the subject of normal market forces in a competitive market. While the former would not in itself establish an abuse, it suggests that the Tribunal should review with care the lawfulness of the price which was unconstrained by any competitive considerations whatsoever. It goes to the question as to whether the relevant market was capable of functioning in a manner likely to produce a reasonable relationship of price to economic value. This was not the case in *Albion Water II*, because the water authority had a 100% share of the relevant market and there were significant barriers to entry. See paragraphs 213 and 266-270 of the judgment.
70. In addition, the Tribunal's decision in *Phenytoin* ([2018] CAT 11) also considered (at paragraph 369) that the CMA was entitled to have regard to the substantial disparity between the companies' prices and their economic value, the fact that competitive conditions on the markets showed that they did not function in a manner which was likely to produce a reasonable relation between the two, that the prices had an adverse effect on the end customer, and the fact that the companies were aware of this.

71. We return to the question of economic value when considering the case of *Hydrocortisone* below.

### **Liothyronine**

72. The main relevance of this case, for our purposes, concerns what it says about so-called “entry-incentivising prices” in the context of setting a reasonable margin. This is best dealt with in context, and we do that at paragraphs 597 - 599 below. We would only add here that the Tribunal in *Liothyronine* also endorsed the observations made by the Tribunal in *Albion Water II* at paragraph 222, set out in paragraph 63 above.

### **Hydrocortisone**

73. There are various aspects of this decision of the Tribunal which we found helpful.

74. First, there is a point as to the correct analytical approach. Here, the Tribunal observed as follows:

“(2) The dangers of backward reasoning

153. Particularly where the abuse alleged is one of excessive pricing, there is great danger in reasoning backwards from a perceived excessive – and so potentially abusive – price.

The backwards reasoning goes like this:

(1) Only a dominant undertaking can raise price so as to constitute an abuse of a dominant position.

If the undertaking were not dominant, competition would ensure a “proper price”.

(2) Therefore, if the price is abusive, the undertaking is dominant.

(3) If the undertaking is dominant, then the market must be defined consistently with that finding of dominance.

154. Particularly in difficult cases, it is important to keep the processes of (i) market definition, (ii) dominance and (iii) abuse as distinct analytical stages. Take an allegedly wantonly or obviously abusive monopoly, where it appears that the monopolist is charging abusive monopoly rents because (i) the monopolist has the market power and (ii) it pays the monopolist to exercise that power because high margins on low sales are what brings in more revenue than smaller margins on higher sales. In such a simple case, it is tempting to reason from outcome, as follows: (i) the price is abusively high (the outcome), (ii) therefore there is dominance (because the monopolist could not abuse market power without dominance) and (iii) therefore the market has got to be defined as excluding what might otherwise be regarded as substitutes to the monopolist’s product, so as to achieve the dominance in the market to render an abuse of dominance possible.

155. The problem with this sort of reasoning is that whilst the conclusion (an abuse of a dominant position) may be right, the reasoning assumes that which needs to be tested for. For that reason, this approach is to be deprecated as creating an avoidable risk of wrong outcomes. The fact is that there are many explanations for high prices that are consistent with competitive behaviour and inconsistent with a finding of infringement of the Chapter II prohibition...”

75. In general, we agree with the above paragraphs. They are consistent with the approach which we advocate in paragraph 53 above. Of course, in a case involving allegations of exploitatively high prices, there are a number of common threads that run through the assessment of the three questions of market definition, dominance and excessively high prices. Consequently, evidence that is relevant to one of these questions might well also be relevant to the others, even though each of the three questions must be assessed independently of one another.

76. At paragraphs 312 and 313, the Tribunal referred to the concept of consumer surplus which was a measure of the additional benefit that individual consumers receive because they are paying less for something than they would have been prepared to pay. At paragraph 313, the Tribunal said this:

“Consumer surplus is an individual value, subjective to the individual consumer. In some cases, these subjective values will converge in that consumers will generally value something in a similar way (e.g. food, medical products, other “essential” goods), but even here subjectivity reigns (e.g. how a consumer might choose between food or a medical product). Consumer surplus is based on value to the consumer, measured in monetary terms. Assuming a consumer has the ability to pay, they will pay a price for a product up to and including the monetary value they place on it – but no more.”

77. Then, at paragraph 322, there is a detailed exposition of three potentially different situations where high prices (in the sense of being above the competitive benchmark) pertain. First, there may be relative inefficiency between sellers. Thus, while prices may be relatively similar, one producer may enjoy a higher surplus because it is more efficient (“Case 1”) - see paragraph 322 (1). Second, one particular supplier may be able to generate - and provide - additional value through what the Tribunal refers to as the provision of “distinctive value” (“Case 2”) - see paragraph 322 (2). Third, where producer surplus is generated for the undertaking without any added value to buyers (“Case 3”) - see paragraph 322 (3).
78. As to Case 2, this arises where buyers are in effect willing to pay a premium, i.e. more than they would pay for an alternative or substitute product. The term “distinctive value” (as opposed to “product differentiation”) is designed to capture

“...any definable aspect of a Seller’s offering that adds value to the Buyer, in the sense that this aspect represents something that Buyers wish to purchase from that Seller in contradistinction to the offerings of other Sellers; and for which the Buyer will pay a premium.”
79. As for product differentiation itself, this is not confined merely to innovation but also to providing a better quality product in other ways and in catering to the subjective tastes or preferences of buyers.
80. The Tribunal further observed at footnote 399 that investment in brand is also an example of what buyers may value and pay a premium for, even though other products are identical:

“Investment in brand is also an example of this: for reasons that may well be objectively indefensible, Buyers will pay a premium for a “brand”, even though the identical product is available unbranded. The owner of a (valued) brand may command a higher price, but will always be at risk from unbranded competition (or other brands).”
81. Case 3 arises where the seller possesses market power which does not generate additional value for buyers. Here buyers are obliged to pay more for what is the same product. In such cases, the higher prices do not for some reason attract competition in the form of new entrants. This may happen where a single seller is able to create sufficient barriers to contestability so as to exclude other competitors.
82. We see the usefulness of sketching out different scenarios where distinctive value is either offered or not offered, but would caution against too prescriptive an approach. As the Tribunal in *Hydrocortisone* itself observed at paragraph 323, the distinction between Cases 2 and 3 is by no means easy to draw and some cases will straddle both Case 2 and Case 3.
83. Subject to the caveat just mentioned, we would adopt the concept of distinctive value as a useful yardstick by which to measure that value in the product which is different to its cost (as established



for these purposes by the relevant competitive benchmark under Limb 1) and which is something in some way different from the offerings of other sellers, but which can include the brand or other value ascribed subjectively by the customer for the product, as distinct from the product's particular features. In that regard, innovation in its features is not necessary if they are perceived by the customer (subjectively or objectively) to amount to a better quality product in some way. We did not understand BT to disagree with this proposition; see, for example, paragraphs 175-177 of its Opening and paragraphs 683-688 of its Closing. We would add that, in our view, the assessment of distinctive value (or not) is highly fact-sensitive and involves a considerable amount of judgment (as noted in paragraphs 65 and 66 above).

84. There is a further aspect to the decision in *Hydrocortisone* which we consider in paragraphs 96 and 97 below.

### **Other Cases and Matters**

85. In the context of economic value, BT refers to what the Court of Appeal stated in *Attheraces* at paragraph 117:

“Secondly, the central concept in abuse of dominant position by excessive and unfair pricing is not identified as the cost of producing the product or the profit made in selling it, but as the “economic value of the product supplied.” The selling price of a product is excessive and an abuse “if it has no reasonable relation to its economic value.”

86. BT also referred to paragraph 155 in the same judgment which reads as follows:

“A particularly high price and high profit margin may, however, be a determining factor if unjustified by any objective criteria, or in comparison with competing products, or where the dominant undertaking is exploiting its ownership of an essential facility....The approach was that, in principle, prices are excessive if they “are higher than would be expected in a competitive market” and “there is no effective competitive pressure to bring them down to competitive levels, nor is there likely to be.” It was recognised that “measuring whether a price is above the level that would exist in a competitive market is rarely an easy task” but the difficulty of the exercise was not a reason for not attempting it.”

87. We would agree with both of those passages taken from *Attheraces*.
88. We would add that *Attheraces* was a case where the first instance judge had found there to have been abuse because of the price charged by the BHB to betting companies for providing details of all the horse races on any given day. He did not consider, for the purposes of economic value, anything other than the costs of providing it. The Court of Appeal allowed BHB's appeal on the basis that the value to the “demand side” i.e. the betting companies, had to be considered as well as the “supply side” costs. The value of the information to the betting companies was very high, for without it they could not have run their businesses effectively. That was the case notwithstanding that the costs to the BHB of producing the information were low. Accordingly, the prices charged were not abusive.
89. In the case of *Deutsche Post AG – Interception of cross-border mail* (OJ 2001 L 331, p. 400) 20 July 2001, Deutsche Post deemed mail containing any reference to Germany (for example, the

inclusion of a German reply address in the contents of the mail) to have a German sender and, accordingly, charged the full domestic tariff for such mail. The Commission decided that, by intercepting, surcharging and delaying normal cross-border mail in this way, Deutsche Post had abused its dominant position on the German market for the delivery of cross-border mail. Further, the Commission found that the price charged by Deutsche Post exceeded the average cost for delivering incoming cross-border mail by at least 25%, and that the price bore no reasonable relationship to actual costs or to the real value of the service provided. In that case, there was no invocation of economic value above the costs of supplying the service, and the Commission disagreed with Deutsche Post as to what those costs truly were.

90. Two other factors should be mentioned: First, in considering whether the undertaking's conduct is abusive, it is legitimate to consider whether it had any anti-competitive or exploitative intent. That said, the presence of any such intent is not a prerequisite to a finding of abuse and equally, the absence of any such intent does not preclude such a finding. See the decision of the Court of Justice in *Tomra Systems v Commission* (2012) T-549/10 at paragraph 19-24.
91. Second, a lack of transparency on the part of the relevant undertaking with regard to its conduct can be a factor going to unfairness. The Court of Appeal so held in *London & South-East Railway v Gutmann* [2022] EWCA Civ 1077 in connection with the rail company's operation of a system which fails to be transparent as to the availability of cheaper alternative prices for the same service.

### **Unfairness by Comparison**

92. All of the above factors are said to be relevant to the first form of abuse under *United Brands*, namely "unfair in itself". This was the main way in which the CR put its case here, but in the alternative, or as support for a finding of unfairness in itself, the CR made and maintained a case of unfairness by comparison. However, insofar as there was a case of "unfairness in comparison", the following points are relevant: First, comparators could be drawn from different markets or the same market at the same time, or comparators separated by time. The key point is whether such comparators are probative. Any such comparators should be selected in accordance with objective, appropriate and verifiable criteria and comparison should be made on a consistent basis. Further, comparators could be relevant under the first form of unfairness as well. See paragraph 331 (1) of *Hydrocortisone* and paragraph 308 (4) of the decision of the Tribunal in *Phenytoin*.
93. Second, if the comparator prices are themselves distorted because they were not set in conditions of effective competition and were affected by the exercise of market power, they are not reliable. See, for example, *Phenytoin* at paragraph 155 and the decision of the Tribunal in *Hydrocortisone* at paragraph 348.

94. Third, there is a more general point. This concerns the interrelationship between the “of itself” and “by comparison” elements of Limb 2. A claimant, absent anything else, does not have to establish unfairness by reference to both of these elements. In that sense, they can be said to be alternatives.
95. However, that is not a complete picture. If, for example, a defendant wishes to put forward comparators by reference to which it is said that the price could not be regarded as unfair, the competition authority or claimant, as the case may be, must address those comparators. Once the comparators are engaged with, as it were, the exercise of assessing them then forms part of the overall assessment of unfairness or otherwise. If the conclusion, or provisional conclusion, is that the prices were unfair in themselves, then a finding of unfairness by comparison would support that position. Conversely, however, if the analysis of the comparators suggests that the prices in question were not unfair, then that conclusion must be fed into the overall assessment of unfairness as well. Otherwise, there would be no point in a defendant raising the issue of fairness by comparison. For those reasons, the Tribunal (or competition authority) must consider comparators if they are properly raised. All of this was made very clear by Sir Geoffrey Vos in his concurring judgment in *Phenytol*:

*“Issue 2: The both limbs issue: Was the CAT wrong to hold that the two-limb test for unfairness in para 252 of United Brands required the CMA to consider both limbs, even if the CMA had held the first “unfair in itself” limb satisfied?”*

256 I was struck in the course of argument by the way in which this issue seemed to turn on semantic and black-letter reasoning. As I have said, Court of Justice decisions and Advocate General opinions are not to be construed as deeds. As is well known, they are generally and deliberately more nuanced and open to interpretation than decisions of domestic courts.

257 The CAT acknowledged at para 366 that it was clear from para 47 of the General Court in *Scippacercoloa* [2009] ECR I-46, and paras 101 and 103 of the Commission Decision in *Scandlines Sverige AB v Port of Helsingborg* [2006] 4 CMLR 23 that the two tests of unfairness in para 252 of *United Brands* [1978] ECR 207 are “alternatives, in the sense that an authority can, as a matter of law, establish a breach of article 102FEU under either alternative 1 or 2 and does not need to succeed under both”.

258 The question under this issue is whether the CAT was right when it went on at paras 366 and 443(5) to say that: (i) the CMA did not have an unfettered choice between the two; (ii) a breach of article 102FEU could not be established by selecting only the first alternative, when a *prima facie* argument had been raised that under the other alternative, the pricing was fair; and (iii) the CMA could not find that there is an infringement where one alternative demonstrates unfairness and the other does not, as a matter of logic, to accord with the burden of proof, to respect the presumption of innocence, and to accord with the sanity check mentioned by Advocate General Wahl at point 124.

259 In my judgment, the CAT was wrong to say that the CMA was obliged to consider the second alternative of the unfairness test having decided that it was appropriate in all the circumstances to adopt the first alternative. As has been repeatedly said, the tests are alternatives. But I do agree with the CAT when it said at para 367 that the CMA could not “simply ignore a *prima facie* valid argument that a price is fair” whichever alternative it chose to adopt.

260 It, therefore, seems to me that the question of whether the choice between the two limbs of the unfairness test adumbrated in *United Brands* [1978] ECR 207 is a binary one, is an academic and irrelevant one. As will appear under issue 3 below, I take the view that the competition authority will always need, at least as part of its duty of good administration, to give some consideration to *prima facie* valid comparators advanced evidentially by the undertakings. That is so whether or not the CMA chooses to proceed eventually under the “unfair in itself” alternative of the unfairness test. Even in that situation, the fact that comparators are expressly mentioned under the second alternative does not absolve the CMA from giving whatever proper attention is

required to comparators raised by the undertakings. In these circumstances, I am in substantive agreement with Green LJ's conclusions on this point...

273 Green LJ also concludes at para 113 that (i) the CMA has no duty in every case proactively to investigate all comparators put forward by an undertaking that prima facie demonstrate that the prices charged were fair, and that (ii) the CMA does, however, have a duty fairly to evaluate any such comparators. As I have said, it may well be prudent for the CMA to make its own investigations, but it is not under a legal duty to do so. If the CMA wrongly ignores evidence of comparators, and those comparators turn out to be relevant or important, their analysis will fail at the CAT. In my judgment, the suggestion of an obligation in every case to conduct any investigation is not warranted in law."

### **The relevance or otherwise of regulation**

96. In *Hydrocortisone*, the Tribunal observed as follows:

"351. We have been somewhat critical of the regulatory environment that has at least facilitated these overcharges. We have been even more critical of – and have rejected in terms – arguments that seek to justify these overcharges by reference to the regulatory environment. We want to be clear that the fact that a mere regulatory environment has engendered a dominant position which is then abused in no way justifies the abuse."

97. The fact that there is a regulatory regime which in theory could apply controls does not preclude the possibility of an abuse. What is relevant is the actual position in the relevant market in the context of any controls which may have been exercised. See *Hydrocortisone* again at paragraph 329 (2). A similar point was made in *Albion Water II* at paragraph 242:

"As regards the need for regulatory approval of the First Access Price, even though Dŵr Cymru apparently believed it needed its access charges to be approved by the Authority, this does not absolve it from its special responsibility under the Chapter II prohibition. Even if the position of the regulator (in favour, at the material time, of access prices set according to regional average costs) and/or the relevant regulatory framework encouraged or made it easier for water companies to engage in anti-competitive conduct, those undertakings remained subject to the Act."

98. In relation to this, BT has quoted from part of paragraph 31 of the decision of the Tribunal in *Phenytoin*. The whole of that (introductory) paragraph reads as follows:

"Cases of pure unfair pricing are rare in competition law. Authorities find them difficult to bring and are, rightly, wary of casting themselves in the role of price regulators. Generally, price control is better left to sectoral regulators, where they exist, and operated prospectively; ex post price regulation through the medium of competition law presents many problems. However, the law prohibits unfair pricing in certain circumstances and in such cases there is no reason in principle why competition law cannot be applied, provided this is done on the correct legal basis and the analysis of evidence is sound."

99. We do not consider that this is inconsistent with what was said in *Hydrocortisone*, as referred to above.

100. BT also refers to part of paragraph 49 of the AG's opinion in *Latvian Copyright* which reads as follows:

"Secondly, a price significantly in excess of a competitive price is more unlikely to occur in markets where there is a sectoral regulator whose task is, inter alia, to fix or control prices charged by the undertakings active in that sector. Sectoral authorities are clearly better-equipped than competition authorities to oversee prices and, where necessary, act to remedy possible abuses. It would seem, therefore, that antitrust infringements in those situations should be mainly confined to cases of error or, more generally, to regulatory failures: cases where the sectoral authority should have intervened and erroneously failed to do so."

101. It seems to us that what is being suggested here is that in practice, in a situation where a regulator has acted in relation to pricing, the prospect of abusive excessive pricing from a competition law point of view is less likely than a case where a regulator has not intervened. The last sentence of the

paragraph contemplates a situation where the regulator did not intervene. We think that this paragraph is perhaps too dogmatic, but in any event, in our case, Ofcom did not intervene to set prices until 2017, and once it effectively did so (through obtaining the Commitments in respect of VOCs), that marked the end of the claim period for the VOCs.

102. In this context, BT itself refers to what the Tribunal said in *Hydrocortisone* but in a different passage:

“330. There is no single method for ascertaining whether a price is unlawful in terms of its excess or not, and any given method will have some inherent weaknesses. When considering whether a price is or is not excessive, a tribunal must have careful regard to “regulatory overreach”, in that interference in an outcome that may actually be competitive is as bad as failing to call out as infringements excessive prices.”

103. Read fairly, all that passage seems to be saying is that a tribunal should take care that it is not pronouncing as unlawful, conduct by an undertaking which is actually competitive, since that itself is detrimental to consumers. We would, of course, agree. We do not see this passage as contradicting the various passages to which we referred at paragraphs 96 to 97 above.
104. On that basis we would reject any suggestion on the part of BT that the mere fact of “regulatory scrutiny” by Ofcom over the claim period somehow mitigates its position in relation to abuse. This does not mean, of course, that the views of Mr Matthew were irrelevant to the topics discussed. We evaluate his evidence, in context, along with the others, below.

### **The Effect and Significance of Ofcom’s 2017 Provisional Conclusions and Statement**

105. It is not suggested (nor could it be) that any aspect of the 2017 Provisional Conclusions and Statement (summarised at paragraphs 155-161 below) bind this Tribunal. At the end of the day, it is for this Tribunal, and no-one else, to decide this case on the basis of the materials put before it.
106. However, the CR contends that the findings contained in those documents are admissible, relevant and should be given substantial weight, so as to corroborate his claims. The position, in law, in relation to prior regulatory findings which may be said to overlap in some way with the issues before a later Tribunal, has been clearly set out by the Court of Appeal in *Evans v Barclays Bank and others* [2023] EWCA Civ 876 (“*FX*”). *FX* involved an appeal from the decision of the CAT to certify collective proceedings on an opt-in and not opt-out basis, subject to a viable claim being shown. One of the grounds of appeal concerned the approach of the majority of the Tribunal to the present viability or otherwise of the claims, and that the majority had failed to draw proper inferences from prior decisions of the Commission that gave weight to the claim. Green LJ (with whom Sir Julian Flaux C and Snowden LJ agreed) dealt with position in principle as follows:

“100. Most importantly, it is well established that the rule [in *Hollington v Hewthorn*] does not apply to the CAT which has its own rules of procedure and evidence. CAT Rule 55(1)(b) makes clear that the CAT has a wide discretion as to the evidence to be admitted. This has been recognised on many occasions and is, in my view, correct: see e.g. *Agents’ Mutual Limited v Gascoigne Halman Limited* [2017] CAT 5 at paragraph [8]; *Argos and Littlewoods v OFT* [2003] CAT 16 at paragraph [105]; *Aberdeen Journals v. OFT* [2003] CAT 11 at paragraphs [126] and [134]), *Consumer Association v Qualcomm* [2023] CAT [9] (“Consumers

Association”) at paragraph [18]. In *Le Patourel* the CAT had relied upon the findings in a prior settlement decision between the respondent, BT, and OFCOM. The Court of Appeal agreed with the CAT that the findings were relevant as showing a serious case to be advanced but made clear that they were not binding upon the CAT at trial (ibid paragraph [106]). And of course, there is already a statutory exception to the rule in section 60A CA 1998.

101. There is no need for the CAT to be hidebound by a common law rule on fairness. Whilst the CAT does not apply the strict rule in *Hollington* it does, of course, endeavour to secure fairness but it is a sophisticated tribunal well able to form its own view on the value, if any, of prior findings.

102. The CAT, if confronted with prior findings said to be relevant, will carefully decide what weight can be attached to those findings. Without intending to be exhaustive, it will examine such matters as: whether the decision is a follow-on decision and the limits of the binding effect under section 60A CA 1998; where not a follow-on decision, the extent of the overlap between the prior findings of facts and the present case; who the earlier decision maker was and whether it was a specialist fact finder or otherwise; what the standard of proof was which was applied to the findings; and the nature of the legal analysis in the prior decision and the extent to which this affects the findings of fact made. The CAT will also consider to what forensic use the earlier findings are sought to be deployed. There might be many relevant uses some of which fall short of reliance upon earlier conclusions about the ultimate merits. The earlier decision might for instance identify relevant evidence and thereby demonstrate lines of inquiry relevant only to disclosure. The CAT will be conscious of the risk that being invited to perform a detailed inquiry into how prior findings came about draws it into disproportionate, satellite, litigation: see *Consumers Association* (ibid) paragraph [30].”

107. The decision in *FX* post-dates, and indeed in the passages quoted, makes reference to, a decision of the Tribunal in *Consumers’ Association v Qualcomm* [2023] CAT 9. Considerable reliance was placed upon *Qualcomm* by BT in respect of the effect upon this Tribunal of the Ofcom decisions. In that case, the Tribunal was asked to strike out certain passages in the Claimant’s Reply which referred to the decision of various foreign tribunals in relation to the Defendant’s licence practices, including royalties charged, which were the subject of the collective proceedings. The Tribunal struck out the relevant passages in the Reply on the basis that it would not be appropriate to attach any weight to the findings reached by other courts, tribunals or regulators. To do otherwise would risk the decision being made, at least in part on evidence which was not before the Tribunal. It would be impractical to even allow weight to be given to those other decisions because it would involve a detailed assessment of the evidence and arguments before those tribunals, leading to satellite litigation. The facts of that case are very different from ours and we do not read it to lay down a general rule that the decision of any other body, especially a regulatory body in the same jurisdiction, is inadmissible. More importantly, if it did, it has been overtaken by *FX*.
108. The question for this Tribunal is thus to consider the weight, if any, to be given to the findings of Ofcom in 2017. The same applies to any other views or actions of Ofcom which are said to be relevant. They may be of particular relevance where Ofcom has deployed or undertaken an evidenced-based analysis on a particular question. Perhaps unsurprisingly, each side has relied upon Ofcom’s views or findings where they were helpful to its case. Where a particular point is dealt with by Ofcom, especially in relation to factual matters, we deal with it below, insofar as necessary, in context.

## Prices and margins on the undertaking's other products

109. *Napp Pharmaceuticals v DGFT* [2002] ECC 13 involved an appeal to the Tribunal against a finding made by the DGFT that Napp had abused its dominant position in the supply of sustained-release morphine tablets and consequential orders. One of the arguments made by Napp was that:

“409...in an industry, such as the pharmaceutical industry, in which relatively few successful drugs must fund the research and development costs of many unsuccessful drugs, and the ongoing research costs of new products yet to be discovered, it is wrong to look at the margins of a single successful product and deem those margins, standing alone, to be excessive. The only sensible approach...is to look at the company's prices and profits over a portfolio of products and then judge whether its return on investment is reasonable on that portfolio basis. That is precisely what the PPRS does. Accordingly, says Napp, a company whose ROC is well within the limits of the PPRS cannot be judged to have charged excessive prices on a single product.”

110. The Tribunal rejected this argument. This was partly because Napp could not escape simply because there was a regulator in the industry and one which had approved its portfolio pricing. But it was also because such an argument

“...impermissibly directs attention away from the specific product market which we are required to consider when deciding whether there is an abuse of a dominant position under section 18 of the Act. In our view, it is not appropriate, when deciding whether an undertaking has abused a dominant position by charging excessive prices in a particular market, to take into account the reasonableness or otherwise of its profits on other, unspecified, markets comprised in some wider but undefined “portfolio” unrelated to the market in which dominance exists.”

111. A similar point was made by the Commission in its Commitments Decision in *Aspen* 10 February 2021 Case AT. 40394. At paragraph 204 it stated that:

“...cross-subsidisation between markets cannot give a dominant undertaking carte blanche to disproportionately hike up prices, especially in a context, such as that at stake, where the Products were profitable at portfolio level already before the price increases...”

112. However, it is important to distinguish what may be regarded as cross-subsidisation between separate activities from the situation in which the different activities of a multi-product firm share common costs, as arises here in the case of BT. Where common costs are shared across multiple outputs, this gives rise to an intrinsic interdependence between the profitability of those activities, and at least a degree of flexibility in the way in which those common costs might be recovered across the different products. This is a matter which we address below.

## Burden and Standard of proof

113. It is, of course, the case that the CR must prove its case on the balance of probabilities. We do not think it helpful to put any gloss on this.
114. BT makes a particular point based on the well-known observation of Lord Hoffmann in *Secretary of State for the Home Department v Rehman* [2001] 3 WLR 877 that while the standard of proof does not vary according to the seriousness of the case, it takes more compelling evidence to prove you saw a lioness in Regents Park than to prove you saw an Alsatian. It referred to this in the context of a reference to the decision of the Tribunal in a Chapter I prohibition case dealing with bid-rigging, *Durkan v Office of Fair Trading* [2011] CAT 6. What the Tribunal said there was this:

“93. It is common ground that the legal burden of proving the existence of an infringement of the Chapter I prohibition lies on the OFT (see *Napp Pharmaceutical Holdings Ltd v Director General of Fair Trading* [2002] CAT 1 (“Napp”), paragraph 95).

94. The question of the standard of proof has been considered in a number of cases. In *Napp*, at paragraph 109, and *JJB Sports plc and All Sports Limited v Office of Fair Trading* [2004] CAT 17 (“JJB”), at paragraph 204, the Tribunal held that the standard of proof is the civil standard of proof on the balance of probabilities. The seriousness of an infringement of the Chapter I prohibition, involving (as here) the imposition of penalties, is a factor to be taken into account in considering the probability of an infringement having occurred. We were referred by Mr Beard to the well known passage from the speech of Lord Hoffmann in *Secretary of State for the Home Department v Rehman* [2001] 3 WLR 877 concerning the relative likelihood of coming across Alsations and lions in Regent’s Park and to a passage in the opinion of Lady Hale in *In Re B* [2008] 3 WLR 1 where she stressed that the seriousness of an allegation of misconduct is not necessarily a factor which makes it less likely that the allegation is true: context is everything. We agree with the OFT’s submission that both those points are relevant here because, although the alleged infringement is a serious one, many of the addressees of the Decision asserted that this kind of conduct had been widespread in the industry and infringements have been admitted by a very large number of companies.

95. It is incumbent on the OFT to adduce precise and consistent evidence in order to establish the existence of an infringement. But it is sufficient, according to the caselaw, if the body of evidence relied on by the OFT, viewed as a whole, meets that requirement: see *JJB*, at paragraph 206.”

115. We agree with what is said there, although we do not think it is particularly relevant in this case.

### **FACTUAL MATTERS (1): BT’S MARKET SHARE**

116. On the assumption that the relevant market is SFV Services, Mr Parker has calculated BT’s market shares, principally using information supplied by Ofcom, which itself received information from BT and the other operators up to the end of 2017, after which he extrapolated the position (see Section 5.2 of DP3). The experts agreed the market share results put forward by the experts in respect of their respective market definition (see JES p81). In summary:

- (1) For the subclass of VOCs and for the period prior to the introduction of the Commitments on 1 April 2018, BT’s market share in terms of number of lines was between 64% and 76%, and when measured in terms of revenue was between 70% and 78%;
- (2) For the subclass of SPCs and for the period prior to the introduction of the Commitments on 1 April 2018, BT’s market share in terms of number of lines was between 97% and 98%, and when measured in terms of revenue was also between 97% and 98%;
- (3) For the subclass of SPCs and for the period after the introduction of the Commitments on 1 April 2018, BT’s market share in terms of number of lines was between 95% and 96%, and when measured in terms of revenue was between 96% and 97%;
- (4) For the subclass of VOCs and for the period after the introduction of the Commitments on 1 April 2018 (when in fact VOCs were no longer in the Class) BT’s estimated market share in terms of number of lines was between 54% and 64%, and in terms of revenue was between 61% and 68%, if the previous market share had continued;



- (5) For SFV services as a whole, i.e. both sub-classes combined, up to the introduction of the Commitments, BT's market share in terms of the number of lines was between 74% and 85% and when measured in terms of revenue was between 78% and 86%;
  - (6) All of the above figures relate to market share of lines i.e. "access"; if one were to look at market share in terms of "non-access" i.e. calls, across SFV Services:
    - (a) For the pre-Commitments period, when measured by the number of minutes, BT's share was between 71% and 80%, and, when measured by revenue, BT's share was between 84% and 85%; and
    - (b) For the post-Commitments period, when measured by the number of minutes, BT's share was between 63% and 71%, and when measured by revenue, BT's share was around 84%;
  - (7) Finally, in terms of SFV revenues as a whole for the period 2013-2018, and using Ofcom data for the period up to 2014 and extrapolating thereafter, BT's market share was between 82% and 85%.
117. We should add that, while the content of paragraphs 116(5) and 116(6) is said to have been agreed by the CR, we do note that these sub-paragraphs involve questions of ARPMs which were disputed and imply pricing by BT higher than its competitors. That said, this point does not affect our assessment of dominance here.
118. The other telecoms companies which provided SFV Services were the Post-Office, TalkTalk, SSE, Virgin Media, Sky, Phone-Co-op, Direct Save Telecom, Plus Net and Utility Warehouse. These companies all provided data to Ofcom as at 2017 for the purposes of Ofcom's 2017 review. Mr Parker did not include Phone-Co-op's figures for the individual sub-classes because he said that it had █% share of each of those markets. The figures for Direct Save Telecom, Plus Net and Utility Warehouse were also excluded on the basis that the Ofcom data indicated that their market shares were immaterial. It is important to note, as the next paragraph shows, that suppliers may continue to supply a voice-only product, for example to its existing customer base, while not promoting, or actively promoting, or even supplying it, for the purpose of new customers.
119. The position in respect of the other suppliers is as follows:
- (1) The Post Office sold its telecoms business to Shell Energy in March 2021. Shell Energy continued to sell SFV Services to new customers until September 2022;
  - (2) TalkTalk stopped actively marketing SFV Services to new customers in 2014, and stopped providing them altogether to new customers by December 2016;

- (3) Virgin Media [REDACTED] [REDACTED] did not strongly promote these services from August 2021;
- (4) Sky [REDACTED] [REDACTED] withdrew SFV services to new customers in 2019;
- (5) SSE [REDACTED] sold its telecoms business to OVO in 2020, which then ceased marketing SFV services to new customers;
- (6) The above is drawn from information provided by the suppliers to Ofcom for the purposes of the 2017 Provisional Conclusions (see paragraph A8.56 of Annex 8 thereto) and the 2020 Report (see paragraphs 3.6 and 3.7 thereof), together with Dr Jenkins' Figure 7.5 under paragraph 7.67 of HJ1, which is based on an analysis of the Pure Pricing database for pricing of Voice services for key fixed line operators in the UK at F/781. The database covers the four product areas of Line rental, Line rental saver products, Voice bundles and Call packages.

### **Background and the Basics of BT's Pricing**

120. BT's voice pricing comprised line rental (a fixed monthly charge) and call charges (which can be either a series of prices per minute for different categories of call, and/or a fixed monthly price for a certain package of calls).
121. While the line rental charge is transparent and easily identified, call charges are more complex and difficult to compare between packages or between operators. The amount of revenue they generate for the provider (and the price paid by the consumer) depends on both the prices and the extent to which voice calls are made.
122. The tariff of BT's voice call charges offered to consumers is largely the same for all voice customers, whether or not they purchased voice services as part of a bundle. But the actual uptake of the different packages depended on user choices – many bundle customers did not make voice calls at all from their landlines.
123. BT's standard line rental ("SLR") has also been the same for all voice customers, whether SFV or bundle customers, though the line rental element in any given bundle forms only a part of the bundle price. Different (non-standard) line rental prices were offered by BT to some customer groups such as those qualifying for the Home Phone Saver package ("HPS"), and (from 2018) those identified as VOCs following the Commitments.

124. There has been substantial change over time in the composition of voice prices, from a classic utility pricing model (comprising a fixed fee plus usage-based charge) towards a greater reliance on fixed subscription-based charges (with either no or less emphasis on the per-call element). This change in part reflects the competition faced from mobile phone contracts which have moved towards a fixed price for a package of calls.
125. There has also been a significant reduction in the volume of calls made from landlines. Figure 2.3 of HJ2 summarises the Ofcom data on UK market voice calls: the total for fixed line voice calls fell by over 75% from over 160m minutes in 2007 to around 35m in 2022. Meanwhile, the number of mobile voice minutes increased from just over 100m to 170m across the same period.
126. This creates a complex factual background to the analysis of market prices and price changes, under which it is not simple to identify a definitive ‘price per unit’ charged by BT or its rivals for the SFV products in question. We return to this below in the context of the market definition and dominance assessments.

### Line Rental Pricing

127. BT’s prices for SLR are shown in the two following tables from DP3. As between April 2017 and September 2018, the price of £18.99, imposed in July 2016, was frozen, and it dropped in the case of VOCs as from 1 April 2018 to £11.99.

**Table 13 BT’s Standard Line Rental price increases, pre-Commitments**

Date	Price Increase Name	BT SLR		
		Price	Change (£)	Change (%)
01/10/2010	Pacific	£13.29	£0.50	4%
28/04/2011	Atlantic	£13.90	£0.30	2%
03/12/2011	White	£14.60	£0.70	5%
05/01/2013	Beech	£15.45	£0.85	6%
04/01/2014	Pegasus	£15.99	£0.54	3%
01/12/2014	Window	£16.99	£1.00	6%
20/09/2015	Laika	£17.99	£1.00	6%
03/07/2016	16/17 Price Change	£18.99	£1.00	6%

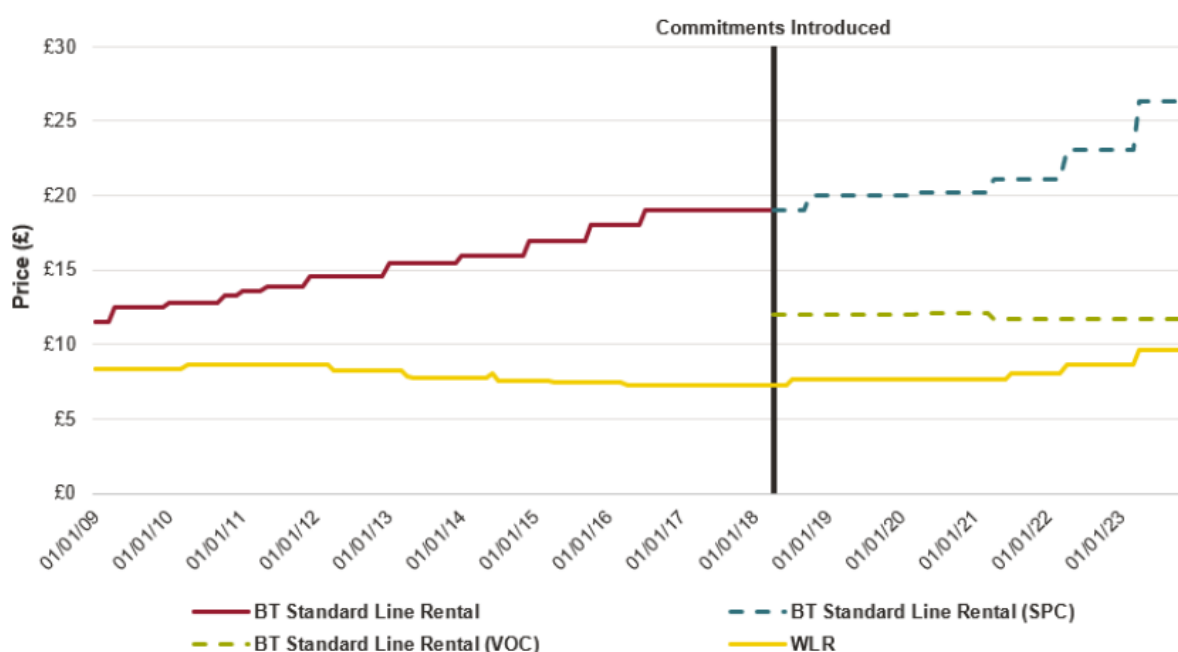
**Table 14 BT's Standard Line Rental price increases, post-Commitments**

Date	Name	BT SLR (for Split Purchase Customers)			BT SLR (for Voice Only Customers)		
		Price	Change (£)	Change (%)	Price	Change (£)	Change (%)
01/04/2018	Commitments Introduced	£18.99	£0.00	0%	£11.99	£-7.00	-37%
16/09/2018	18/19 Price Change	£19.99	£1.00	5%	£11.99	£0.00	0%
31/03/2020	Price Change 2020	£20.20	£0.21	1%	£12.14	£0.15	1%
31/03/2021	Price Change 2021	£21.10	£0.90	4%	£11.73	£-0.41	-3%
31/03/2022	Price Change 2022	£23.05	£1.95	9%	£11.73	£0.00	0%
31/03/2023	Price Change 2023	£26.35	£3.30	14%	£11.73	£0.00	0%

128. We should add that the dates given above are when the various price changes came into effect. Typically, they were announced around 3 months before they came into effect – see Annex 2 to JB2.

129. In order to provide a voice service to a household, the retail operation of BT needs to buy in a wholesale line rental (“WLR”) service from Openreach. Other retailers like TalkTalk also have to buy a relevant wholesale product from Openreach unless they have their own network, like Virgin. WLR costs were generally decreasing prior to the Commitments, and then increasing somewhat afterwards, as shown in the Chart below:

**Chart 1: BT Standard Line Rental price increases compared to cost inputs, 2009-2023**



130. One can see from this chart that the gap between SLR and the WLR paid by BT to Openreach has widened considerably – from around £4 to around £11.50 at the time of the Commitments and (for SPCs) to more than £15 by 2022. This visible ‘alligator jaws’ image was cited by the CR and his

experts as evidence of BT's exercise of market power, but it is only part of the picture. There were other factors at play that need to be taken into account (see paragraph 140 below) before any robust conclusions could be drawn as to the effect of the SLR price increase on the SFV customers.

131. The line rental charge pricing of the other telecoms operators in relation to BT's pricing is set out in the following Table which comes from paragraph 5.80 in DP3:

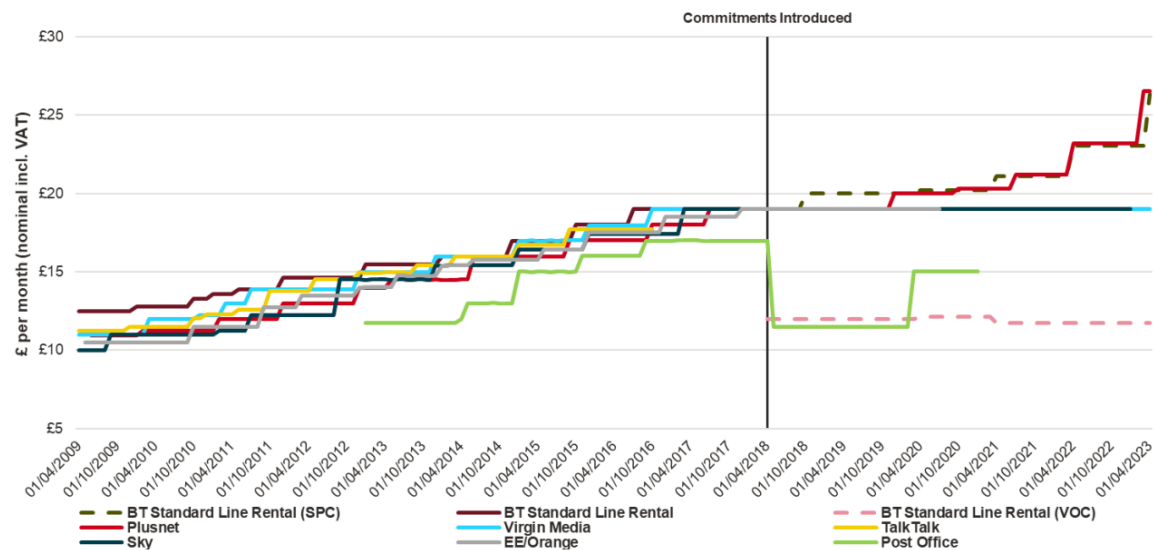
**Table 12 Price changes of the line rental component of BT Standard Line Rental compared to competitor products, April 2009 – April 2018**

Date	BT	Plusnet	Virgin Media	TalkTalk	Sky	EE/ Orange	Post Office
01/04/2009	£12.50			£11.25		-	-
01/06/2009							-
01/09/2009					£11.00		-
01/12/2009				£11.49			-
01/01/2010	£12.79						-
01/02/2010		£11.25					-
01/03/2010			£11.99				-
01/10/2010	£13.29			£12.04		£11.50	-
01/11/2010			£12.24				-
01/12/2010				£12.30			-

01/01/2011	£13.60					-
01/02/2011		£11.99		£11.25		-
01/03/2011			£12.99			-
01/05/2011	£13.90			£12.60		-
01/07/2011			£13.90		£12.25	-
01/09/2011					£12.75	-
01/10/2011				£13.80		-
01/12/2011	£14.60	£12.99				-
01/03/2012					£13.50	-
01/05/2012				£14.50		-
01/09/2012					£14.50	-
01/12/2012		£13.99	£14.99	£14.95	£14.00	-
01/01/2013	£15.45					
01/05/2013		£14.50				
01/06/2013					£14.75	
01/09/2013				£15.40		
01/12/2013			£15.99		£15.40	
01/01/2014	£15.99				£15.40	
01/03/2014				£15.95		
01/04/2014						£12.00
01/05/2014						£13.00
01/06/2014		£15.95			£15.75	
01/12/2014	£16.99					
01/01/2015			£16.99	£16.70	£16.40	£15.00
01/05/2015					£16.40	
01/09/2015		£16.99		£17.70		
01/10/2015	£17.99					
01/11/2015						£16.00
01/12/2015			£17.99		£17.40	£17.50
01/07/2016	£18.99					
01/09/2016						£16.99
01/10/2016		£17.99	£19.00			
01/12/2016				-	£18.50	
01/03/2017				-	£18.99	
01/07/2017		£18.99		-		
01/12/2017				-	£19.00	

132. Put graphically, the various line rental prices of BT's competitors, as compared with its own such prices, can be seen from the following Figure which is under paragraph 5.79 of DP3:

**Figure 22 Prices of the line rental component of BT Standard Line Rental compared to competitor products, April 2009 – April 2023**



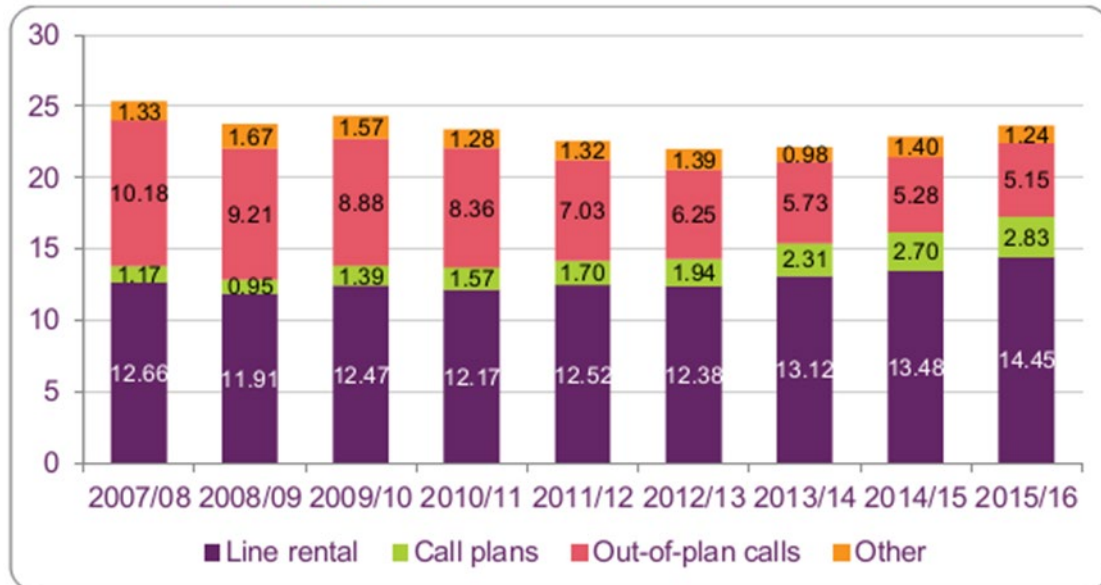
## Call Charges

133. The charges made by BT and its rivals for both individual calls and call plans were subject to a variety of changes both before and during the claim period including changes in the balance between per-minute, package and fixed charges. These changes took place against a background of declining call volumes. On the actual prices charged by BT and its rivals for call packages and out-of-plan calls, Dr Jenkins’ analysis at paragraphs 7.73-7.77 of HJ1 shows that overall, BT’s prices for call plans and out-of-plan calls were largely comparable with and were sometimes exceeded by the prices of its competitors. This was the view of Ofcom also.
134. The CR claimed that if one measured the price of calls by ARPM (i.e. average revenue per minute), a very different picture emerges with BT’s ARPMs consistently above those of its rivals. However, there are difficulties with this analysis, as we explain at paragraphs 380-390 below.

## ARPU

135. Line rental and call charges, and changes in call volumes, are brought together in measuring the total voice revenue received from each customer - the so-called Average Revenue per User (“ARPU”). It is common ground that, broadly speaking, first, ARPU has been relatively flat in real terms since at least 2007 until the end of the claim period, Mr Parker observing in DP2, at paragraph 2.30, that “Average revenue per line was relatively stable over time”. See Figure A5.4 below from the Annexes to the 2017 Provisional Conclusions:

**Figure A5.4: BT's SFV revenues (£ per line per month, ex. VAT, CPI adjusted for December 2016 prices) [X]**

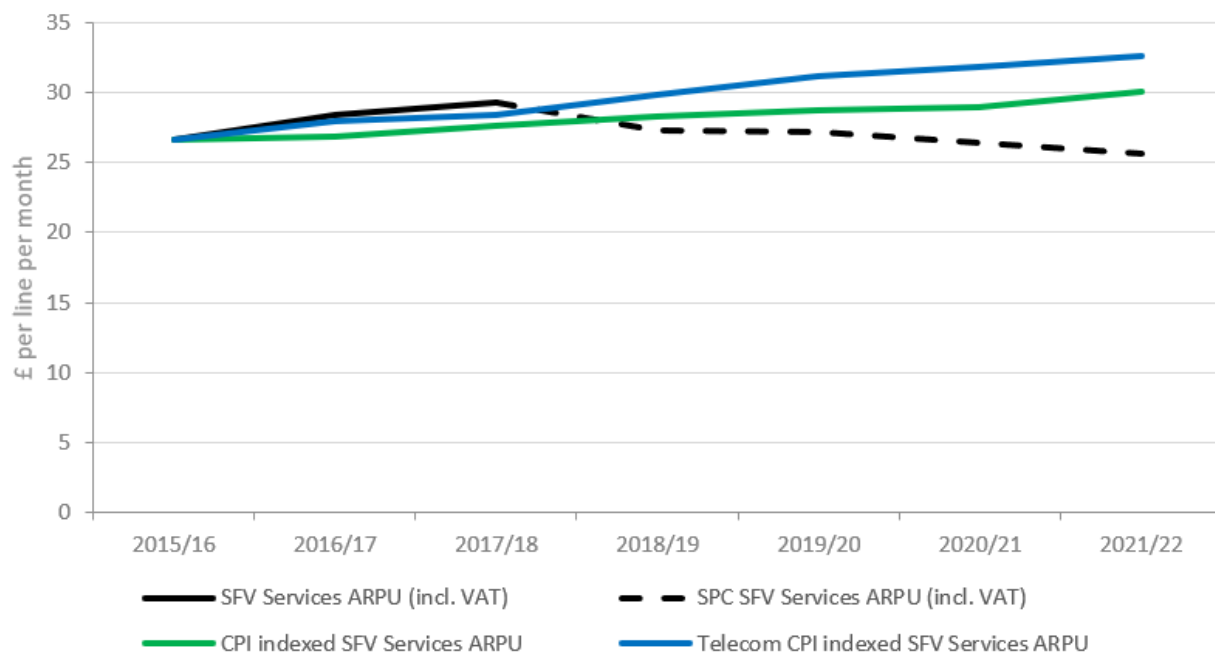


Source: Response dated 24 June 2016 to questions 2 and 3 of the 10th BT s.135 under the NMR and 9 December 2016 to questions 5 and 6 of the 2nd BT s.135.

136. As from the start of the claim period, ARPU rose in nominal terms between 2015/16 and 2017/18 before declining and with a nominal decrease of 3% at the end of the claim period, compared with the start of it, as is shown by Figure 7.4 from HJ1:



**Figure 7.4 Change in ARPU for SFV Services over time**



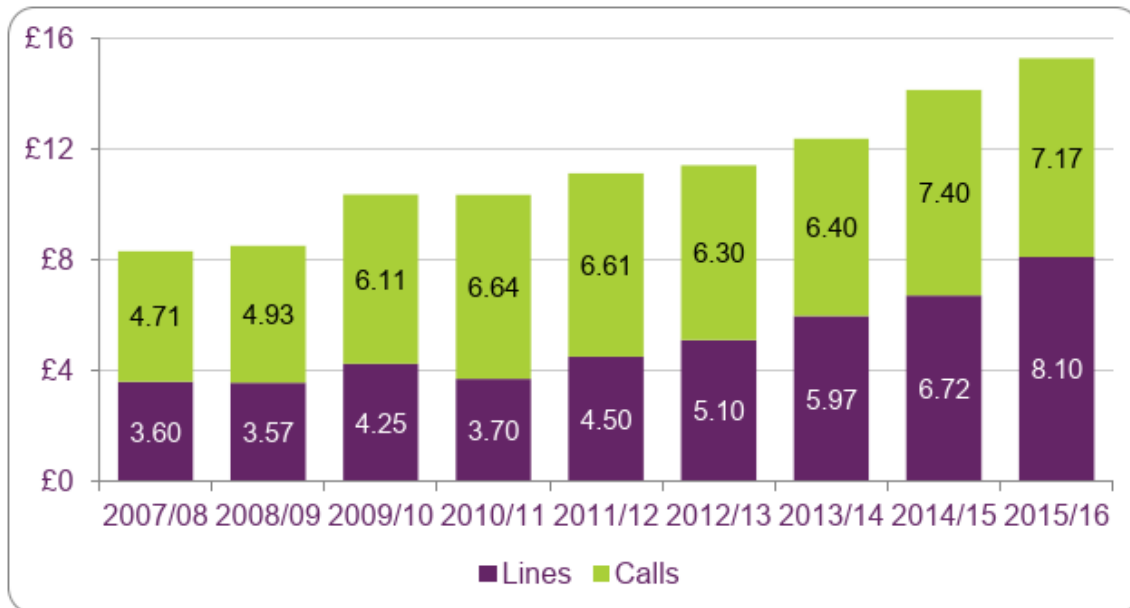
Notes: Series does not start until 2015/16 due to the availability of relevant disclosure information.

Source: Oxera analysis based on data from ONS and the F19 Summary (BT00092355), the F18 and F20 Summary (BT00092336) and F21 Summary (BT00092356).

## Gross Margin

137. Chart 1 under paragraph 129 above shows a steadily increasing gap between BT's line rental price and the WLR price it paid to Openreach.
138. Gross margin overall, i.e. for access and calls can also be shown from Figure A5.10 in the Annexes to the 2017 Provisional Conclusions.

**Figure A5.10: Estimated gross margins for line rental and calls (£ per line per month, CPI adjusted for December 2016 prices) [3<]**



Source: Response dated 24 June 2016 to questions 2 and 3 of the 10th BT s.135 under the NMR and 9 December 2016 to questions 5 and 6 of the 2nd BT s.135.

139. As for the claim period onwards, Dr Jenkins' Table 4 from Annex B3a to the JES shows effective percentage gross margins for SFV Services of around 65% across the entire claim period and for bundles, from around 36% to 40%. In absolute (cash) terms the gross margins per customer from bundles are higher than from SFV Services in every year of the claim period.

**Table 4 Gross margin per customer buying fixed voice services in a bundle and SFV Services customer**

	Formula	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
<b>Bundles<sup>1</sup></b>								
Revenue (£m)	[A1]	3,397	3,805	3,945	4,066	3,986	3,598	3,688
Cost of Sales (£m)	[B1]	2,006	2,388	2,517	2,537	2,556	2,402	2,423
Gross margin (£m)	[C1] = [A1] – [B1]	1,391	1,417	1,428	1,529	1,431	1,196	1,265
Number of customers (#m)	[D1]	6.4	6.7	6.7	6.5	6.3	6.1	5.6
<b>Gross margin per customer (£/line/year)</b>	[E1] = [C1] / [D1]	217.99	212.84	213.74	236.90	228.78	194.68	224.33
<b>SFV Services</b>								
Revenue (£m)	[A2]	724	607	503	174	138	110	83
Cost of Sales (£m)	[B2]	251	212	172	64	50	40	33
Gross margin (£m)	[C2] = [A2] – [B2]	473	395	331	110	88	70	51
Number of customers (#m)	[D2]	2.7	2.1	1.7	0.6	0.5	0.4	0.3
<b>Gross margin per customer (£/line/year)</b>	[E2] = [C2] / [D2]	173.61	184.40	192.22	172.42	173.80	167.71	156.07
<b>Difference in margin (£/line/year)</b>	[F] = [E1] – [E2]	44.38	28.44	21.52	64.48	54.97	26.97	68.26

140. The evidence on ARPU, summarised at paragraphs 135 and 136 above suggests that the combined effect of increases in line rental charges, changes in the levels and composition of call charges, and declining call volumes have combined to deliver the broadly flat ARPU from SFV customers since 2007. How this plays into the evidence on SFV profitability depends on how this flat ARPU compares with the cost of providing these Services, given the movements that have been observed in WLR per customer and the impact that declining call volumes has had on BT's costs.

141. The most effective way to take these other factors into account is to look at BT's margins on SFV customers over time, focusing on the margin between ARPU and costs. When this exercise is done, it shows that, gross margins (i.e. ARPU minus direct costs) increased from around £8 to £15 per line in real terms, an increase in percentage gross margin on sales from around 32% to 63% (see Ofcom's Figure A5.10 at paragraph 138 above). This 63% gross margin in 2015 is very close to the experts' agreed gross margin SFV calculations throughout the claim period, which stand at around 65%.

## **FACTUAL MATTERS (2): OFCOM AND BT**

### **Background**

142. We have summarised some aspects of Ofcom's involvement at paragraphs 11 - 16 above. We add some more detail here.
143. Until 1981, BT was the monopoly provider of telecommunications services, with statutory restrictions preventing market entry. It was then privatised in 1984, following which it was subject to retail price controls which included capping its SFV Services prices. Prior to 2006, BT had been determined by Oftel, then Ofcom, its successor, to have SMP. By section 78 of the Communications Act 2003, a person had SMP in relation to a market if it enjoys a position which amounts to or is equivalent to dominance of the market. A firm which has SMP is then subject to various forms of regulation including price control.

### **2006**

144. In 2006, Ofcom consulted on whether retail price control should continue beyond 31 July 2006 (when the then current set of controls came to an end) in its "Retail Price Controls: Explanatory Statement and Proposals" dated 21 March 2006 ("the 2006 Consultation"). By its "Retail Price Controls: Explanatory Statement" dated 19 July 2006 ("the 2006 Statement"), Ofcom decided that there would no longer be retail price controls as from 1 August 2006. In its conclusions, it said this:
- "5.15 In reaching a conclusion concerning the expiry of the RPC, Ofcom has balanced the consequences of BT's continued market power in these markets with its view of the extent to which other factors – chiefly competitive pressure and other regulation – limits BT's ability to set excessive prices.
- 5.16 Ofcom considers that allowing expiry of BT's retail price controls but underpinned by BT's assurances and supported by an extensive communications campaign meets the requirements set out in Sections 3 and 4 (above). The interests of consumers will be served by their increased awareness of the choices available and with increasing competition engendered by appropriate wholesale regulation. This in turn should lead to new services greater choice for consumers and further reductions in retail prices."
145. Because BT was still deemed to have SMP, it was subject to other regulatory controls, for example, the duty not to discriminate, price publication and notification requirements, along with providing regulatory financial statements (RFSs). It also remained unable to sell bundles with fixed voice services, even though rival telecoms retailers did offer such bundles.

## 2009

146. In 2009, Ofcom consulted further, on whether BT still had SMP – see its “Fixed Narrowband Retail Services Market Review, Consultation,” dated 19 March 2009 (“the 2009 Consultation”). By its “Fixed Narrowband Retail Services Markets: Identification of markets and determination of market power” dated 15 September 2009 (“the 2009 Statement”), Ofcom determined that BT no longer had SMP. Ofcom therefore removed remaining regulatory controls. This enabled BT to sell bundles with fixed voice services and it was no longer required to provide separate cost accounting for SFV Services, including providing RFSs.

## 2013

147. On 26 September 2013, Ofcom published its “Statement: Review of the Fixed Narrowband Services Markets” (“the 2013 Statement”), in which it concluded (inter alia) that “the fixed voice retail calls markets in the UK (excluding the Hull Area) remain effectively competitive and no company holds a position of SMP”.

## 2014

148. On 28 January 2014, Ofcom published its report on the “Cost and Value of Communications Services in the UK” (“the 2014 Report”). It noted as follows at paragraph 2.1.6:

“There is an active market in the UK for standalone (i.e. not bundled) fixed line rental services. Retail competition is enabled by regulated access to wholesale line rental, the price of which has fallen and will continue to fall. This has enabled the provision of competitive services by other providers. For example, the Post Office currently offers a standalone landline service for £12 per month.

Social tariffs are also available as a low cost option for low income users. The price of BT Basic, the principal social tariff, is lower now in real terms than it was six years ago. This is a good choice for eligible consumers with low outbound call usage (for example, for consumers who rely more on receiving than making calls to keep in touch). Eligibility is defined as being in receipt of certain benefits available to low income households.

Despite this range of choice and the overall positive trend in fixed voice costs, some retail prices for line rental have increased in recent years. This is related to the fact that landlines generally tend to be sold as a bundle with other products – historically with voice calls, more recently with broadband. Market competition has tended to focus on the headline price of the bundle, which has generally fallen. Consequently consumers buying a landline service without broadband may not benefit fully from the effects of competition. Furthermore, some providers (TalkTalk and Virgin Media) have recently ceased their standalone landline service. Ofcom will continue to monitor this situation carefully.”

## 2015

149. In March 2015, Ofcom announced a Strategic Review of Digital Communications and in July 2015, it published a Discussion Document. As the title suggests this was principally about broadband but also mobile services as opposed to landline telephone services.
150. On 7 October 2015, Sharon White, the (then) CEO of Ofcom, gave a speech at the LSE, in which she stated that landline and broadband prices had risen in recent months “without the apparent justification of higher costs or improved service”, and that BT and three other providers had raised

line rental prices that year. She said Ofcom was “concerned about this” and was watching the market “closely”.

## 2016

151. On 25 February 2016, Ofcom published its “Initial conclusions from the Strategic Review of Digital Communications” (“the 2016 Statement”). Notwithstanding the general focus of this review, it noted as follows:

“7.9 We have particular concerns about the situation for consumers who use standalone landline services. These consumers generally do not engage with the market: 71% of standalone landline customers have never switched provider or considered doing so. These customers tend to be older and more vulnerable. Almost 60% of consumers who buy standalone landline products and have no broadband service are over-75 and nearly half (47%) live in DE households on the socio-economic scale. Actions to empower these consumers may not be enough on their own to produce a very different market outcome.

7.10 A number of changes can be observed in stand-alone landline services:

- different providers’ prices are converging towards higher levels. For example, the Post Office has increased its prices after significantly undercutting BT a few years ago;
- line rental prices are rising, despite the price of wholesale services on which they are based falling (see Figure 17);
- rising prices for both call bundles and out-of-bundle calls; and
- less choice among the larger providers. For example, TalkTalk no longer offers a standalone landline service while Sky and Virgin Media do not actively promote this product.”

152. The 2016 Statement did not itself propose any direct changes so far as landline services were concerned save in respect of the relationship between BT and Openreach which affected both landline and broadband. However, in the course of 2016, Ofcom was having discussions with BT about its landline pricing, among other things.
153. However, on 4 May 2016, the Advertising Standards Authority (“the ASA”) announced new rules in relation to broadband advertising. These prohibited providers of bundles from advertising only the ‘incremental broadband price’ (i.e. the part of the bundle price attributed to the charge for broadband only) but not the total price of the bundle, which included the line rental, which was often significantly more than the broadband charge. The new rules, which came into effect on 31 October 2016, required bundle providers to “[s]how all-inclusive up-front and monthly costs; no more separating out line rental.”
154. In December 2016, Ofcom launched its Review of the Market for Standalone Landline Telephone Services (“the Landline Review”).

## 2017

155. As already noted, the 2017 Provisional Conclusions in respect of the Landline Review were published on 28 February 2017. It provisionally found that the market for SFV Services was different from the bundles market, and that BT had SMP in respect of the former market. In the context of its market definition analysis, it said that current SFV line access prices were substantially above competitive levels.

156. There are 10 Annexes to the 2017 Provisional Conclusions. Annex 8 consisted of the supporting evidence relied upon by Ofcom (“Annex 8”). The executive summary of the 2017 Provisional Conclusions included the following:

“1.5 However, customers that do not take bundled services have not benefited from competition in the same way. We are particularly concerned about people who only buy a landline from a provider – either because they do not want broadband or pay-tv, or because they take these services separately, usually from different companies.

1.6 Our concerns are that relative to those who purchase services in a bundle, these consumers have less choice of suppliers, are not benefiting from strong price competition or promotional offers and their loyalty to their suppliers is leading to ever higher prices. Further, while price increases up to 2013 might have been explained by the rebalancing of revenue from calls and the line rental, since then we have observed a more rapid inflation and it is now clear we need to act. Data relates to the proportion of customers self-reporting a bundle of services, and understates the proportion purchasing multiple services from a single provider. We use this to allow for comparability with 2009 data. Revised analysis for 2016 based on the main provider used for each service is reported in Figure A8.1. This analysis also defines those who pay line rental in addition to their broadband service, as a bundle.

1.7 We have found that these customers – often elderly people who have remained with the same landline provider for many decades – are getting increasingly poor value for money. They are particularly affected by price increases, and, we consider, are in need of additional protection in a market that is not serving them well enough.

1.8 To address this situation, we are now proposing to cut the price of BT’s standard line rental by at least £5 per month for customers with standalone landline contracts. Thereafter BT would only be allowed to increase its average prices for line rental and calls in line with inflation.”

1.9 ...From December 2009 to December 2016, line rental prices have risen by between 25% and 49% in real terms. At the same time, the wholesale costs for providing landline services have fallen by up to 26% in real terms. Wholesale costs are represented by the WLR and MPF lines in Figure 1.2. These two wholesale products are used by providers to offer retail line rental services to consumers.

1.10 This fall in the wholesale costs has allowed more competitive pricing in the bundled market but for landline only has simply meant that the profit in the provision of this service has grown significantly...

1.11 This trend is observable across all major providers of landline services – not just BT. We are therefore concerned that standalone landline telephone consumers are increasingly worse off compared to consumers of bundled services.

1.12 There are currently about 2.9 million standalone landline consumers which account for 11% of total residential landline customers. They fall into two categories:

- About 1.7 million consumers buy landline services but do not purchase fixed broadband. We refer to this group as “voice-only” consumers.
- Approximately 1.2 million consumers buy both landline and broadband services but on a standalone basis outside of a bundle. They have faced the same line rental price increases as voice-only consumers and have not benefited from competition in bundles. We refer to this second group as “split purchasers”.

1.13 Standalone landline customers generally do not engage with the market: 70% of standalone landline customers have never switched provider or considered doing so. They tend to be older and less likely to shop around for a better deal. Approximately 43% of standalone landline customers are at least 75 years old, and 35% live in DE socio-economic group households (for comparison, 4% of dual-play customers are 75 or over, and 20% are in DE group households)...

1.17 BT benefits from a very high market share; over 70%, in a market where many customers are not actively engaged. This in turn has allowed BT to act as a price leader, steadily increasing the price of standalone landline services. Further, given the difficulty in winning new customers from BT, the range of choice from competing providers has declined as prices have increased.

1.18 As illustrated in Figure 1.2 above, BT has been able to raise prices to its standalone landline telephone customers despite falling costs.

1.19 A key reason for the decline in costs has been reductions in regulated charges for wholesale inputs. However, while wholesale regulation has supported competition in bundles, as we have discussed, it has clearly not been able to sufficiently protect these standalone customers.

1.20 Consequently, we consider we need to act directly in the retail market through regulation of BT's retail landline services...

4.7.2 Experience of switching: Around 70% of SFV 93 customers report that they have never switched provider. Many of these respondents are likely to have been with BT since it was the monopoly provider of fixed line services (see paragraph 4.39.1 below). In contrast, dual-play services are relatively new, and 26% have switched provider in the past 3 years."

157. Following negotiations with Ofcom in 2017, BT volunteered the Commitments, which included: (i) a reduction of £7 on the monthly line rental price for VOCs; (ii) a Consumer Price Index ("CPI") cap on future price increases, based on a basket of SFV calls and access services for VOCs; and (iii) a commitment to provide SPCs with an annual statement setting out the customer's annual spend and savings available if landline and broadband services were bought as a bundle. The price cut did not apply to: SPCs; VOCs who bought BT Basic (later named BT Home Essentials) or BT Home Phone Saver ("HPS"); and any VOCs who were businesses.
158. These Commitments were noted in the 2017 Statement. This essentially maintained the views expressed in the 2017 Provisional Conclusions and explained its approval of the offered Commitments. See paragraph 15 above. The 2017 Statement was accompanied by three Annexes. The third Annex described the supporting information for the Statement which included a document itself called "Evidence Supporting the Statement" ("the Evidence"). This served the same function as Appendix 8 to the 2017 Provisional Conclusions. In the Statement, Ofcom maintained its earlier view and pointed out that line rental prices had risen by between 23% and 47% in the period from December 2009 to June 2017, while the wholesale cost of providing these services had fallen by 27% in real terms.
159. In the summary, the 2017 Statement concluded as follows:

"1.10 Since the February Consultation, we have been made aware that providers of standalone telephony services on Openreach's network are in fact able to identify which of their customers are voice-only and which are split purchasers. Therefore, while providers have not so far set different prices (or other terms and conditions) between these two customer groups, they could do so if they wished. Accordingly, we are no longer of the view that voice-only and split-purchase customers should be considered part of the same market.

1.11 While we have concerns about the current outcomes for both customer groups, our concerns are more acute for voice-only customers. Voice-only customers generally do not engage with the market: 77% of voice-only customers have never switched provider or considered doing so. They tend to be older and less likely to shop around for a better deal. Over 40% of voice-only customers are at least 75 years old, and 40% live in DE socioeconomic group households (for comparison, 5% of dual-play customers are 75 or over, and 20% are in DE group households).<sup>5</sup> Moreover there are now relatively few providers of landline only services for these consumers to choose from.

1.12 Even if measures to promote engagement and competition for voice-only customers are successful, they are likely to take time to have an impact (and there are challenges to them being successful, which requires both that voice-only customers engage more actively and also that this stimulates a growth in the existing, limited competition). BT currently holds a dominant position in the market for voice-only customers and the lack of competition enables it to maintain prices above the competitive level.

1.13 We therefore consider that a significant price cut is important to alleviate the detriment suffered by voice-only customers. We are also in favour of providing information to consumers, because of the potential benefits in encouraging their engagement in the market and greater competition.

1.14 Like voice-only customers, split purchasers have suffered increases in line rental charges in recent years without significant offsetting benefits. However, split purchasers are typically younger and more technologically literate, and, by definition, have internet access which allows them to access alternative offers more easily. Unlike voice-only customers, split purchasers have a wide range of choices available to them, such as dual-play (telephone and broadband) bundles, which should allow them to seek better value for money from providers if they increase their levels of engagement.

1.15 To address the detriment faced by split purchasers we have decided that it is more appropriate to allow time for split purchasers to become more actively engaged and potentially switch to dual-play bundles where that is a better option for them, than to include them in a price control at this stage. Split purchasers may benefit from being informed that, in many cases, they are not obtaining good value for money and can find themselves a better deal.”

160. We should point out that the actual text of paragraph 1.11 said that 55% of dual play customers were over 75 rather than 5%. The reference to 55% is clearly an error - see the underlying evidence referred to and relied upon at page 35 of the Evidence.

161. In accepting BT’s proposals, Ofcom said:

“1.20 We consider that BT’s voluntary proposal addresses our concerns over the prices offered to voice-only customers. It brings line rental prices back down to levels last seen in 2009 in real terms, as shown in Figure 2 below. It reverses the trend of recent years for ever higher prices and goes further to ensure that prices are constrained by CPI for the next three years.

1.21 BT has also agreed to improve its communications with its voice-only customers to provide information on potential savings and the switching process.

1.22 For split-purchase customers, the focus of BT’s proposal is now solely on encouraging engagement through an annual statement. We consider that this, plus the absence of a price cut, might encourage them to engage more actively with the deals available in the market for dual-play and other bundles. Additionally, we will be exploring other types of prompts or tools for consumers more generally in our consumer engagement project. We launched this project in July 2017 through a call for inputs.

1.23 We therefore consider that BT’s voluntary proposal is sufficient to address our concerns in relation to this review. Accordingly, we have decided against the imposition of formal regulation at this time.”

## **2020 and 2021**

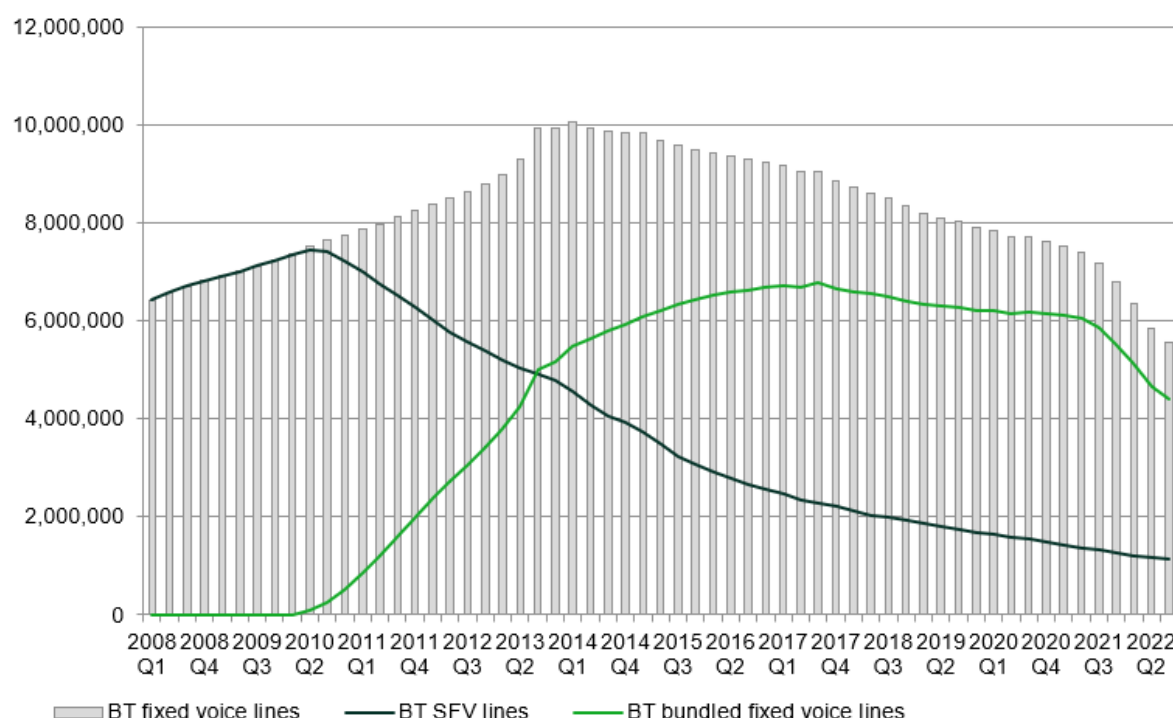
162. In its 2020 Consultation, Ofcom considered that price protection for VOCs “remains necessary to address our previous concerns from our last review in 2017” because there “is little competition in the market for this group of customers”. In the 2021 Statement (see paragraph 16 above), Ofcom accepted a new set of voluntary commitments from BT for a further five-year period from March 2021 which applied an inflation-linked control on a basket of SFV calls and access services to VOCs. Ofcom did not assess SFV prices charged to SPCs in the 2020 Review, nor did it propose that BT now make price cuts to this part of the service, as it had for VOCs.



### **FACTUAL MATTERS (3): SWITCHING**

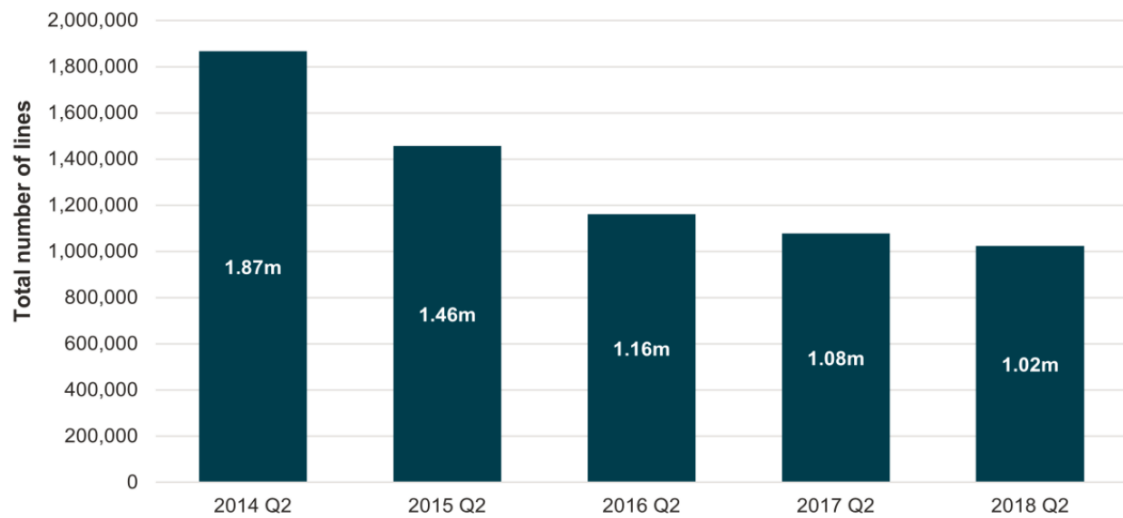
163. The overall position is best shown by the figure below, from HJ1:

**Figure 3.4 Number of BT lines sold to SFV customers and number of BT fixed voice services sold in a bundle**

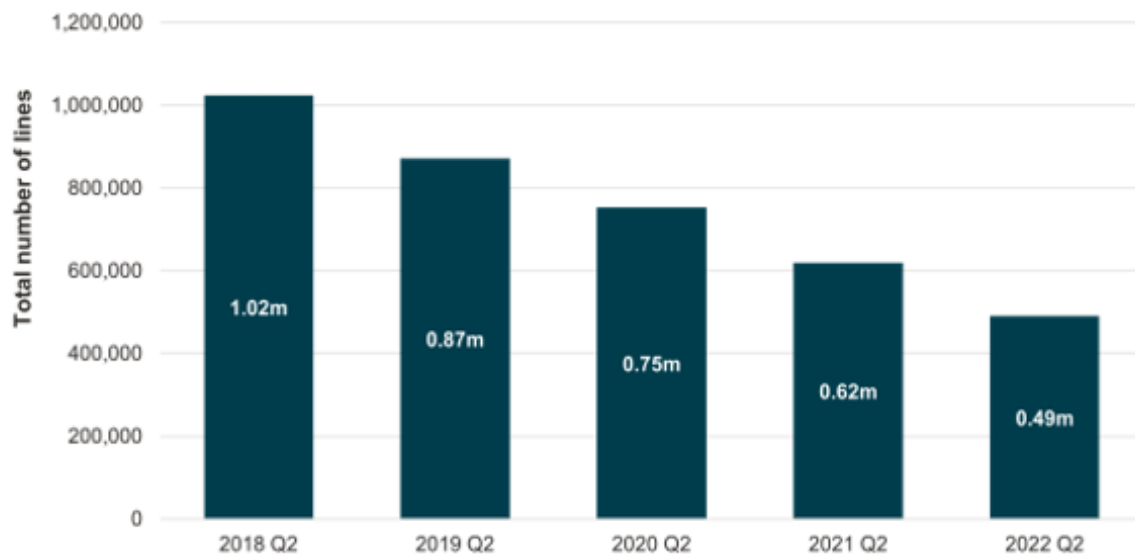


164. One can see from this graph that SFV Customer numbers reached a peak (over the period shown) in 2010 of around 7.6m, followed by a steady decline down to about 1m in 2022. This decline was accompanied by a significant increase in the number of fixed voice lines within bundles from 2009 to around 2014, after which point the number of BT bundle customers stabilised and then declined in the last 2 years of the claim period.
165. If one looks simply at the decreasing SPC numbers, this is shown in the following tables from DP3:

**Figure 9**      **Estimated number of BT Split Purchase Customers, 2014 Q2 - 2018 Q2**

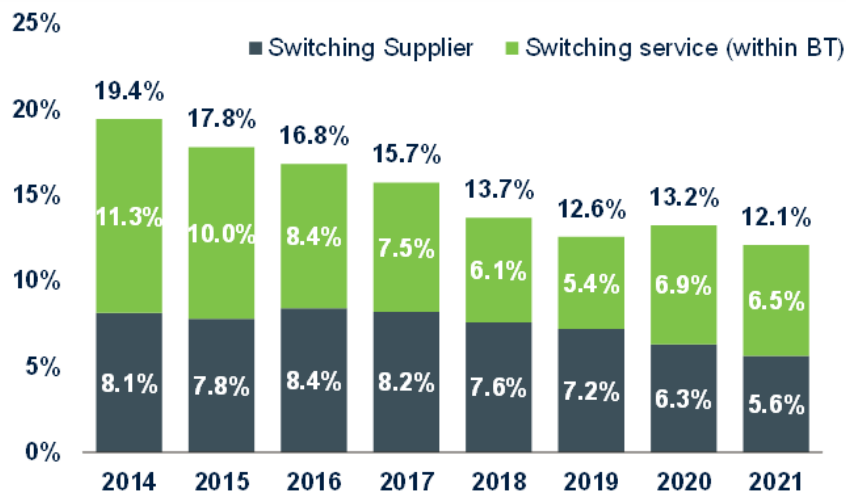


**Figure 12**      **Estimated number of BT Split Purchase Customers, 2018 Q2 - 2022 Q2**



166. For VOC figures, there was a reduction from 2.1m in 2014 Q2 to 0.5m in 2022 Q2 - a fall of almost 75%. See paragraph 3.39 of HJ2, based on the same data pack as Mr Parker used for his SPC decline figures.
167. The figure below shows, for each year, the percentage of that years' SFV customers which switched and, within that percentage, how many switched supplier, i.e. away from BT, and how many switched service within BT. So on any view, there was a significant amount of switching each year. This figure derives from paragraph 201 of SH1.

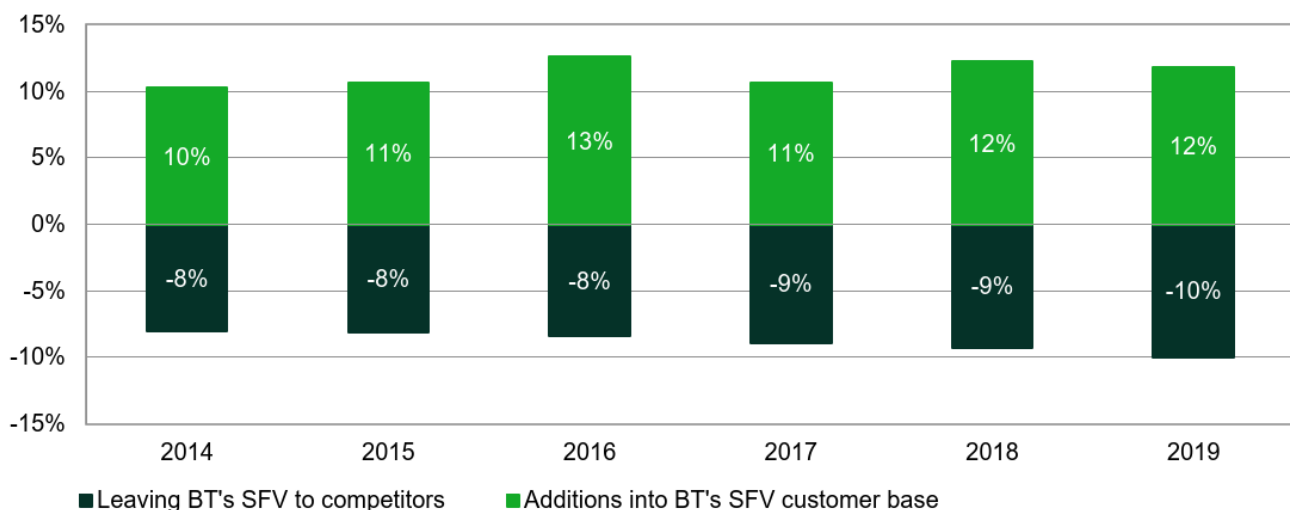
**Figure 10: Total rates of BT SFV customer switching (supplier & service)**



168. As for the breakdown of switching SFV customers between VOCs and SPCs, Dr Hunt said that the switching rate was higher for SPCs than for VOCs, on the basis of his own analysis of the raw data (see paragraph 200 of SH1), and significantly higher on the basis of his restated Ofcom Switching Tracker figures (see paragraph 207 of SH1).

169. In this regard, it needs to be recalled that in each year, there were also SFV customers who joined from elsewhere (“the joiners”). See the green elements of the diagram below, shown under paragraph 5.83 of HJ1 (the black sections of each column may be ignored for present purposes):

**Figure 5.19 BT’s SFV customer additions and losses to BT’s competitors, 2014–2019**



170. These percentages were extrapolated by Dr Jenkins from the underlying figures which are shown in Tables 11 and 12 of the Agreed Matters Document:

**Table 11 Additions to BT's SFV customer base (2014-2022)**

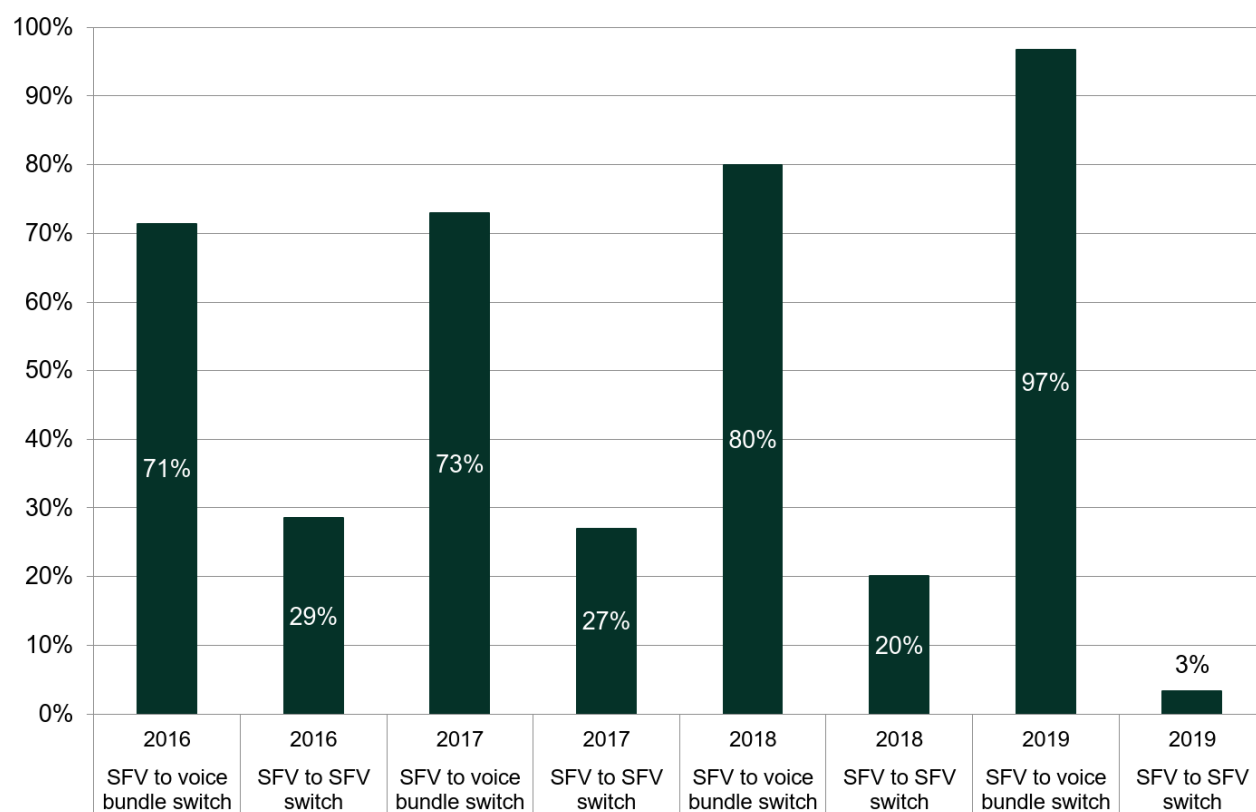
	2014	2015	2016	2017	Jan-Mar 2018	Apr-Dec 2018	2019	2020	2021	Jan-Oct 2022
<b>Total additions into SFV</b>	435,980	381,189	331,927	263,633	52,286	179,514	195,581	198,437	170,879	78,511

**Table 12 Additions to BT's SFV customer base split by VOCs and SPCs (2018-2022)**

	Apr-Dec 2018	2019	2020	2021	Jan-Oct 2022
<b>Additions to VOCs</b>	24,742	29,934	40,852	59,541	28,951
<b>Additions to SPCs</b>	154,772	165,647	157,585	131,338	49,560
<b>Total additions into SFV</b>	179,514	195,581	198,437	170,879	78,511

171. Mr Parker has questioned whether those figures are correct, based on the number of customers who said, in 2022, that they had been customers as at 2014 (see paragraph 175 below). There may in fact be no discrepancy if at least some of the new joiners departed relatively quickly after they had joined. But in any event, the real point is that, while there were some new joiners, this had minimal impact on the overall rate of decline as shown in Figure 3.4 under paragraph 163 above.
172. As to where the SFV customers went overall (whether BT or not, but most were BT), Figure 4.4 under paragraph 4.53 of HJ1 shows that an increasing majority went to bundles as opposed to competing providers' voice-only services:

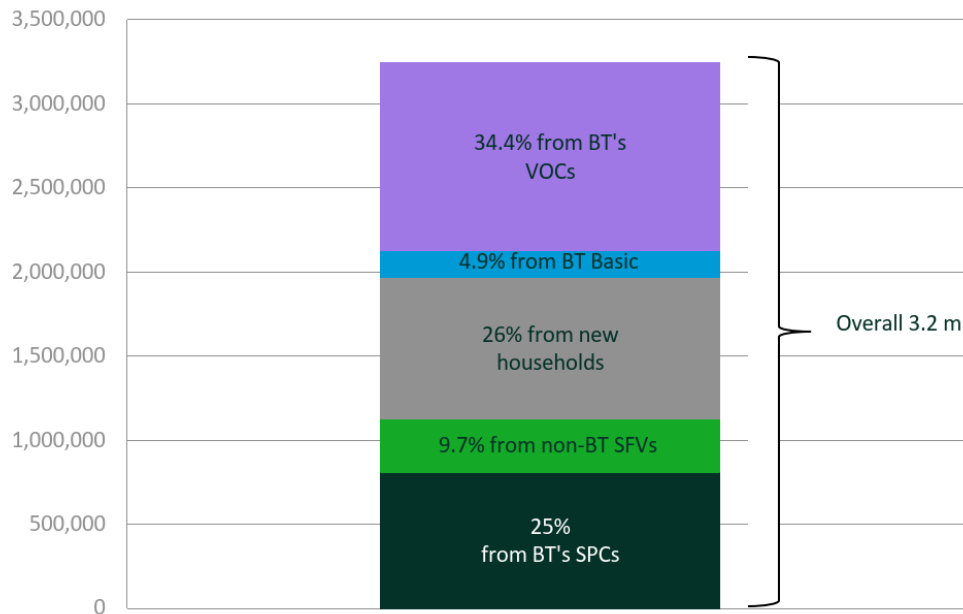
**Figure 4.4 Products chosen by recent SFV switchers, 2016-2019, all operators**



Source: Ofcom Switching tracker data tables, 2016 Tracker Table 34, 2017 Tracker Table 41 {C/351/95-96};

173. If one takes the total increase in BT's bundled fixed lines from 2014 to 2018, the figure below shows the source of the increased number of lines, as set out at paragraph 3.48 of HJ2:

**Figure 3.2 Assumed sources of the increase in bundled fixed lines, Q2 2014 to Q2 2018**



174. This shows that 59.4% of the increase came from BT SFV customers (excluding BT Basic customers who are not part of the Class).
175. Further, it follows from the figures used by Dr Jenkins (as to which there was no real dispute, since they came from BT itself), of the 1,113,285 SFV customers in October 2022 (a total derived from the F19 Summary, BT00092355), 881,370 had been SFV customers in January 2014. But this latter figure itself corresponded to only 18.8% of the total of 4,681,019 SFV customers in January 2014.
176. The figures referred to above are either agreed, or any dispute over them does not matter for present purposes.
177. We should add that these switching rates are much higher than those quoted by Ofcom and used in its 2017 Provisional Conclusions. The explanation for this discrepancy is common ground. It is that Ofcom's analysis only captured consumers who switched landline provider away from BT and remained a stand-alone fixed voice customer. It therefore did not include BT customers who switched to a bundle, nor did it include those who stayed with BT for the landline, but then changed or added broadband from another provider. See paragraphs 512 - 522 of SH1.

## **FACTUAL MATTERS (4): BT'S PERCEPTIONS AS TO LINE RENTAL INCREASES AND SWITCHING**

### **Introduction**

178. This is an important topic because it is relevant to certain aspects of market definition as well as Limb 2. The relevant material is constituted by the evidence of BT's witnesses and its own contemporaneous documents.
179. To recapitulate on BT's line rental increases,
- (1) Between 1 October 2010 and 3 July 2016, there were price increases at least once in every year;
  - (2) Between 1 December 2014 and 3 July 2016 there were 3 consecutive price rises of £1 each, culminating in an SLR of £18.99;
  - (3) Due to a general price freeze introduced in 2017, that £18.99 price remained in place until 1 April 2018. At that point, it dropped by £7 for VOCs but remained for SPCs, until 16 September 2018 when it rose by £1 to £19.99;
  - (4) Thereafter, for SPCs, price increases followed, not by a set amount (for example £1) but rather by a percentage related to CPI;
  - (5) Thus, the £19.99 price was changed on 31 March 2020 by a modest 21p which equated with CPI;
  - (6) For the following years, the increase was CPI +3.9% which made for much larger increases.
180. We have set out the position in relation to BT's competitors, so far as line rental prices were concerned, in paragraphs 131 - 132 above. The issue of their pricing, as opposed to that of BT, arises in the context of price leadership within the topic of Dominance, considered below.

### **The Immediate Purpose of BT's line rental increases**

181. It is clear from the evidence of all of BT's witnesses that the immediate causes of the numerous line rental increases were the revenue targets which the Voice division had to meet.
182. As Mr Cackett explained, each year, BT Consumer produced a 5-year Medium Term Plan ("MTP"). Internal references to the "budget" were normally to the detailed first year budget within the MTP. The MTP was, in effect, BT Consumer's proposed contribution to the final targets set by BT Group for its various constituents, including BT Consumer. Those targets were set each year and BT Consumer would have to consider whether its own MTP was likely to meet the targets or not. If it appeared that the MTP would not meet the targets set by BT Group, the latter target might be adjusted, so as to reflect the likely performance of the MTP; alternatively, the MTP might be adjusted to conform more closely to the target, for example, by cutting some costs.

183. The budget figures would deal with costs and revenue. As for revenue targets for BT Consumer, these were in turn split up into revenue targets for each division, including Voice. They were then dealt with by that division's General Managers. In relation to Voice, this involved meetings with Ms Blight, who was Voice's General Manager from November 2015 until late 2016 and also Mr Bunt, who became Acting General Manager upon Ms Blight's departure on leave, and then General Manager from 1 April 2017, once Ms Blight had moved to a different role. He remained in that post until April 2019, when he was promoted to Director of Portfolio and Pricing within BT Consumer. He became BT Consumer's Regulatory Affairs Director in December 2019, and then the Retail Regulatory Affairs director for both BT Consumer and the business and public sector provision of BT Group, called BT Enterprise.
184. Mr Bunt had originally been appointed Senior Propositions Manager of the Voice Propositions Team in November 2013, becoming Head of Pricing within Voices Propositions Team in April 2015. At that point, BT Consumer was made up of four divisions, namely Voice, Broadband, TV and Sport, with a fifth division, namely Mobile, being added from around October 2015.
185. In general, and it follows from what is said above, price changes in line rental made or to be made by Voice were considered in the context of the annual revenue (and costs) targets which Voice had to meet. The increases were not driven, for example, by increases in costs, not least because the primary direct cost was WLR which was either flat or decreasing somewhat.
186. Both Mr Bunt and Ms Blight accepted that in practice, and especially when line rental was increasing by £1 a year, that this was driven by the need to meet Voice's revenue targets. It was also understood that the profits from Voice could contribute within BT Group to investments in fibre-optic cable, 5G, and other expenditure not related directly to Voice. There was clearly a belief that increasing line rental prices would increase BT's total voice revenues, compared to the levels that would arise absent the price rise; in other words, that any reduction in consumer demand arising from these line rental price increases would not outweigh the increase in line rental per customer.
187. To take an example of how price changes were designed to achieve particular revenue targets, one can take the projected price increases for 2015-2016, known as Project Laika. The key support slide for 2015-2016 is dated 4 September 2014. The extract below shows how the revenue target is to be delivered:



**1516 Pricing Plan – 1 of 2**  
**A base plan to deliver £41.4m against the £39m target**

### Context

- 14/15: £38.5m from general voice pricing (£40m upside less £1.5m in gives)
- The £10m incremental challenge for 14/15 was delivered through a range of profit protection activities through these opportunities can not be replicated, unlike the basic annual price change

### Base Price Change

- MTP pricing target for 15/16 is £39m
- Pricing below covers Voice only at this point – BB & Bundles are providing input by 5<sup>th</sup> Sept

Item	Pricing	Benefit 15/16 (£'m)
Line Rental	£1 increase (5.9%)	24.3
Packages	6.4% increase (i.e. 6.5% once prices rounded)	6.0
Calls and Calling Features	6.4% increase (i.e. 6.5% once prices rounded)	7.4
Gives		-2.0
<b>Total</b>		<b>35.7</b>

### Further Pricing Activity – Recommended Plan delivers £5.7m

Item	Timing	Price Change	GM 15/16 (£'m)
LRS Price Increase (to align with increased standard rental)	Price Change	6.50%	3.3
Re-FEWE-ing	Various	£3.50	0.5
Type - J (and Paper Bills charging)	CCP42	£2	0.4
LR+ paying for paper bills	CCP41	£1.59	0.7
Move Price Change to Sunday 29th November	29th Nov 15	Various	0.8
<b>Total</b>			<b>5.7</b>

188. The extent to which a £1 price increase was seen by those in the Voice division as a default is expressed in Mr Bunt's 15/16 Price Plan document dated 12 December 2014 ("15/16 Pricing"). This contains a number of recommendations by Mr Bunt. At page 6, he observed thus:

### 15/16 Pricing – LT Strategy

#### Sustainability of Current Pricing Approach:

- Pegasus to 15/16 pricing has seen 2 key changes in approach:
  1. 1 month creep in price change date
  2. £1 increase in LR on each occasion
- The sustainability of this creep is in question especially as in future years this moves the price change close to the start of the Football season – which is a strategically important period.

#### Long Term reduction in our dependence on price changes

- Price changes create significant headroom for our competitors to do likewise
- A culture of annual price change can become a drug on which we get hooked, losing perspective of the elasticity of our pricing an volume impact
- Our 3-5 year view is to reduce the budgeted price change down year-on-year to improve the competitiveness of our offering and enable us to put the squeeze on our competitors *15/16 £41.4m, 16/17 £35m, 17/18 £30m*

189. In her evidence, Ms Blight said that she agreed 100% with the “drug” analogy and added this (Day8/135):
- “...and that is what I sort of was alluding to when I talked about short term. Because of course when you put the price up, you immediately get the sugar high of extra revenue, but then it is very hard to analyse the churn impact and disaggregate what is the churn from the price change versus the churn from Sky’s marketing or something the Post Office does.”
190. In fact, the thrust of her evidence was that the Voice team would have to be creative in terms of providing extra value, given that the line rental price increases were almost inevitable, which is where the question of Gives is relevant (see below).
191. In evidence, Mr Bunt accepted that line rental increases were pretty much a “given” and that Voice was really fixed with the revenue targets. He said that, when he suggested not to increase prices at a particular point, he would be overruled by “the grown-ups” i.e. senior BT management. He added that there was, not only within Voice, but also within the senior members of the Consumer Leadership Team, to whom the Voice team would present its proposals, “collective handwringing” at the absence of a better plan than line rental increases to meet the MTP targets.
192. For his part, Mr Cackett did not think that an annual price increase of £1 was a “given”, but on the other hand, the starting point would be what was done in the previous year. He also accepted that there was a tension between those in Voice, who questioned whether prices needed to be increased and those on Mr Cackett’s side, who said that the price increase should not be interfered with. He said that nonetheless, there was considerable discussion before deciding the outcome for any particular year; it might look like a *fait accompli* because of what was done each year, but it was probably significantly more nuanced than that. We do not think that there is really much between the evidence of Mr Bunt and Ms Blight on the one hand and that of Mr Cackett on the other in relation to this matter.
193. The £1 price increase contemplated by Project Laika was indeed implemented, in September 2015.
194. It is, of course, also important to bear in mind that, as we have noted above, the successive increases in line rental prices did not secure any real year-on-year increases in BT’s ARPU from SFV customers. It was clearly BT’s belief that the line rental price increases helped to increase voice revenues compared to the counterfactual in which line rental prices were maintained, but other factors, notably the decreasing call volumes, prevented any material increases in ARPU despite the line rental price rises.
195. All of this is important background for, among other things the question of BT’s perception of the risk of churn in the context of price increases.

## **MARKET DEFINITION**

### **Introduction**

196. As already noted, the CR contends that the relevant market is SFV Services prior to the Commitments, and SPCs afterwards, and that BT is dominant in both markets. BT contends that the relevant market is wider, being a product market which encompasses SFV Services and bundles. If BT is right, that is the end of the claim because the CR does not contend that BT is dominant within that wider market. If the CR is right, BT does not concede that it is dominant in SFV Services, and so we would then proceed to determine that issue.
197. Each side relies on a number of different factors to support its position which are discussed below.
198. At this point, we should just record what is agreed between the parties about other aspects of the markets, as set out in the JES:
- (1) Prior to the Commitments, VOCs and SPCs formed part of the same market, given BT's inability to price discriminate between the two customer groups at that stage;
  - (2) Both pre-and post-Commitments:
    - (a) SFV access (i.e. line rental) and SFV calls form part of the same market;
    - (b) the relevant markets exclude BT Basic / Home Essentials;
    - (c) the relevant markets exclude SFV services aimed at business customers;
    - (d) the relevant markets exclude mobile voice services; and
    - (e) the relevant geographic market is UK-wide (excluding the Hull area);
  - (3) Further, Mr Parker maintained that after the Commitments, when BT was able to price discriminate between SPCs and VOCs, SFV Services sold to VOCs who received the Commitments discount were in a different market from SFV Services sold to SPCs (and VOCs not eligible for the discount); for her part, Dr Jenkins agreed that this was likely. See her comments at paragraph 5.1.9 of the JES.

### **The Basic Approach**

199. We did not understand the parties to disagree about the purpose of market definition in the present context. As it is put in paragraph 2.1 of the CMA Market Definition Guidelines:
- “Market definition is not an end in itself but a key step in identifying the competitive constraints acting on a supplier of a given product or service. Market definition provides a framework for competition analysis. For example, market shares can be calculated only after the market has been defined and, when considering the potential for new entry, it is necessary to identify the market that might be entered. Market definition is usually the first step in the assessment of market power.”
200. See also, to similar effect, paragraphs 6, 9(a) and 10 of the Commission Notice C/2024/1645 on “the definition of the relevant market for the purposes of Union competition law” (“the Commission MD Notice”).

201. When assessing the focal product, i.e. the product that is being considered as a candidate for a relevant product market, the fact that other products might to some extent be considered as alternatives due to being substitutable and/or functionally similar is relevant but not in itself conclusive. That is because:

“The key idea is that of a competitive constraint: do the other products alleged to form part of the same market act as a competitive constraint on the conduct of the allegedly dominant firm?”

See *Aberdeen Journals v Director General of Fair Trading (No. 1)* [2002] CAT 4 (“*Aberdeen Journals I*”) at para. 97 and *Generics (UK) Ltd v CMA* [2018] CAT 4 at para. 401.

202. Here, therefore, the focal product is SFV Services (or such services to SPCs after the Commitments) and the main other products that are considered to provide a possible competitive constraint on the focal product are bundles.

### **The SSNIP Test**

203. Both sides also agree that one common approach to ascertaining the correct market by reference to the competitive constraint exerted (or not) by the other product is to use the SSNIP Test framework. This involves identifying the smallest group of products in which a hypothetical monopolist (“HM”), which controls the focal product, could profitably sustain at least a “small but significant non-transitory increase in price” (i.e. “SSNIP”) above the competitive level. The size of such an increase is typically taken to be 5-10%. If the HM can “pass” that test, i.e. it is commercially better off after the increase, this indicates that the focal product is its own market i.e. the market is narrow. If, on the other hand, the test is “failed” so that the price increase cannot be profitably maintained (because of the extent to which the HM loses customers to other products as a result of the SSNIP), this indicates that the market is wider. Therefore, the key question is whether the ability of consumers to switch from a voice-only contract (SFV or later, SPC) to a voice plus broadband bundle would provide an effective competitive constraint on a hypothetical monopoly supplier of SFV Services (or later, such services to SPCs).

204. As to how the SSNIP test might be carried out, paragraph 3.7 of the CMA Market Definition Guidelines includes the following factors as likely to be important:

- Evidence from the undertakings active in the market and their commercial strategies may be useful. For example, company documents may indicate which products the undertakings under investigation believe to be the closest substitute to their own products...

- Customers and competitors will often be interviewed. In particular, customers can sometimes be asked directly how they would react to a hypothetical price rise, although because of the hypothetical nature of the question, answers may need to be treated with a degree of caution...

- Evidence on product characteristics may provide useful information where customer substitution patterns are likely to be influenced significantly by those characteristics. Where the objective characteristics of products are very similar and their intended uses the same this would be good evidence that the products are close substitutes. However, the following caveats should be noted. First, even where products apparently have very similar characteristics and intended use, switching costs and brand loyalty may affect how substitutable they are in practice. Second, just because products display similar physical characteristics, this does not necessarily mean that customers would view them to be close substitutes. For example, peak customers may not view rail

travel during off peak times to be a close substitute for rail travel at peak times. Third, products with very different physical characteristics may be close substitutes if, from a customer's point of view, they have a very similar use.

- Patterns in price changes can be informative. For example, two products showing the same pattern of price changes, for reasons not connected to costs or general price inflation, would be consistent with (although not proof of) these two products being close substitutes. Customer reactions to price changes in the past may also be relevant...

- Evidence on own or cross price elasticities of demand may also be examined if it is available...

- In some cases **critical loss** analysis may be relevant. One definition of critical loss is the minimum percentage loss in volume of sales required to make a 5 (or 10) per cent price increase on a product unprofitable. The critical percentage tends to be lower when an undertaking has a high mark up over unit costs (since each sale lost entails a relatively large loss in profit). However, the fact that an undertaking can set a high mark up might also demonstrate that its current customer base is not particularly price sensitive..."

205. The following also emerges from the Commission MD Notice:

"56...Undertakings typically monitor competition in the ordinary course of business. There may also be industry associations or experts monitoring competition. While such industry views on market boundaries do not necessarily correspond to the concept of the relevant market within the meaning of Union competition law, information on which undertakings regard each other as (close) competitors, as well as the views of other market participants and industry experts on competitive constraints, can provide useful information for assessing demand substitution..."

77. Evidence used by the Commission to define markets should be reliable. This is likely to be the case, for instance, when the evidence comes from public authorities or is supported by multiple sources, including by market participants with conflicting interests, such as suppliers and their direct customers...

81...In cases involving regulated markets, including, for instance, the telecommunications, energy or healthcare sectors, the Commission may also seek data from and the views of sector-specific regulators..."

206. The Tribunal in *Aberdeen Journals I* stated as follows in this context:

"103. In general, evidence as to how the undertakings in question themselves see the market is likely to be particularly significant. As the Director points out at paragraph 2.6 of OFT 403:

"The idea of a market is familiar. Annual reports, business plans and other documents often refer to the market in which the undertaking operates. This will normally include other undertakings which the undertaking views as its competitors."

104. In the Tribunal's view, contemporary evidence as to how the allegedly dominant undertaking itself views its competitors, and vice versa, may, depending on the particular circumstances, be of decisive importance when it comes to defining the market in any given case."

### The Cellophane Fallacy

207. In an abuse of dominance case concerned with excessive pricing, the allegation is that the firm in question is already charging a price significantly above competitive levels, as a result of the exercise of its market power. This poses a problem for the SSNIP test. That is because, while a modest price increase from the prevailing price of the HM may fail the SSNIP test, it does not follow that the SSNIP test would fail where the price increase was implemented from a lower (competitive) starting point. This is the well-known Cellophane Fallacy, recognised, for example in paragraph 5.5 of the CMA Market Definition Guidelines and paragraph 30 of the Commission MD Notice. Indeed, in its Decision of 15 October 2014 in Case AT.39523 *Slovak Telecom* at para. 158 (cited more fully at paragraph 427 below), the Commission said that because of the Cellophane Fallacy, it "does not normally rely on the SSNIP-test exercise in the context of cases which are based on Article 102 of the Treaty."

208. Both experts accept the existence of the Cellophane Fallacy. However, it is problematic only in one direction i.e. where the SSNIP test is failed, indicating a broader market. If the SSNIP is passed, even at an increase from the prevailing price, such that the narrow market is (still) entailed, it has no adverse effect on what can be concluded from the test.
209. Dr Jenkins in the book *Economics for the Competition Lawyer* (3<sup>rd</sup> Edition), written by her and others (“JNK”) put it thus at paragraph 3.79:

“At the very least a one-way test can be applied. If, at the prevailing price level, a monopolist can profitably impose a SSNIP, you can be confident that the market is no wider. If, in contrast, you find that the monopolist cannot profitably increase price, there may be a cellophane fallacy and the market may be defined too broadly. Ultimately, if there is a high probability that the analysis will suffer from a cellophane fallacy, you may have to conclude that market definition is not a useful intermediate step and instead focus directly on indicators of market power, such as profitability”.

### **Price Discrimination**

210. If the HM has two separate customer groups and it can price discriminate between them by charging one group a price which is higher than that charged to the other by a SSNIP or more, and doing so profitably, and where the difference is unrelated to cost, this suggests that each group forms a separate market. Paragraph 88 of the Commission MD Notice puts it thus when explaining that separate markets can be inferred from price discrimination typically:

“when three cumulative conditions are met: (a) it is possible to identify clearly to which group an individual customer belongs at the moment of selling the relevant product to the customer; (b) trade between customers or arbitrage by third parties is unlikely; (c) the discrimination between customers or customer groups is of a non-transitory nature”.

### **The Relevance of Switching**

211. On any view, the phenomenon of extensive amounts of switching, as shown in paragraphs 163 - 176 above, is significant. The question is whether or not it reveals evidence on the kind of substitution from SFV to bundles, that would show a competitive constraint on a hypothetical SFV monopolist.
212. As Mr Parker put it in the JES at paragraph 5.1.1:
- “Evidence on switching is one type of evidence that is relevant to market definition. The key issue is whether there is sufficient switching to have acted as a competitive constraint on the hypothetical monopolist. (Parker 3, paras. 4.16(a) and 4.17) For switching to act as a constraint, switching needs to take place as a result of changes in relative prices, rather than other non-price factors, such as changes in tastes.”
213. The CR says that switching occurred mainly as a result of what Mr Parker refers to as the “secular trend”. In other words, it reflects an increase in customer preference for bundles rather than SFV Services (only a small minority of VOCs migrated to other voice-only providers which, in any event, were decreasing in numbers). It was not, in the main, a reaction to any price increases on the part of BT, although Mr Parker does not suggest there could be no such reaction. That being so, he reasons that the phenomenon of switching cannot assist BT in relation to market definition, and in particular on the issue as to whether bundles act as a competitive restraint on SFV pricing and the operation of the SSNIP test.

214. On the other hand, BT contends that switching is indeed, to a significant, albeit not exclusive degree, a reaction to price increases by BT. On that basis, not only is it relevant to the market definition issue, but it positively suggests that bundles do act as a competitive restraint on SFV pricing in a way which means the SSNIP test fails.
215. Since the reason, or main reason, for switching is such an important foundational question, we deal with it at this point, before turning to the analyses on market definition offered by Mr Parker, on the one hand, and Dr Jenkins on the other. Both Mr Parker and Dr Jenkins have also given evidence on the issue of switching, which we refer to in context below.

## **Reasons for switching**

### *The Possibility of Secular Trend*

216. The possibility of secular trend, based on changes in customer preference, as opposed to any increased price of the focal product was recognised by Dr Jenkins and her co-authors in JNK, at paragraphs 3-187 – 3.189:

“3.187 The other question is whether-and at what point-the new product imposes a pricing constraint on the old product. An example is the analysis of the leased-lines market by OPTA, the Dutch telecoms regulator, in 2005. A leased line is a permanently connected communications link between two premises, dedicated to a customer's exclusive use. At the time, business users had begun to switch from leased lines to other data services, such as those based on internet protocol technology. While these newer data services had more variable capacity and required more outsourcing of network management functions, customers considered them a lower-cost alternative to leased lines. Having noted a high degree of migration from leased lines to the newer data services between 2002 and 2004, OPTA nonetheless concluded that the movement between the products was not relevant for market definition:

Switching and migration from service A to B does not automatically constitute demand substitution. Demand substitution requires that switching from A to B is caused by changes in the price difference between A and B. In this case, there is price pressure. Migration, however, can result from other factors, such as the emergence of a completely new service (B) or changes in user preferences. Consumers migrate as a result, where this migration no longer depends on further small (5 per cent to 10 per cent) changes in the price difference between A and B.

3.188. Is this an overly restrictive interpretation of the hypothetical monopolist test? What ultimately matters is whether the old product is a product worth monopolizing. Here, product migration does have relevance... There comes a point when demand for the old product has fallen so far that it is no longer a product worth monopolizing and therefore does not constitute a separate market. From this perspective, product migration over time is just as relevant to market definition as switching between products in response to price changes.

3.189 Yet some caution is still required in these cases. The migration process may not be uniform across all groups of consumers in the market. After the early adopters of the new product and then mass migration by others, there may be situations where the consumers who remain with the old product are those with the highest willingness to pay or the lowest ability to switch. Because of these remaining consumers the old products may still be a market worth monopolizing...”

217. The same point is made at paragraph 52 of the Commission MD Notice:

“In some cases, undertakings may also collect relevant information on demand substitutes during the ordinary course of business. For example, an undertaking may have data on the customers that it has won and lost and the identity of the competitors which lost/won those customers. By contrast, evidence of customers shifting away from a product as a result of factors unrelated to changes in relative supply conditions, such as a change in preferences or consumption patterns over time, are less informative for demand substitution.”

218. More specifically, Mr Matthew observes in DM1:

“157. One potentially significant feature of telecoms markets is that new or upgraded products are introduced in waves. As these new and upgraded products become available, a process of customer upgrading usually follows over a period that often takes several years. Initially the new products may be used by early adopters followed by the main part of the customer base, with a residual group of customers that do not value the better products available and continue to use the legacy products, in some cases continuing to do so until the old products are actually withdrawn. This process of customer migration can be observed in the take up of broadband by voice customers (facilitated by local loop unbundling regulation) which resulted in the rapid growth of bundles as the predominant way of purchasing fixed telecoms products, the upgrades of “standard” broadband to “superfast” broadband (facilitated by virtual unbundled local access regulation), and the current migration to full fibre broadband.”

219. Dr Jenkins does not deny this as a possibility; indeed, her approach is to give some weight to it, but she nevertheless concludes that there is sufficient price-based switching from SFV to bundles to meet the requirements of the SSNIP test.

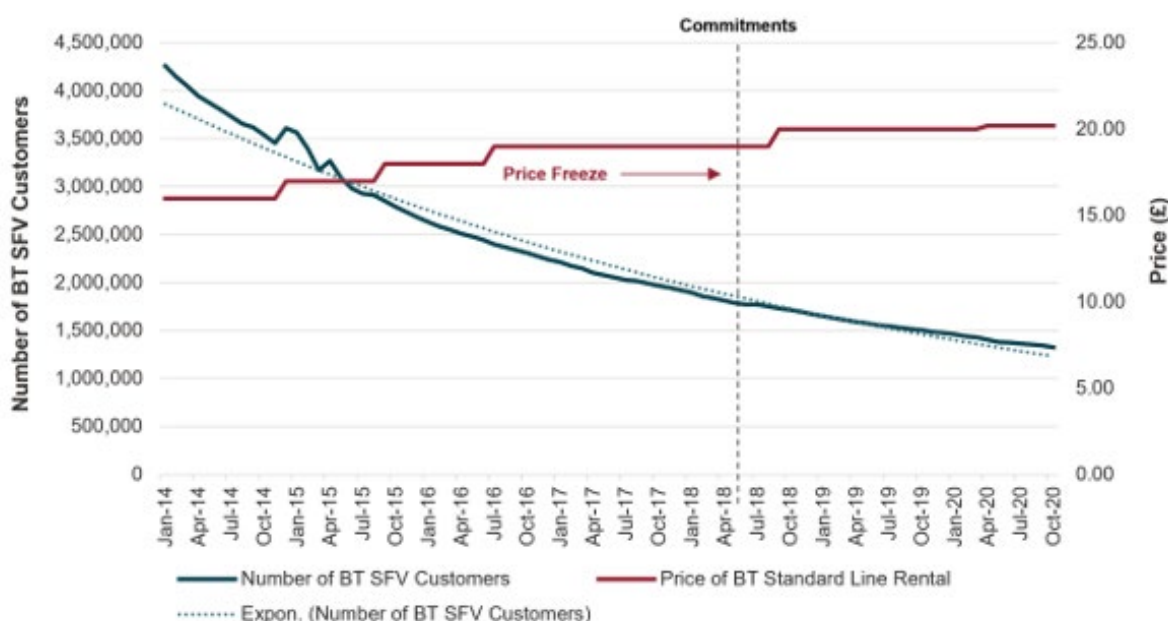
*Gradual and consistent decline in SFV Customers*

220. Mr Parker addresses the issue of secular trend directly at paragraphs 3.61 to 3.63 of DP4. He says that, broadly, there can be seen a gradual and consistent decline in SFV Services customers across the claim period, even where there was either a freeze on line rental price or where the Commitments price had been introduced for VOCs. Further, and in any event, the decline in SFV customers did not seem to turn on a particular line rental price increase at a particular time; in other words, there were no “spikes” in customer loss which one might have expected following a price rise. He says that a fairly swift reaction to price increase in terms of switching might be expected here, since customers who wished to terminate their contracts because of a price increase could do so without penalty, provided they acted within 30 days from the date of being notified of the increase (of which BT had to give at least 30 days’ notice), as mandated by Ofcom’s General Condition 9.6.

221. Figure 3 in DP4 shows the rate of decline of BT’s SFV customers, and the various changes to BT’s standard line rental over the claim period.



**Figure 3 Change in the number of BT SFV Customers over the period covered by Dr Jenkins's CLA, January 2014 – October 2020**



222. The particular point that the decline continued in SFV customer numbers even during the price freeze is brought out in the further table prepared by Mr Parker as Table 1 in MdR's letter of 15 February 2024:

**Price Freeze**

Start	Jul-14	Jul-15	Jul-16	Jul-17	Jul-18	Jul-19	Jul-20	Jul-21
End	Apr-15	Apr-16	Apr-17	Apr-18	Apr-19	Apr-20	Apr-21	Apr-22
Start BT SFV Customers	3,727,915	2,928,056	2,396,517	2,026,677	1,772,172	1,546,625	1,365,492	1,170,340
End BT SFV Customers	3,265,641	2,509,833	2,104,063	1,812,957	1,592,047	1,402,177	1,216,152	1,040,610
Diff.	462,274	418,223	292,454	213,720	180,125	144,448	149,340	129,730
% change	-12%	-14%	-12%	-11%	-10%	-9%	-11%	-11%

**Source** Oxera datapack - BT customers switching analysis, Sheet('Customer journey)

**Notes** The Price Freeze refers to the period Jul-17 to Apr-18 during which BT froze line rental price increases.

223. Professor Loomes agreed. In the hot tub discussion on Day 19/70-71 he said that:
- "I am perfectly happy to agree that there has been, over the years, a substantial migration away from SFV products and towards bundled products, that is certainly true. I think it is highly likely to be for historical, technological, social reasons, qualitative features. The improvement in what having broadband offers to people, they see it is more important, they see its benefits. They are also pushed to some extent by the difficulties of operating in a world which is increasingly referring people to go online, rather than dealing with them face-to-face or on the telephone.... But it is a continuum, and therefore we should not be surprised to see that as circumstances, the so-called secular trend, as circumstances make it more and more advantageous to be in a bundle, to have broadband at least, and more and more difficult not to have it, you are going to see this gradual migration."
224. He was then cross-examined about this statement on Day 20 and whether it applied only to VOCs or to SPCs as well. He said he thought that SPCs might also move in the direction towards bundles (impliedly for the same reason as VOCs), but he accepted that this would not be so if the move was

simply to get broadband, as opposed to, for example, obtaining TV as well, or to get a better version of broadband.

225. Mr Parker put this switching down largely (though not exclusively) to the fact that an increasing number of UK consumers had been persuaded of the benefits of having home broadband access over time, and that most of the switching was due to decisions associated with the natural process of migration towards home broadband. He thought that price factors played only a minor role and that therefore, in the context of applying the SSNIP test framework, it would not be safe to equate the amount of switching overall with the additional losses that a SFV HM would suffer were it to impose a price rise that was 5-10% above the competitive level. If he is right in that proposition, then there would be less reason to conclude that an HM would refrain from imposing a unilateral price increase because of the specific switching consequences of doing so.
226. Importantly, this is not to say that the HM would be immune from or unharmed by the general market-wide trend towards bundles and away from SFV contracts. Any such supplier would fear (and suffer commercially from) the adverse commercial consequences of this change. Instead, the CR's case as advanced by Mr Parker was that the *extra* commercial damage caused by any *additional* switching that was specifically related to a decision to impose a SSNIP above the competitive level would not, in itself, be a factor that would make the ongoing switching away from SFV very much worse than it would be absent that price rise.
227. It is obviously true that the basis of any secular trend towards bundles must be somewhat different for SPCs, since they already have broadband. In the period prior to 2018, we are unable to identify VOCs and SPCs separately, so it is not possible to identify the extent to which the trend towards bundles applied differently for the two groups. However, SPCs still form part of a gradual but consistent decline in the SFV Services customer base and this occurs whether there was a particular price rise or not. Moreover, for the period from 2018 onwards, there is clear evidence that a substantial number of SPCs cancelled their voice-only contracts in favour of a bundle contract, and Mr Parker's contention was that their propensity to do so was not much affected by marginal changes in SFV prices. Indeed, his interpretation of the existence of SPCs paying a large price premium for buying two standalone products instead of a single DP bundle was that any supplier currently choosing to charge the inflated standalone voice price (which in practice was BT in over 90% of cases) clearly had not been dissuaded from charging such a premium across the entire claim period.
228. We think it is perfectly plausible to suggest a secular trend towards bundles from SPCs as these customers realise that bundles provide a more convenient way to receive voice and broadband

services, and that this shift arises as a matter of customer preference, which is not essentially related to price changes made by BT at any given point.

*Price Increase in face of declining SFV customer base*

229. BT has submitted that the CR has not adduced any specific evidence to show the existence of the secular trend, for example, survey evidence. That is a fair point and we take it into account. On the other hand the CR can say that switching cannot have been primarily price-related because if it was, and BT perceived that it was, BT would not have continued to increase line rental prices as it did. Here, we focus on line rental because price changes in relation to call charges are more complex and less obvious; see also the issue of ARPMs discussed below.
230. As to that point, made by Mr Parker in the hot tub discussion (Day 9/128-130), there are really only two answers. The first is that BT did not care about any effect on its price increase, precisely because it believed that switching was going to occur anyway; that answer would support the CR's case on secular trend. The other answer is to say that it was rational to keep increasing prices, despite the fact that they would inevitably lead to significant switching, because of BT's migration intent or the recapture effect, which meant that BT (in contrast to the hypothetical stand-alone SFV monopolist) positively benefited from consumers who switched to bundles. We deal with both of these points below. We should say here, however, that we reject the suggestion that BT's pricing was motivated by a migration intent because of the absence of any real evidence to support its existence. As for the recapture effect, we accept that this can be a factor which would make it less "painful" for BT to increase prices, than might be the case for a single product operator. However, we do not find the evidence on this phenomenon sufficiently strong to discredit Mr Parker's evidence on market definition and as we note below it does create some problems for BT's arguments on the relevant product market, because recapture incentives accentuate the Cellophane Fallacy problem and will tend to elevate BT pricing further above the competitive level.
231. If, on the other hand, ARPU is to be taken as the only valid proxy for price in this context, this is a powerful argument against switching being price-related, since ARPU was essentially flat and on that basis there were no price increases to begin with, and thus any switching was for another reason.

*Dr Jenkins' Evidence on Secular Trend*

232. Part of Dr Jenkins' evidence here was to point out that in her Critical Loss Analysis ("CLA"), she has made a 20% adjustment to take account of any secular trend effect. The problem with this is that the basis for that particular adjustment is not clear. In the hot tub discussion she said that "okay, it is hard to know exactly what is going on there". She then said at Day 9/123 that:

"yes, there may be things going on that make bundles attractive and you have price changing at the same time" and stated that she did not see "how you can disentangle those two things...the price is an integral part of what it is driving at".

233. We did not think that these observations took the matter much further. Indeed, it seemed odd, because in conducting a market definition exercise, the task of distinguishing price from other influences - though seldom straightforward or uncontroversial - is one of the core tasks we would expect an expert economist to tackle.
234. It is correct that at p124, Dr Jenkins said this:
- “I am saying that when making that choice for any substitute product, it is always the case that what you are thinking about is the combination of the price and the product features that are going on. So even if it were the case that you said, well, the price stayed the same and the quality improved of bundles, and we saw switching towards it, that is still relevant, economically driven switching for the Voice customers. The other product is becoming more attractive.”
235. The problem about this statement is that it seems to us to place insufficient focus on the need to distinguish switching that is due to relative price changes, and switching that is due to changes in tastes and the perceived quality of broadband access (or the secular trend) that would have influenced customer changes irrespective of any pricing incentives. The economic logic of the SSNIP test clearly requires an assessment of price effects holding other things constant, and in this passage Dr Jenkins has failed to address this critical distinction.
236. In making this criticism of Dr Jenkins’ approach, we do not suggest that price is the only thing that matters, or that considerations of quality etc. do not affect the way competition and choices between different products work. Rather, the point is that this is precisely why it is necessary to isolate and hold constant those other factors when conducting the SSNIP test in order to understand the factors that would constrain the pricing conduct of an HM. Dr Jenkins’ approach did not really tackle this critical task.
237. This was exemplified when in the end, at Day 9/126, she said this:
- “Indeed, the way I structured my market definition analysis was to start by saying there is just a lot of switching from Voice sold at standalone to Voice sold in a bundle; in and of itself that is a clear sign that the two products are seen to be substitutes in some kind of way.”
238. Accordingly, we did not find Dr Jenkins’ evidence here very satisfactory.
239. We return to her evidence in the context of the specific points about switching which she made to support the general argument that SFV Services and bundles were in the same market, dealt with in paragraphs 391 - 397 below.

*Dr Jenkins’ Event Study on the Commitments Price Reduction*

240. At this juncture, we deal with Dr Jenkins’ “Event Study”, which she undertook, in fact in the context of unfairness, together with observations about it made by Mr Parker in the context of her CLA which is considered below. We think that it is highly relevant here because the evidence uncovered in this debate provides one of the strongest indications that VOCs switching was not primarily related to price.

241. The “event” considered by Dr Jenkins was the introduction of the Commitments on 1 April 2018. She deals with this at Section 7A.2 of HJ1 and Annex 10 thereto. Her analysis shows that the decline in VOC numbers slowed down after the Commitments, that the slowdown was statistically significant, and that it was consistent with those VOCs being responsive to price changes, in this context, price reductions. However, she went on to say that she was not saying that this formally demonstrated causality between the introduction of the Commitments, and switching away, but at least it ruled out as causes, the ASA Ruling or the result of an overall upwards trend in the rate of decline.
242. Mr Parker then drew upon the event study in this way in Annex A to the JES: the price reduction effected by the Commitments with a drop in SLR, from £18.99 per month to £11.99 per month, represented a 30% price change, if taken as a share of SLR ARPUs, assuming no change in call prices. Dr Jenkins’ minimum price elasticity figure for the purposes of her CLA (see paragraph 429 below) is -2.63. If that price elasticity was correct, then it would suggest that a 30% price fall would lead to an increase in VOCs of 78%. In fact, the VOCs fell by 9%. And even if the price elasticity for VOCs was somewhat different for SPCs, there would still remain a large unexplained difference.
243. Dr Jenkins’ response to this is to suggest that there is an “asymmetry”, whereby the elasticity in reactions against price increases is not the same as elasticity in response to price decreases. She suggests (without any clear evidential basis) that once an SFV customer has left BT for a bundle, for example, there is a disinclination to move again, even if it would be in response to a price decrease. We did not find this a persuasive point and even if there was some impediment preventing consumers switching back to SFV contracts, it would still not explain why switching from SFV to bundles continued after the Commitments, even if the rate of decline so far as the VOCs were concerned had reduced somewhat.
244. Mr Parker goes on to say that the better explanation for the 9% drop is that it is simply part of a gradual and consistent reduction in the number of SFV customers over the claim period, which is essentially a function of secular trend rather than pricing. We agree with him about that, and we think that the consequences of the event study amount to important evidence to show that switching is not primarily related to price.

*BT’s own perception as to reasons for switching*

Introduction

245. BT’s own view as to the reasons for switching, or “churn” as it described it, is relevant evidence as to what those reasons in fact were. One important way of assessing what its view was, is by examining the extent to which BT was concerned about churn occurring, or having occurred as a result specifically of its own SFV pricing decisions.

246. That BT monitored actual churn is clear. In paragraph 23 of JB2, Mr Bunt says that when he had been Head of Pricing in April 2015, he wanted churn rate to be monitored more closely and methodically than previously. In addition, and as from early 2015, BT used spreadsheets, which showed weekly churn rates.
247. One such spreadsheet, dated 8 February 2016, set out the numbers of customers for different services, who had churned in a particular week, and then a code for why they left. The code “Detrimental change Mgrsign off [manager sign-off]” applies where a customer, having been notified of a price increase, then elects to terminate without charge. “LLU (L)”, referring to local loop unbundling, is where the customer has gone to a broadband supplier. “Going to WLR competitor” is where a voice-only customer has moved to a different voice-only supplier.
248. As Mr Bunt explained at paragraph 26 of JB2, there were limits to the utility of the spreadsheet because the data was based only on those customers who had positively informed BT when they were leaving, or where it was obvious to BT what had happened because there was a transfer to a different voice-only supplier. In addition, sometimes, the call centre representative had been given a reason, but failed to record it. So the actual number of customers who left for a particular reason could be significantly higher. In the event, Mr Bunt still used the spreadsheet but he was aware of its limitations.
249. However, the documents that have particular relevance for these purposes are churn figures or estimates in the context of proposed pricing decisions, or in reviews of such decisions.

General views about churn and pricing: the documents and the evidence of Mr Bunt and Ms Blight

250. In this context, and in cross-examination, Mr Bunt was taken to a number of documents said to reflect BT’s views about churn. The first was the “BT Consumer: Q2 FY14/15 Consumer Operational Review” dated 30 September 2014. This was therefore looking at the immediate results of notification in August 2014 of the Robin/Window price increases which were to be implemented in December 2014. Among other things, it stated:
- 0.1% - incremental to BAU bill response PTC - forecast was 0.4%
  - 2k calls from 1.5m notifications, well below PTC forecast
  - 0.5k pushes of “No HTT button” to date
  - No material increase in customers ceasing directly due to price
251. The 2,000 customers who called in response to the price increase notification were all customers, not just SFV customers. This was obviously a very small proportion of total SFV customers, even if there were more who would be terminating because of the price increases than the 2,000 shown. This is reflected in the final sentence recording no material increase in customers ceasing directly due to price.

252. One then goes to Mr Bunt's 15/16 Pricing Plan dated 12 December 2014. At page 11 is an assessment of a proposal for a price increase of £2 (rather than £1) above the existing £16.99 but with an option for a new 18-month contract at a price of £17.49. On the figures, there would be a £12m benefit from those back-book customers who simply continued with their existing contract and paid the increased rate. On the other hand, there would be a loss from customers who chose to recontract at £17.49 (compared with them having to pay £17.99 on the basis of a £1 increase only) of £3.9m. Further, it was assumed that there would be £1.5m lost due to customer churn. Overall, there would still be a significant revenue benefit with a £2 price increase, but one notes the reference to "PR risk" and in the event the price rise was £1. What this document shows is that the levels of churn estimated by BT were insufficient to outweigh the revenue-increasing impact of a price increase.
253. On 15 January 2015, a further iteration of the 15/16 Pricing Plan was produced. At page 6, it stated that recent price changes had demonstrated that churn driven by price change was low, namely 2,500 voice customers exercised their right to terminate the contract having been advised of the price increases, out of a total of around 9m voice customers in total. It went on to say:
- "Based on this we can conclude that Price changes are sustainable with increasing subtlety."
254. Mr Bunt agreed that this meant that BT was satisfied that churn was not here an obstacle to price rises. He added that BT was contemplating other structures and approaches which might be looked at, but in fact the contemplated price rise did take place.
255. A churn analysis PowerPoint dated 19 January 2015 in relation to the implementation in December 2014 of the Window price increase stated that the evidence showed that, while a price increase was likely to cause a spike in churn for a short period, it was not detrimental to churn numbers. Overall, the churn impact to date had been minimal, but many customers may not have had their first quarterly bill showing the price increase and therefore the exercise should be run again at the end of Q4.
256. Then, on 4 June 2015, Mr Bunt was asked whether he could produce a revised 15/16 Pricing Plan paper. He did so, adding in an email that he anticipated that the churn for 2015/16 would be broadly similar to that in 2014/15 i.e. 2,000 customers. He added that:
- "our pricing scale decision are not based on complex elasticity modelling but rather on finding a sweet spot between budgetary needs and PR risk."
257. Mr Bunt said in evidence that the pricing decision may have been based on some other factors as well, but accepted that this comment showed that the decision was not being based on complex modelling of customer switching following a price increase. There was simply the predicted 2,000 customers which were the subject of direct churn.

258. Mr Bunt was then taken to a document dated 29 July 2016 called “Price Change 2017” which was produced shortly after implementation of the 2016/2017 price change. This stated that:

- We have seen greater churn than in previous years (7k) – however this is dwarfed in comparison to the additional revenue driven by the higher % increases. It is not clear how much this churn was driven by us or competitors (free fibre.) But for 17/18 we should be careful to not to over-tip the balance by repeating all of the higher % increases from 16/17

259. Mr Bunt accepted that the middle line was suggesting that it was not clear whether it was the price increase which drove away the 7,000 customers or some other competitive activity, and the example given was an offer of free fibre.

260. There was a later iteration of the same document dated 15 August 2016, which said this at p5:

**Price Change 1617 drove 8k incremental churn vs 1516 but is more than offset by the increase in revenue YoY, while PTC remains below target and only slightly up vs 1516**

- Increased churn is likely to have been driven by both a higher % increase in Price Change and highly competitive offers in market at the same time (e.g. free fibre)
- In 1718 we need to be wary of repeating a high % price increase and driving greater incremental churn

	1516	1617	YoY var	YoY %
Churn	23k	31k	8k	13%
Price change revenue	£133m	£196m	£63m	47%

261. What is clear from this is that BT were certainly alive to the prospect of some price-related churn (across the board) and it needed to be careful, going forwards; but on the other hand, it did not discourage BT from implementing the 2016/2017 price change. Mr Bunt added that in fact, because of the increase in broadband prices for 2016/2017, this would have made the overall price increase to bundle customers greater in percentage terms.

262. We should add that, notwithstanding the passage cited in paragraph 260 above, this document still assumed a price increase of £1 (see for example page 7). This had been foreshadowed in an earlier version of the same document dated 22 July 2016 where, at page 2, a key assumption was a price increase to £19.99.

263. In the event, by 19 October 2016, the decision had been taken to freeze the line rental price at £18.99. In answer to questions from the Tribunal about the reason for this (Day 7/56-57), Mr Bunt said that by this time, there had already been conversations with Ofcom in relation to its review (which had started much earlier, in 2016) and about offering a rental price freeze, and so BT would not have felt it could impose a price increase at that time. Mr Bunt had the timing right because, for example, in a letter to Mr Oxley of Ofcom dated 22 December 2016, BT was already offering a £2 line rental reduction for “true solus” customers (i.e VOCs) along with a price freeze, and an earlier document prepared for Ofcom stated that in previous discussions with Ofcom, BT had proposed a price freeze.



264. As against those documents, Mr Bunt was referred to some other documents in re-examination. One such document was “Consumer Voice Strategy 15/16 onwards” dated 19 March 2015. It is necessary to consider a number of elements of this. First, at p2 it states:

**Lines: Reduce solus churn to 16% within 2 years to maximise revenue and upsell opportunity**

- Execute continuous multi-channel recontracting plan to increase in-contract customer volumes
- Move customers to lowest churning products and deepen relationships to mitigate competitor churn
- Build capability to maximise recontracts with lowest possible operational impact (e.g. coupons and decisioning)

265. Mr Bunt explained that this was a strategy to reduce the churn from BT’s SFV customers and the rate of 16% is of course familiar from the switching rates described above. In fact, Mr Bunt said that it was nearer 20%.

266. At p5 it then says:

**Context**

Solus voice lines have seen a steady decline over recent years due to three main factors:

- General consolidation of services in the market place in bundles
- Competitor losses (30% of solus churn) driven by solus competitor attacks
- High levels of bereavement (21% of solus churn) on solus base

and

**Strategy**

- Reduce the solus churn by regular re-contracting activity across relevant channels
- Deepen relationship and move customers to lower churn products making it easier to upsell and harder for competitors to acquire (e.g. Free PCD attach, reduces churn rate by 8.4pp)
- Use a targeted approach to optimise ARPU delta, LRS mix, and CCSOs, underpinned by decisioning, targeted campaigns and advisor incentivisation
- Improved campaign agility and minimal operational impact through coupon expansion and optimising / expansion of decisioning

267. Mr Bunt explained that “competitor losses” meant predominantly the marketing and customer acquisition activities of the Post Office. Finally, he explained the references to product development and related matters which appeared at p5. He said that this was about how the development budget, which was available to make the products more attractive and work better, could reduce the need for customers to call, and to improve customer satisfaction.

268. We follow all of that, and see that BT was concerned about SFV churn. But nothing in this document expressed any concern about its own pricing behaviour in relation to churn. That is the key point. Indeed, what this document does not suggest is any need to reduce prices (or not have price increases) because of the risk of churn. Yet further, as we shall see, in our view, much of the switching we described was not price-related anyway.

269. Ms Blight was also cross-examined about this. She had said in paragraph 59 of MB1 in the context of a possible price increase of £2 for 2016/17, that this was not taken forward. While it would have created additional revenue, it was felt that this level of price increase would have undermined any positive press and customer reactions, and would have led to greater churn in the long run. She accepted in evidence that had there been any concerns about churn and competitor pricing, it would have been recorded in at least some of the relevant pricing slides. In fact, the slides contained in the 2016/17 pricing pack do not make reference to greater churn in the context of rejecting the £2 increase proposal. Instead, one of the points against such an increase was “PR red flag on £2 line rental increase”, in other words, much the same as the point made in relation to 2015/16 - see paragraph 252 above. It is true that Ms Blight suggested that PR and regulatory issues would have a knock-on impact on churn, and that it was obvious that a reason for not recommending a £2 increase must have been because of a concern over churn, but we did not find this a convincing explanation. When asked why it appeared that no one was saying that after 5 years of increases with customer losses every year, something was not right, Ms Blight suggested that perhaps their calculations were wrong and they should not have put up prices as much, and this would have saved churn. However, the point is that this did not happen. In reality, of course, the fact is that there were no concerns expressed in relation to the actual price increases for line rental of £1 or other amounts, or in relation to price increases for other elements of the charges to customers.

#### Home Phone Saver (“HPS”)

270. BT also cites the specific example of the introduction of HPS in July 2014 as showing that BT took the risk of customer churn into account in its pricing decisions. The churn risk at play here is said to be in particular the loss of VOCs to the Post Office and it should be noted that evidence on substitution from one SFV provider to another, even if it is related to price, does not address the SSNIP test question on SFV Services or assist BT in its argument for a wider product market definition.
271. To set some context, the Post Office had been providing (among other things) voice-only services since at least the beginning of 2013. It ceased to provide them when it sold its telecoms business to Shell Energy in March 2021.
272. The central features of HPS, once introduced, were as follows:
- (1) A single flat charge of (initially) £19.99, which was payable for a fixed period of 3 years;
  - (2) Unlimited anytime calls (“UAC”) to other landlines along with calls to mobiles at a competitive rate of 1p per minute; and
  - (3) Other features such as Caller Display and Anomalous Call Reject were included within the package.

273. When HPS was first being considered, BT's line rental was £15.99, whereas the Post Office line rental was £12, but with a separate charge for UAC.
274. Two questions arise: first, what were the reasons for the introduction of HPS and second, how exactly was it marketed?
275. As to the reason for its introduction, Ms Cheek (who was not involved at the beginning) said that she understood from colleagues that one of the reasons was to try and avoid customer churn. For his part, Mr Bunt said that HPS was an attempt to counter the trend of customer churn to the Post Office. In oral evidence, when asked why BT was not more price-competitive, given that its main competitor, the Post Office was significantly cheaper, he said that this was why BT introduced HPS, and that the documents all showed this.
276. In reality, the documents themselves do tell the story of the thinking behind HPS and the concern over churn to the Post Office. We set out what we consider to be the key documents below.
277. The first is the Project Robin 2014/2015 document dated 10 December 2013. As already noted, the key objective was to meet the revenue target, which was then expressed to be £67m. At page 6, a proposition (referred to as a "prop") was introduced, which ultimately became HPS. It said that there were 1.1m voice-only customers, of whom 200,000 were on BT Basic and of the remainder, 19% had left and 60% of leavers went to the Post Office. This amounted to around 100,000 customers per year. The core feature of the prop was then spelt out, involving, at that stage, a £20 per month charge as against the Post Office's £12 line rental and £5.75 charge for UAC. The benefit was described as follows:
- "Retain 19k customers in 14/15
  - PR defence for 14/15 price changes
  - Defence against the Post Office
  - Additional benefits:
    - Acquisition"
278. Under "implementation" it said that the prop would be targeted at existing BT customers who were pensioners, and it would be a key retention prop. It is plain from this document that the reasons for the proposal included both a defence against the Post Office and a PR defence for the impending price rises.
279. The next document is the 2014/15 Pricing Update dated 7 February 2014. At page 8, it referred to the 1.1m true solus customers, and that in 2012/13, 38,000 went to the Post Office and 80,000 went to other competitors. In 2013/2014, the projected loss to the Post Office was 27,000. The version of HPS then being proposed was set out at page 9 and its cost was said to be £1m. Assuming that 50,000 customers took it up and there was 80% cannibalisation. The latter refers to customers who in fact would have stayed with BT anyway, and might now take advantage of the HPS as opposed

to paying the standard line rental. Different iterations of the HPS are then shown at page 19 and the third, Option 3, was said to represent “a credible alternative to the Post Office and strong defence against future campaigns.” There is then a comparison between BT’s standard line rental and call package with that of the Post Office. It was noted that gross margin was very sensitive to the ratio of “saves”, i.e. those customers who took up HPS and would otherwise have churned, to cannibalised sales as described above. The minimum ratio was said to be 50:50. If there was huge cannibalisation, this would not have worked, because the HPS scheme would do more to reduce BT revenues than it did to retain them.

280. Page 35 addressed what were described as the key affected segment - namely older voice-only customers. Of those customers, it was said that there was 20% churn in a year and 20% of those went to the Post Office, again referring to a figure of 100,000 each year (although this does not square with the more modest figures given at page 8). These customers were “being pushed away by rising prices” and budgeting and peace of mind were very important for this segment. HPS was then said to be primarily a “save tool” to use as a PR defence and a “give” during the Robin price increase and not to be offered proactively on the BT.com website. It was available only to voice-only customers.

281. There was then a further version of the Pricing Update, dated 12 February 2014. Again, this refers to voice-only churn including to the Post Office. It said that the prop defended against the government’s concerns over mid-contract price rises and other things, Ofcom’s concern over bill shock and headlines around exploiting loyal customers and confusing plans and tariffs. The cost to BT was said to be £0.6m with a 50,000 take-up, and 80% cannibalisation.

282. In the Pricing Update of 5 March 2014 the rationale was said to be:

- “• PR Defence: Strong defence against criticism that our loyal voice customers get punished by rising costs of the service
- Regulatory: Strong defence against Ofcom argument that solus voice non-switchers are being penalised
- Churn reduction: 1.1m true solus customers, 15% annual churn, 90k competitive losses per year; FPS will help reduce churn”

283. The Project Window Execution Update dated 24 June 2014 contained detailed calculations of the “Save-Cannibalised ratio” and its Notes at page 11 included the following:

- “• Very sensitive to save : cannibalisation ratio.
- Important to get due credit and we want the press coverage but not the swell in take-up.
- We are notifying everywhere we have to, so we can say we are telling our customers about this – but nowhere else.
- Limit availability, only include in prose comms”

284. The Post-Investment Review-Home Phone Saver dated 23 January 2015 initially described the HPS (here referred to as FPS – Fixed Price Solus) as:

- “• PR Defence: Strong defence against criticism that our loyal voice customers get punished by rising costs of the service
- Regulatory: Strong defence against Ofcom argument that solus voice non-switchers are being penalised

- Churn reduction: 1.1m true solus customers, 15% annual churn, 90k competitive losses per year; FPS will help reduce churn”

285. It then said that 13,000 customers had been saved as opposed to the 9,500 estimated. There was said to be a 9.2% churn benefit, a £10.5m saving, but with a cannibalisation loss of £3.37m. Under the heading “PR Defence” there was said to have been positive reports on the BBC and in the Guardian and national papers.
286. Under Actual Project Performance after stating better than expected results, it went on to say:
- “The risk remains of revenue cannibalisation for customers that would have taken higher margin products. This is managed by restricting the availability of the product and ensuring it is only focussed on high propensity to churn customers.”
287. It is plain from these documents that HPS was intended to serve a number of purposes and there were two main ones. First it was a response to customer churn, and in particular to that to the Post Office. Second, it was a PR defence to the various concerns which had been picked up about this group of customers in the media and by Ofcom, and in relation to the reaction to the general line rental increase that was going to take place. In other words, HPS was neither a simple reaction to the Post Office, nor could it be seen as “merely” a PR defence.
288. It is important to note that the financial consequences were carefully thought through. That was because of the need to balance the revenues that BT retained from those who took the HPS as opposed to leaving altogether with the revenues it lost to those who would not have left, but took advantage of the HPS pricing when they might otherwise have stayed with BT on the standard tariff. This leads into the second aspect of HPS, namely the nature of its marketing.
289. Because of the careful ratio between saves and cannibalisation which had to be maintained, BT did not want HPS to be taken up by “all and sundry”, as it were. As some of the documents above show, it was very much a targeted retention tool. Its availability would be shown in all customers’ bills with the price changes. Beyond that, BT wished to concentrate the promotion of HPS on those customers whom it thought would otherwise leave.
290. This explains the references in the Project Window Execution Update dated 24 June 2014 cited in paragraph 283 above. In addition, that document also stated at p10:
- “Objective
- Limit marketing to customers during Window whilst demonstrating externally that the prop is widely available...
  - Reactive saves only...
- Targeted Marketing
- From September we will target high churn risk ‘true’ solus customers. This helps with the save ratio.”
291. Then, by an email dated 8 June 2016, Mr Bunt provided what he said should be the advice to BT’s call centre staff, as follows:
- “Thought it through and there are 2 things I want to say: 1. Stop pushing the button 2. Stop proactively selling HPS

Here's my proposed wording – let me have your thoughts: “There are a couple of tweaks we need to make to how we are working to make sure this price change continues to be extremely successful. Firstly, a reminder that we should only be pushing the AOT button If someone is upset with our price change and is off to talk to someone else about switching their service – and they tell us so explicitly – then we need to “push the button”. We must make sure we only push that button if a customer is upset because of the price change, the button isn't for general dissatisfaction and a customer needs to be specific before we press. Secondly, Home Phone Saver 2019 is an important tool that we should use to save customers. We should also use it if customers call and deliberately request it. It should only be used in those 2 circumstances and we need to ensure that we aren't providing it to customers without a strong reason.”

292. AOT here stands for “Advice of Transfer”. In this context, COT stands for “Customer Options Team” which would deal with a customer who wished to cancel their contract.
293. As to this, Mr Bunt said that in fact, BT wrote to over 1m customers referring to HPS in the context of the price increase letters, and beyond this, it was targeted marketing. The former is simply a reference to all of the eligible VOCs and it is common ground they would have seen HPS on the relevant letters. However, the point of Mr Bunt's instructions was to limit customers' exposure to HPS otherwise, which he accepted. This was because BT did not want SFV customers to “sort of stumble across the product” as it was directed only to those who were likely to switch and because of the risk of too much cannibalisation.
294. Subsequently, there was a change of approach which coincided with Ofcom's renewed interest in BT's pricing. Thus Jeremy Benson at BT emailed as follows to Stuart Murray as follows on 31 October 2016:

The customer [REDACTED] spoke to BT several times over the weekend as her Mother-in-Law has moved house. She asked about Home Phone Saver and was told a number of times that it wasn't available to new customers. She had been on Virgin in her previous property.

We looked into this to see if it was a wider issue. From what I've found out, in a nutshell, we were selling 'too many' (not a good product for us commercially as you know), so we made it unavailable on certain systems (Agent.com), and some advisors could not see (and thus sell) it. It could only be ordered on Oneview which had restricted access for advisors.

This has now been rectified with Emergency briefs sent to advisors last week, so all advisors should have visibility of it on their systems and be able to sell to customers.

I have asked the commercial team to confirm that HPS won't be restricted in future and that customers will always be able to buy it.

295. Then, on 1 November, Mr Benson suggested as follows:

Yes we have – that given the current state of play with Ofcom on solus voice, we’ve emphasised that Home Phone Saver is a key part of our (solus) defence strategy with them, and that we need to make sure all our advisers have the correct information, and that HPS is fully available without any (commercial) restrictions in place. We wouldn’t want any complaints getting to Ofcom from customers saying they couldn’t get it.

The business fully understand this, and are following up with the key Channel teams for their assurances, and seeing whether there is anything else we can do to add greater certainty (e.g. an updated blanket briefing).

Would it help if I drafted a note for you to send to Kelly Barlow, underlining the importance of ensuring sales are not restricted, although I think the team has it under control now?

296. Mr Murray responded that the position might not have been exactly as Mr Benson described it, and BT might need to change its position with Ofcom on HPS, but nonetheless there was clearly a recognition that HPS may need to be promoted more widely. Mr Bunt accepted that the context here was Ofcom’s price concerns.
297. While BT at paragraph 168 (d) of its Response dated 19 May 2017 stated that
- “Given the active marketing by BT of the Home Phone Saver product, there can be no suggestion of a price discrimination strategy. Rather BT created this product in the face of competition from the Post Office.”
- we do not think that this tells the whole story, notwithstanding Mr Bunt’s suggestion in evidence that it did.
298. First, it is clear that HPS had not always been actively marketed, even if, by the time of the Response, a decision had been made to open it up fully, in the light of Ofcom’s pricing concerns (See paragraphs 294 and 295 above). Second, while the competition from the Post Office was part of its rationale, it was not the whole of it. See paragraph 287 above.
299. In re-examination, Mr Bunt was referred to the Consumer Update from Mr Petter, the CEO of BT Consumer. At p10, Mr Petter said that HPS was available to existing customers through BT’s call centres. That was true, although there were the limitations on how it was offered there, referred to in paragraph 291 above. He added that all relevant customers were written to about the product in the annual price change notification, which is common ground. He then said that there were targeted campaigns and that by June 2016, 165,000 customers had taken up the 3 iterations of HPS to date. He went on to say (and this was pointed out to Mr Bunt in re-examination) that BT had sent more than 4 million communications promoting HPS over the last 2 years. On the face of it, that must be a reference to, or included, writing to all customers as part of the price change notification, which would have happened 3 times in the previous 2 years. So, in our view, what was said here is not inconsistent with what emerged from the documents referred to above.
300. Equally, reference was made to the BT Update magazine of September 2014. HPS was referred to in it as one of a number of “great deals”. This was, according to Mr Bunt, a “bill insert magazine” so it was put in every single bill to the relevant customers. The Update concerned in fact looks like one that may have come with price notification letters, as this is what the first substantive page

speaks to. However, in any event, it was clearly not the targeted marketing which Mr Bunt himself (and the documents referred to above) confirmed was limited to those customers who BT considered constituted a high risk of churn.

301. Overall, there is, of course, nothing wrong with BT choosing to limit the way in which HPS was marketed, and we would agree that it was a targeted retention tool. However, what it does mean is that it was a limited exercise in the context of pricing decisions and it was obviously not a direct response to the Post Office's pricing in the sense of BT deciding not to increase line rental, or decreasing it. Further, since HPS was targeted at customers who it feared would switch to another SFV supplier, the substitution threat at issue here has nothing to do with the substitution between SFV and bundles that lies at the heart of BT's arguments on the relevant market. We do not consider that the case of HPS therefore adds much on the issue of market definition in the context of churn.

#### *Competition from the Post Office*

302. Clearly there were some VOCs who switched to the Post Office which had significantly cheaper prices. But as a proportion of the Class, this was relatively small (see paragraphs 277, 279 and 280 above) and so it cannot by any means constitute the primary driver for switching overall.

#### *Conclusion*

303. Overall, we think that the evidence shows that the primary driver for switching was indeed the secular trend which would have exerted a downward pressure on SFV demand irrespective of price movements. That being the case, BT's arguments against a narrow SFV market cannot rely on switching away from SFV alone, and must identify the extent to which the threat of further switching (over and above that which would occur in any event) provides a competitive constraint on the hypothetical monopoly supplier of SFV. In fact it did not show that there was a significant threat in that sense.

#### **Summary of Mr Parker's approach**

304. Mr Parker employs three different "real world" data sets which he says all show that the SSNIP test has been passed i.e. the market is the narrower one of SFV Services.

#### *SPC-Dual play bundle price differential*

305. First, he takes what he says are the significant absolute price differentials at any point in time between SPC pricing when added to a standalone broadband on the one hand, and DP bundle pricing on the other.

#### *Line Rental Price Increases*

306. Second, he relies on the fact of significant increases in line rental pricing both before and during the claim period, even though wholesale costs were decreasing.



### *Call Price Increases*

307. Finally, Mr Parker relies upon what he says were call price increases (and differentials between BT and other providers' call pricing) over the claim period, based upon ARPM.

### **Summary of Dr Jenkins' Approach**

#### *Switching per se*

308. Dr Jenkins' first, and more general approach was to say that the very fact of the extensive switching referred to above show that standalone voice services, and bundles are both part of the same market.

#### *Dr Jenkins' Critical Loss Analysis ("CLA")*

309. Second, and more specifically, Dr Jenkins relies on her CLA, which can be a useful way to apply the SSNIP Test. It involves, ultimately, a comparison between a notional "critical loss" of customers to the HM, following a price increase of 5-10%, and the "actual loss" of customers in response to actual price changes. In both cases, the loss of customers is expressed as a percentage of the original customer base. Dr Jenkins' CLA showed that the actual loss would exceed the critical loss, which means that the SSNIP test failed, which in turn points to a wider market.

#### *Bundles as constraints on SFV Pricing*

310. Finally, Dr Jenkins posits that, because of how BT's line rental and call price increases were applied across both SFV and bundle customers, it follows that bundles did indeed exercise a constraint on SFV pricing, in which case they must both be in the same market.

### **Analysis: Mr Parker's Approach**

#### *Mr Parker's use of BT price data*

311. Before turning to the detail of Mr Parker's 3 datasets and the particular points taken against each of them by BT, there are some general objections to his approach, which should be considered first.

#### Introduction

312. The SSNIP test framework is based around a 'thought experiment' in which the competitive constraints on an HM of a candidate product are assessed, based on available market evidence and other insights. Since the candidate market in the current case is SFV services (including VOCs up until 2017 but excluding them after 2018), and since BT itself supplied a substantial share of this candidate market in the earlier period (and over 90% in respect of SPCs only after 2018), it is inevitable that much of the empirical analysis for the SSNIP test was based around the observed pricing and consumer responses faced by BT itself.
313. Thus Mr Parker has focused on BT's own pricing in different ways for each of his data-based SSNIP analyses, and Dr Jenkins has deployed BT data on the switching figures and has also used its gross margin for the purpose of her CLA. Further, in the price elasticity calculations which form part of her CLA, she has used BT's line rental pricing.

314. However, Dr Jenkins says that Mr Parker should have taken steps to distinguish BT's actual pricing decisions from the pricing that might be observed from an SFV HM. This is because BT is a multi-product firm, facing competitive dynamics in that context, whereas the HM must be taken to be a single-product supplier. Why this matters is because it is then said that the pricing decisions made by BT are not necessarily reflective of what a HM might charge, because it may be internally rational for BT to increase price by more than 5% or 10% above a benchmark in a notional SSNIP test, even though a HM would not do so because it would lose too many customers and thereby become unprofitable. In fact, Dr Jenkins' objection is not so much to the use of BT data as such. At paragraph 5.2.14 of the JES, she agreed that:

“...it is standard practice to use the data from an incumbent with a large product share as a proxy for the data that would be available from a hypothetical monopolist if it existed, Mr. Parker's argument goes further than this as he is using the behaviour of the incumbent in his argument. He relies on the decision of BT to implement and not reverse the pricing policy that they did and it stands or falls on whether the hypothetical monopolist would have found it profitable to make the same decisions.”

315. So the objection is not to the use of BT data as such in conducting the market analysis (indeed given BT's high share of SFV Services it would be hard to conduct any market analysis without including some BT sales), but rather to the inferences that Mr Parker sought to draw from BT's pricing and commercial conduct, given that BT's position and commercial incentives differ from that of the HM. Further, Dr Jenkins says that the outcome of her objection is not to say that there should be some modification of the BT price data to be used in the SSNIP test; rather, it is to disregard the BT's pricing decisions entirely, on the basis that the subject of the test is not BT but the (different) HM.

316. As we discerned during opening arguments, there are really two versions of this objection, a strong and a weak one. The strong version is BT's supposed “migration intent” and the weaker one (because it does not depend on such a specific intent) may be referred to as the “recapture effect”. We deal with each in turn.

#### BT Migration Intent

317. This describes a supposed motivation on the part of BT to set line rental prices at a relatively high level, in order to incentivise SFV customers to move over to BT bundles, which, because they cost BT only marginally more to provide, would actually yield higher profits for BT despite the small increment in the price between SFV and bundles. This suggestion first appeared in BT's Response to the CR's CPO application at paragraph 68 (although in fact referring to other telecoms providers). Ms Blight also referred, at paragraph 29 of MB1, to BT encouraging customers to take BT bundles, although she does not actually say that BT increased its line rental prices in order to do so. As for Mr Bunt, at paragraph 33 of JB1, he said that:

“I agree with what is said in paragraphs 66 to 68 of the Response about the competitive factors that encouraged providers to incentivise the take-up of bundles including broadband. In my role within Voice Pricing, one of

the key drivers to BT's pricing strategy was to move customers away from voice only services to broadband and bundles. In fact, during my whole period at BT, the overall strategy has been to get customers online using BT's broadband packages, which we achieved in a number of ways: (1) through marketing generous broadband bundle offers to new customers; (2) through cross-selling of broadband packages to existing landline only customers; and (3) by launching targeted products such as BT Basic plus broadband,."

318. However, he accepted that none of the documents put to him showed any such intent on the part of BT, except for an email exchange dated 29 December 2015, in which there was a reference to the fact that while the aim was to make the VOCs take broadband and become "stickier" which would support broadband growth,

"aggressive deals to date have not persuaded them to take-up BB therefore a step change here is unlikely."

319. Mr Bunt said in evidence that this was an example of migration intent, but we disagree.

320. As for Mr Parker, he doubted the relevance of the suggestion in terms of any argument that bundles acted as a constraint on SFV pricing. Indeed, he pointed out that the opposite would be true, because it would create upwards, not downwards pressure, which would be inconsistent with BT's argument that bundles acted as a price constraint for SFV Services.

321. Then Dr Jenkins took up the point in HJ2 and in particular at paragraph 3.59-3.66. This was in the context of the suggestion that Mr Parker was conflating the position of the HM for the purpose of the SSNIP test with BT's actual position.

322. We do not accept that there was any such migration intent on the part of BT. This is because, first, there is in truth no witness evidence from BT to support the notion that it was acting in this way when setting or increasing SFV prices. Moreover, there was nothing in its extensive documentation disclosed to support this idea. Ofcom reached a similar conclusion at paragraph 3.42.3 of the 2017 Provisional Conclusions which was responding to a submission made by BT (through Oxera) that there was such an incentive. There is simply no factual foundation for it and in the end, BT did not strongly press the point in its closing submissions.

323. A further point made by Mr Parker against the migration intent theory is that it was implausible anyway, because it assumed that bundles were more profitable for BT than SFV Services, which was not correct. That criticism turned on whether the appropriate comparator in this context for profitability was gross or net margin.

324. Dr Jenkins says that the correct metric is absolute gross margins (i.e. in cash terms), and that selling bundles created a higher gross margin per customer than selling SFV Services. The latter point is plainly right, since BT was providing an additional service (i.e. broadband) for an additional price and there were economies of scope. See paragraph 11.9 of Annex B to the JES. Nor is it suggested that bundles were being sold at a loss.

325. For his part, Mr Parker says that the comparison should be with net margin, and when one takes into account incremental costs and contribution to common costs, on his analysis, SFV Services were more profitable than bundles. He also cited Dr Jenkins' own evidence, which endorsed the need for firms to cover their indirect cost as well as direct costs in order to trade profitably in the long run. Of course, all of that, then turns on the detailed (and diverging) analyses of costs for the purposes of arriving at a competitive benchmark by each side's experts for the purpose of Limb 1.
326. We do not consider it necessary to explore this further issue in any detail here. It seems to us that in this context, BT Consumer may well have looked at differences between SFV Services and bundles on an absolute gross margin basis. And certainly, Mr Bunt said that they looked at pricing very much through the prism of gross margins. However, Mr Cackett's evidence was clear that from BT Group's perspective the ultimate focus was on a net profit figure that did take account of indirect as well as direct costs, which would tend to support Mr Parker's approach. But at the end of the day, none of that means that BT in fact raised SFV prices in order to migrate customers to bundles.

BT's Recapture Effect: Introduction

327. In the particular case of BT, it is obviously correct that if an SFV customer, whether VOC or SPC, switched, that customer might then take up a BT bundle. If so, BT has thereby "recaptured" the customer.
328. Dr Jenkins refers to recapture rates in the context, again, of the suggestion that Mr Parker has conflated the position of the HM with BT's own position. Her point is that, while pricing at a particular level may still be profitable for BT (because although it loses SFV customers, it recaptures some of them and their revenues in additional bundle sales), the question is what the HM, as a notional single-product supplier, would have done. To put it another way, since DP and other bundles were seen as the closest competing product to the candidate SFV product market, there is a clear risk that BT's commercial stake in this substitute product could distort a SSNIP analysis that was based on BT's pricing incentives and market conduct. Therefore, the pricing conduct of BT cannot be equated with the conduct of the HM.
329. Dr Jenkins deals with the facts behind this at paragraphs 3.62-3.64 of HJ2. Her Figure 3.5 shows that a substantial proportion of SFV customers leaving (between 42% and 50% over a 6-year period) who cited price increases as their reason for doing so, in fact switched either into a BT bundle or BT mobile. Mr Parker produced his own figures, but they do not differ very much. For Dr Jenkins, BT's recapture incentive (i.e. the fact that BT's revenues would be recaptured and even enhanced if an SFV customer who switched away from BT traded up to a BT bundle), was a core part of Dr Jenkins' description of pricing and BT's motivation.

330. There was broad agreement between the experts on the fact that the price gap between BT's SFV and DP bundles was small, but they adopted very different interpretations of this evidence. In contrast to Dr Jenkins' view, Mr Parker considered that the small increment in price arising between SFV and the DP bundle arose from the fact that bundle prices were competitive whereas SFV prices were excessively high due to the absence of effective competition in this product.

BT's Recapture Effect: Analysis

331. As has already been noted at paragraphs 323 - 325 above, Mr Parker's conclusion was that bundles were significantly less profitable than SFV contracts on a net profit basis (i.e. when an appropriate account was taken of indirect costs).
332. The relative net profitability of SFV versus bundles is a complex matter to assess, but the fact that BT earns positive margins on bundles, and that its business is clearly set up to compete actively for such sales, is sufficient to create a recapture effect that does need to be taken into consideration when assessing BT's pricing of SFV services, and which also calls for caution in treating BT as synonymous with the HM in the SSNIP test.
333. The standard economic analysis of pricing, where such recapture incentives are present, is that it will tend to increase the price level that the affected firm will charge in the primary product market - in this case SFV services. The rationale is simple: if there is any finite probability of some recapture, and provided positive profits are earned on the related product (in this case bundles), then the commercial harm from losing sales in the primary product is mitigated and this will in turn relax the constraints that would otherwise deter the firm in question from raising the primary product price.
334. While Dr Jenkins was keen to emphasise the demand-side linkages between SFV and bundles, we should note that this raises the possibility that the recapture incentive could cause BT to elevate SFV prices in a manner that might support the CR's market power allegations. In theory, a monopoly supplier of a product X that also supplies and benefits from recapture to a related product Y might be expected to charge a price in excess of even the standalone monopoly price level for X in order to take account of the recapture incentive. Therefore, this phenomenon only increases the extent of the Cellophane Fallacy which we discuss in the context of Dr Jenkins' CLA at paragraphs 424 - 430 below.
335. For his part, Mr Parker had originally been critical of Dr Jenkins' reliance on BT's recapture incentives prior to the Hearing. For example, at paragraph 10.20 Annex A3b of the JES he commented:

"I note that the recapture rate is only relevant if bundles are more profitable than SFV Services, as in that case BT would have some incentive to try and move its SFV Customers onto bundled products. The analysis in Annex A3a above shows that, under Dr Jenkins's own categorisation of the revenues and costs of providing

BT Services, BT Bundles are less profitable in the long run than BT SFV Services. It therefore would not be economically rational for BT to try to migrate customers from more profitable SFV Services to relatively less profitable bundled products. There is, therefore, no rate of recapture which would be consistent with it being rational for BT to increase its prices of SFV Services, given Dr Jenkins's elasticity estimates..."

336. In the body of the JES at paragraph 5.1.4 he said that:
- "the recapture incentive is not relevant when considering the differences in incentives between BT and the hypothetical monopolist, as there is no evidence to suggest BT faced such an incentive."
337. Even accepting that bundles were less profitable to BT than SFV contracts, this conclusion does not seem credible (unless it were established that BT actually made no profit from selling bundles).
338. However, following some exchanges between the Tribunal and the parties during their Oral Openings, Mr Parker appeared more willing to accept that the recapture point might have some relevance. In DP5, submitted during the Hearing on 6 February 2024, Mr Parker advocated the adoption of a variant on the standard HM test in which the analysis instead considered a hypothetical multi-product monopolist test ('HMMT') as a way to deal with this factor. The HMMT is a concept found in the industrial organisation literature and is also discussed in the US DOJ Horizontal Merger Guidelines under a different term, as a way to deal with the economic assessment when horizontal mergers between multi-product firms take place. Mr Parker argued that in the current case, the HMMT would be a monopoly supplier of both voice and bundles, and that the test should be whether that firm had the power to impose a SSNIP.
339. This change of tack and new expert evidence prompted a procedural objection from BT's counsel, but this effectively disappeared when Dr Jenkins produced HJ3, which heavily criticised Mr Parker's adoption of the HMMT test in this case, arguing that it took the analysis of market definition well beyond its intended first stage status and attempted instead to complete a full competitive assessment. With some justification, she criticised Mr Parker's HMMT as defining a broad candidate market that encompassed all sellers of SFV and bundles in a single frame. The fact that such a broadly defined hypothetical firm might have market power was incapable of shedding much light on whether BT alone possessed such power as a supplier of SFV services. Moreover, in the end, the late raising of the HMMT point by Mr Parker did not in fact leave enough time for a thoroughgoing analysis of it, by either expert or indeed the Tribunal.
340. As matters stand, our considered view is that the market definition exercise here should focus on the conventional HMT (HM test) rather than Mr Parker's suggested HMMT. Further, in making the assessment of BT's position in that market, it seems clearly right that we should take due account of the fact that BT is an important supplier of bundles as well as SFV services. In other words, there was potential for the operation of a recapture effect. However, it is more difficult to assess the significance of that factor here. After all, the recapture position was not complete, because BT did not recapture 50% of those who provided the data referred to in paragraph 329 above, and on Mr

Parker's own analysis the margins earned on bundles were far thinner than those earned by BT on SFV sales.

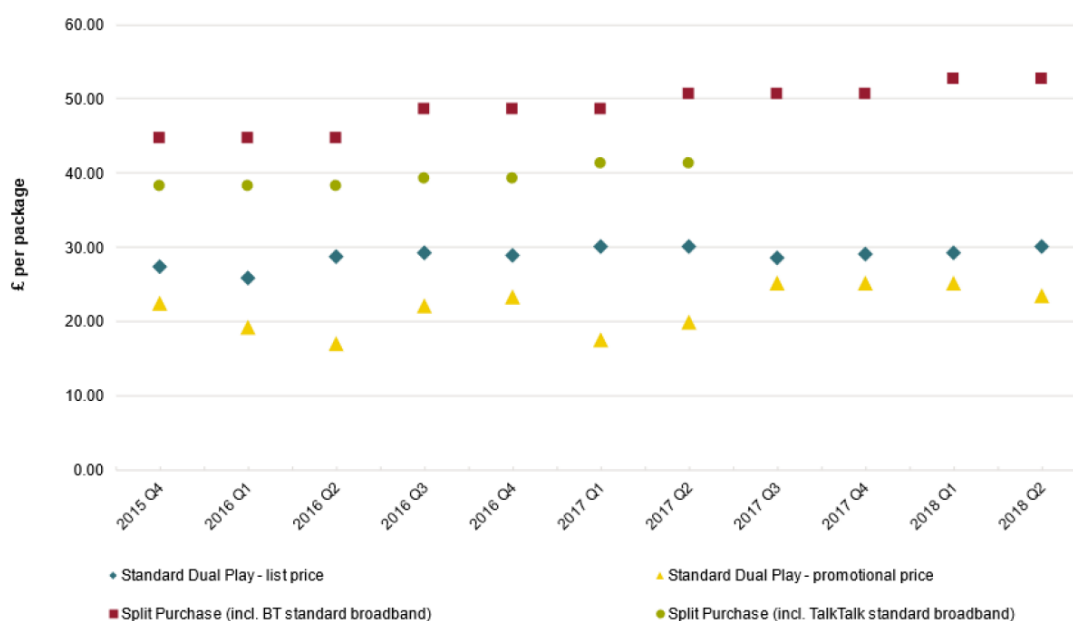
341. We do not think that the recapture effect point materially affects Mr Parker's SPC-Bundle Price Differential argument. This is not simply because it is hard to quantify, but because the differentials he arrives at are far in excess of the typical SSNIP of 5-10% anyway. See paragraph 348 below. As for line rental increases, we do not agree that they can be examined in isolation anyway, and once the relative margins are built in (see paragraph 378 below), the difference between them is such that even some adjustment to take account of the recapture effect would not destroy the point. Finally, on call charges, we reach the view that the argument here does not assist the CR anyway – see paragraph 390 below.
342. Accordingly, and overall, we do not think that the point about recapture effect, although valid in itself, affects the outcome of our views of Mr Parker's evidence, or indeed on market definition as a whole.

#### *Mr Parker's SPC-Bundle Price Differential*

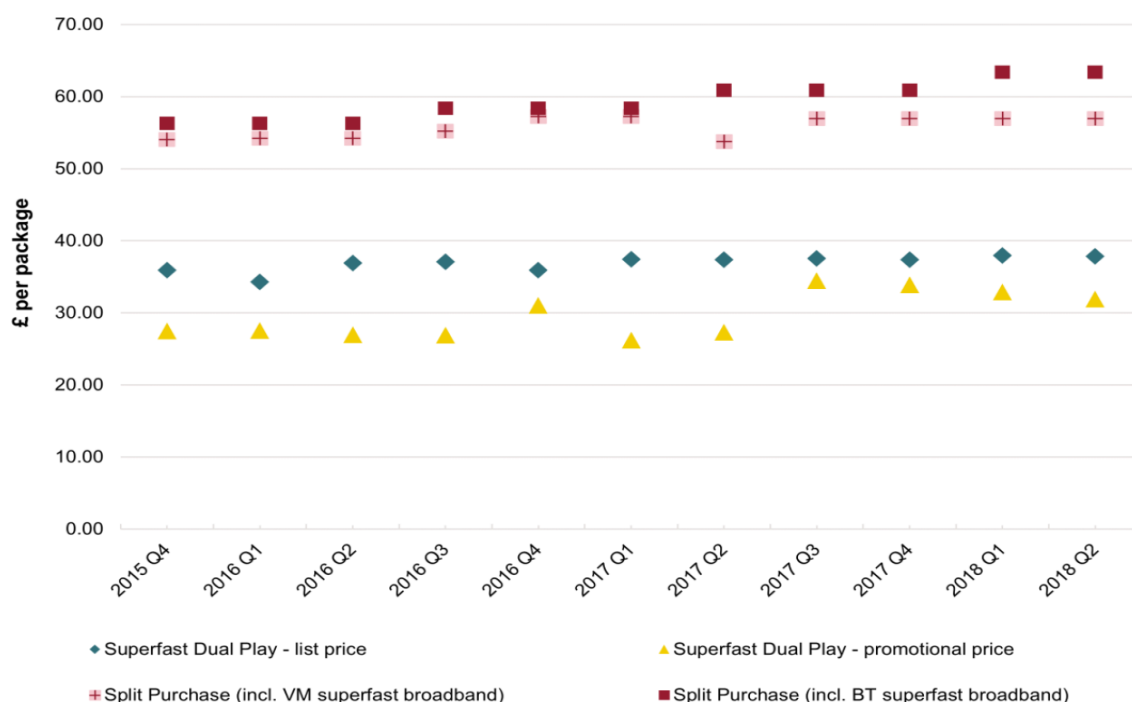
##### Description of the approach

343. The differential relied upon by Mr Parker between the price charged to SPCs who have separate voice and broadband contracts, and dual bundle prices, is set out at Figures 7 and 8 of DP3:

**Figure 7 Total prices paid by Split Purchase Customers and Dual Play Customers for the access component of fixed voice services and standard fixed broadband services, 2015 Q4 – 2018 Q2**



**Figure 8** Total prices paid by Split Purchase Customers and Dual Play Customers for the access component of fixed voice services and superfast fixed broadband services, 2015 Q4 – 2018 Q2



344. The dark red squares in Figures 7 and 8 show list prices to split service customers, i.e., the minority of SPCs (20% or less) who purchased both standalone voice services and standalone broadband services from BT. In the case of Figure 8, the light red squares show list prices to split service supplier customers who purchased both standalone voice services from BT and standalone broadband from Virgin Media.
345. The green dots, for Figure 7, represent the BT fixed voice price plus the list price of the TalkTalk standalone 17MB/Unlimited broadband package.
346. For both Figures 7 and 8, between Q4 2015 and Q1 2017, the yellow triangles and blue diamonds show, respectively, the average of the cheapest available promotional price for a dual-play bundle from BT, PlusNet, Virgin Media, TalkTalk, Sky and EE (yellow) and the average of the cheapest available list price for a dual-play bundle from the same providers (blue).
347. Mr Parker says (as is correct if the Figures are correct) that this means that:
- (1) SPCs who bought voice and standard broadband under separate contracts between 2015 Q4 and 2018 Q2 paid, on average, depending on the choice of broadband provider, in the range of:



- (a) £11 to £20 (or 37% to 69%) more for fixed voice and broadband services than customers purchasing standard Dual Play at the list price, with SPCs paying a minimum of £9 (or 33%) more in any given month; and
  - (b) £19 to £27 (or 88% to 123%) more for fixed voice and broadband services than customers purchasing standard Dual Play at the promotional price, with SPCs paying a minimum of £16 (or 70%) more in any given month; and
- (2) SPCs who bought voice and superfast broadband under separate contracts (see Figure 8) between 2015 Q4 and 2018 Q2 paid, on average, depending on the choice of broadband provider, in the range of:
- (a) £19 to £22 (or 51% to 60%) more for fixed voice and broadband services than customers purchasing superfast Dual Play at the list price, with SPCs paying a minimum of £16 (or 44%) more in any given month; and
  - (b) £26 to £30 (or 89% to 100%) more for fixed voice and broadband services than customers purchasing superfast Dual Play at the promotional price, with SPCs paying a minimum of £23 (or 65%) more in any given month.

348. He noted that these differentials were far in excess of the typical SSNIP of 5-10% and that they appear to be sustained. This is therefore an example of price discrimination, proving that SFV (or here the SPC element of it) and bundle customers are in different markets.

349. Of course, this is only dealing with SPC pricing. However, Mr Parker says that this is an appropriate proxy for VOC pricing as well. That is because in the period relevant for VOCs, namely pre-Commitments, it is accepted that VOCs and SPCs were in the same market and indeed BT was not able to distinguish between the two. We are not convinced that this logic works and consider that the Price Differential argument can be used in respect of SPCs only. On the other hand, there is, for VOCs only, the effect of Dr Jenkins' "event study", which supports the CR's case on market definition. See paragraphs 240 - 244 and 434 above.

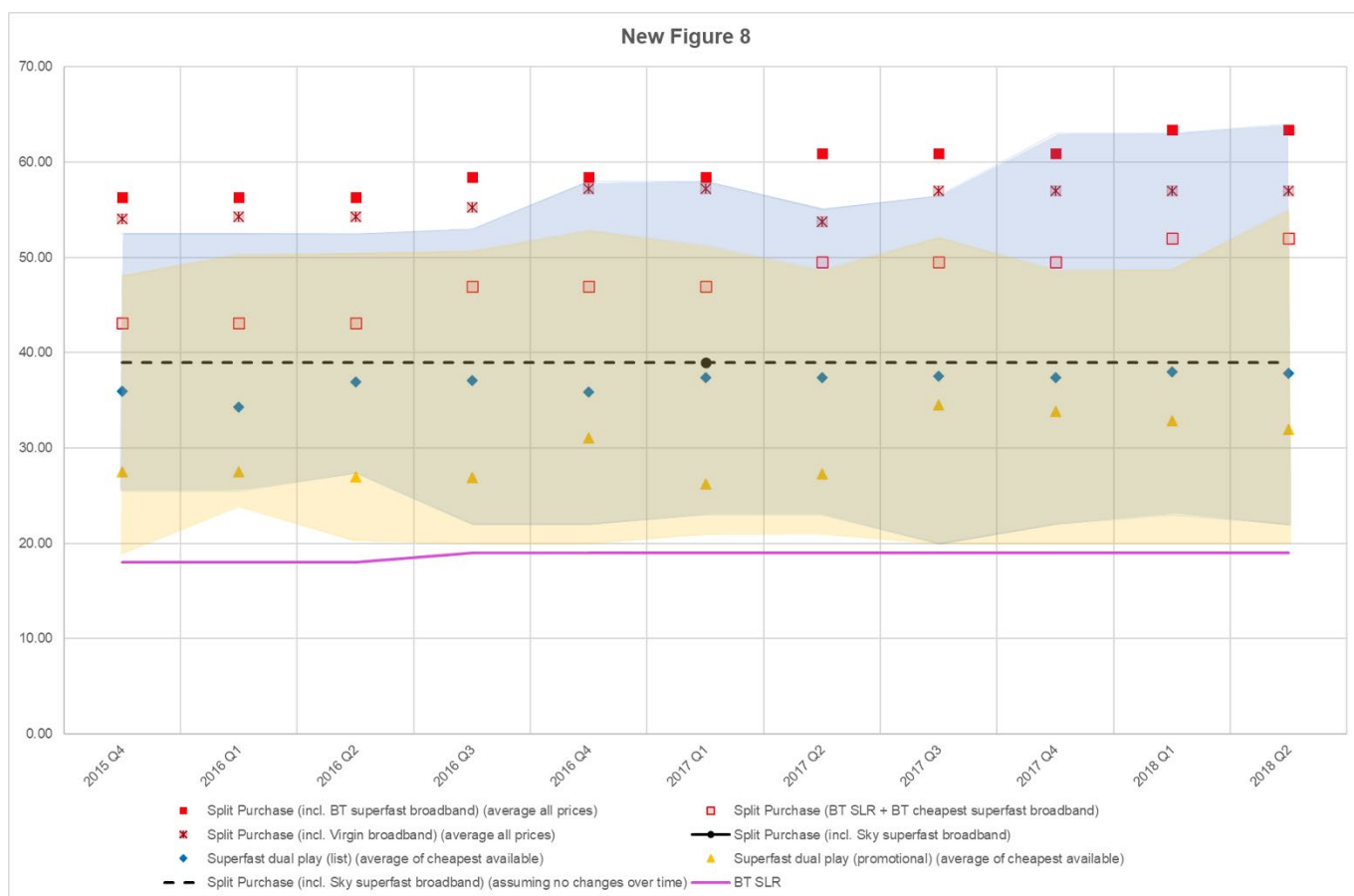
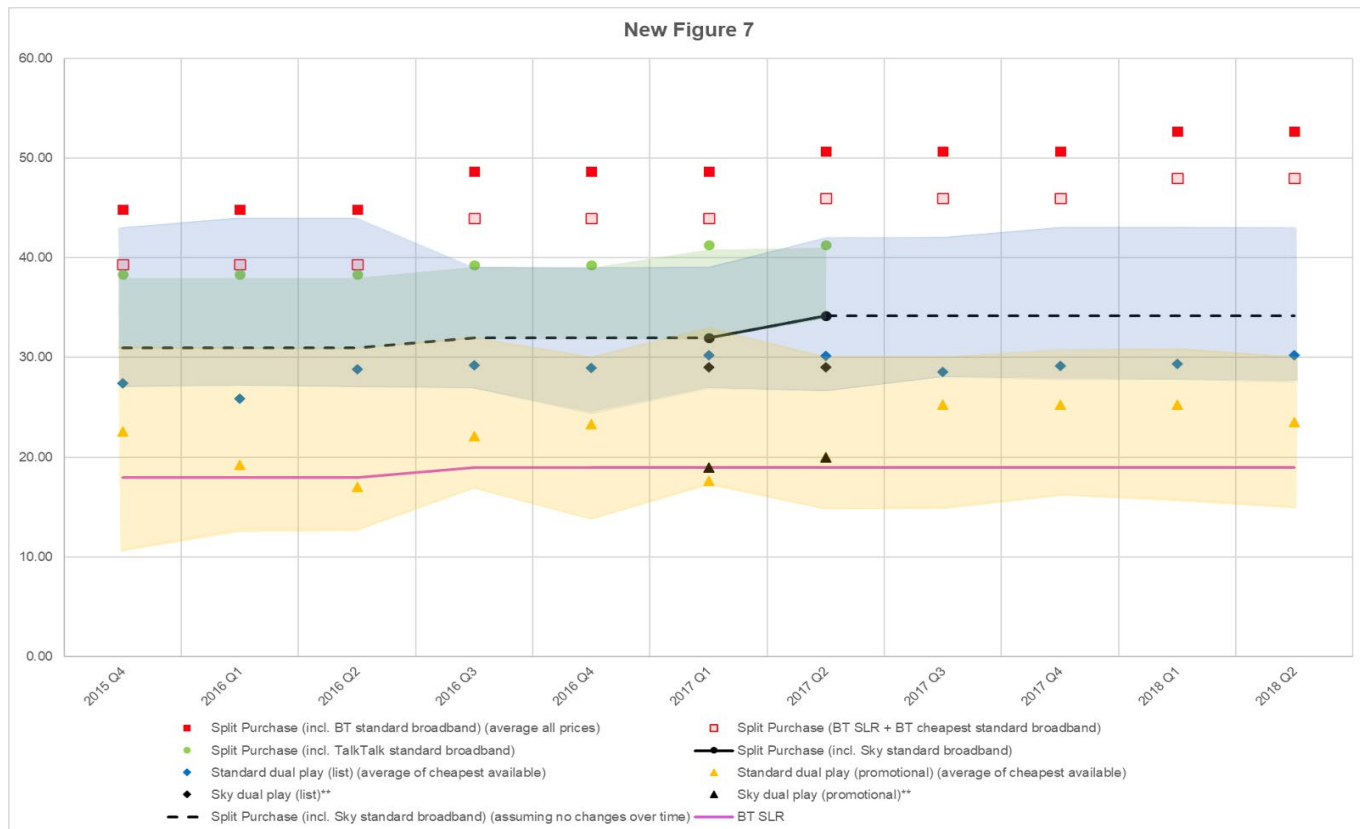
#### The Price Differential

350. We here deal with the particular figures used by Mr Parker in his Tables 7 and 8. Mr Parker's dataset essentially comes from Ofcom's Supporting Evidence, along with its "Pricing Trends for Communications Services in the UK" reports for 2020-2022. Indeed, for Ofcom, the relevant differential between SPC pricing and bundle pricing was such that it concluded that SFV Services were not in the same market as bundles. See in particular paragraph 3.41.1 of the 2017 Provisional Conclusions.

351. Prior to the trial, while Dr Jenkins had made a number of general objections to Mr Parker's use of this differential (dealt with above), she did not challenge the particular figures used in his Figures 7 and 8 and did not produce any alternative sets of figures herself. At paragraph 5.2.5 of the JES, and in the hot tub discussion, she said that she had no reason to doubt his figures. Although she questioned whether SPCs would have paid list prices to the broadband supplier, she accepted that no alternative figures had been produced by BT.
352. However, in his cross-examination of Mr Parker, Mr Beard KC made a number of points about the validity or appropriateness of the figures which Mr Parker used, and it is necessary to deal with these matters, even though they had not been foreshadowed in BT's Opening or in HJ1 or HJ2.
353. First, it was suggested that, of the 20% of SPCs who were split service i.e. they took both voice and broadband from BT, it was possible that if any of them had BT employee discounts, they may be paying substantially less. Mr Parker agreed but said that he had not seen any evidence about such discounts. This was because BT has not adduced any evidence on the point, which it could have done. It is correct that, in answer to a question from Mr Doran, Mr Bunt said that the split service group were a "strange group" with "strange behaviours"; and there were a lot of ex-employees there who previously had a landline paid for and received free broadband, but that is as far as the evidence went and we do not think it materially assists. It is worth pointing out that Mr Bunt went on to say that:
- "those [split service] customers were paying above average dual play prices when you added up the two components."
354. As for split supplier customers, and leaving aside particular points made, for example, about Sky, BT suggested that there was evidence to show that such SPCs in fact found it cheaper to be with split suppliers rather than go to bundles. Reference was made, first, to some evidence given by Mr Bunt in cross-examination. He said that there were many customers in this group whom Mr Bunt thought were getting incredibly good broadband deals, like free broadband or similar when they took Sky TV. So the reason they were not moving was because they already had the best possible deal i.e. free broadband. In reality, all he was talking about was Sky and this is dealt with separately below.
355. BT also referred to the results of the Ofcom NMR Residential Consumer Survey 2017, where the question asked was:
- "Q14. Why do you use (BROADBAND SUPPLIER) for your broadband service rather than using (LANDLINE SUPPLIER) for your broadband and your landline? Base: UK adults aged 16+ with a landline phone service using different providers for landline and fixed broadband (282)"
356. 45% of those surveyed said that the reason was "Deal/Price" while 43% said "Service quality/trusted". We see that, although this was a relatively small sample, it was (understandably)

not clear how far this cohort had looked into other deals and whether it extended beyond Sky, for example, offering free broadband where Sky TV was taken.

357. The next point concerns data from Sky itself. This issue arose because, in relation to the majority of SPCs who were split supplier rather than split service, Figure 7 only gave the example of one non-BT broadband supplier, namely TalkTalk. And in the case of Figure 8, the only example was Virgin Media. When asked why Sky prices for the supply of standalone broadband were not included, Mr Parker said that this was because Sky had not consented to the CR's request for disclosure of the data it had given to Ofcom for the purposes of the 2017 review. However, this was not a complete answer because in fact, the (publicly available) Ofcom materials revealed some of Sky's pricing. Mr Parker accepted that he could have used that dataset.
358. The information set out in Table 1.32 of Ofcom's Supporting Evidence shows that Sky's standalone broadband price was significantly less than TalkTalk's. For Q1 2017, the total SPC price using Sky broadband would be £34.15p, which was only £4 more than the blue diamond (lowest bundle list price), although this is still more than a 10% difference. But it would also be just less than the standard BT bundle list price of £34.99, shown in Ofcom's figures. In addition, Figure 8.43 in the Annex to the 2017 Provisional Conclusions shows that a total SPC price using Sky's standard broadband would be £31.99, whereas BT's standard bundle was actually more.
359. As for Figure 8, an SPC taking Sky superfast broadband would be paying £38.99. This is very much lower than the combined price which would be paid by an SPC using Virgin Media broadband which would be around £55. It would also be the same as the Sky bundle and less than BT's bundle for the slower speed of 17 Mb being £40.99.
360. BT's submission is that when Sky's pricing is factored in, the differential between SPC and bundle pricing becomes much less stark. To that end, BT's Closing Submissions contained reworked Figures 7 and 8 as follows:



361. The upshot of this is that the SPC price which uses the Sky broadband element is much closer to the DP list price than the other SPC prices. Precisely how or by whom these new figures have been calculated is not clear and the CR says that this is effectively new evidence which its experts have not had the opportunity to consider. Moreover, to the extent it is evidence, it could and should have been produced much earlier. We think that this is a reasonable objection.
362. In our view, the correct way to proceed here is to utilise the further tables which have been produced by Mr Parker to deal with the question of Sky and which form Tables 1 and 2 within the Annex to the CR's Closing. No objection was taken to these tables by BT. They show the following:

**Table 1      Relative prices (in % terms) paid by Split Purchase Customers for fixed voice and fixed standard broadband services compared to standard broadband Dual Play Customers, 2015 Q4 – 2018 Q2**

% saving from switching to...	Split Purchase (incl. BT broadband)		Split Purchase (incl. TalkTalk broadband)		Split Purchase (incl. Sky broadband)	
	Dual Play (list)	Dual Play (promo)	Dual Play (list)	Dual Play (promo)	Dual Play (list)	Dual Play (promo)
2015 Q4	63%	98%	40%	70%	-	-
2016 Q1	73%	133%	48%	99%	-	-
2016 Q2	55%	163%	33%	125%	-	-
2016 Q3	67%	120%	35%	78%	-	-
2016 Q4	68%	109%	36%	69%	■	■
2017 Q1	61%	176%	37%	134%	■	■
2017 Q2	68%	153%	37%	106%	-	-
2017 Q3	77%	101%	-	-	-	-
2017 Q4	74%	101%	-	-	-	-
2018 Q1	79%	109%	-	-	-	-
2018 Q2	74%	124%	-	-	-	-

Source: Frontier Economics based on data from: BT Consumer Price Guides for the period 2015 Q4 to 2018 Q2; TalkTalk's s135 data submission to Ofcom for the period 2015 Q4 to 2017 Q2; Ofcom's Annexes to the Provisional Conclusions and Evidence supporting the Statement (for data on the price of standalone standard broadband from Sky in 2016 Q4 and 2017 Q1 respectively); and Ofcom's Pricing Trends Communications Reports for 2019 and 2022.

**Table 2 Relative prices (in % terms) paid by Split Purchase Customers for fixed voice and fixed superfast broadband services compared to superfast broadband Dual Play Customers, 2015 Q4 – 2018 Q2**

% saving from switching to...	Split Purchase (incl. BT broadband)		Split Purchase (incl. VM broadband)		Split Purchase (incl. Sky broadband)	
	Dual Play (list)	Dual Play (promo)	Dual Play (list)	Dual Play (promo)	Dual Play (list)	Dual Play (promo)
2015 Q4	57%	105%	50%	97%	-	-
2016 Q1	64%	104%	58%	97%	-	-
2016 Q2	52%	109%	47%	101%	-	-
2016 Q3	57%	117%	49%	105%	-	-
2016 Q4	63%	88%	59%	84%	■	■
2017 Q1	56%	123%	53%	118%	-	-
2017 Q2	63%	123%	44%	97%	-	-
2017 Q3	62%	77%	52%	65%	-	-
2017 Q4	63%	80%	52%	68%	-	-
2018 Q1	67%	93%	50%	73%	-	-
2018 Q2	67%	98%	50%	78%	-	-

Source: Frontier Economics based on data from: BT Consumer Price Guides for the period 2015 Q4 to 2018 Q2; Virgin Media's broadband only web page for the period 2015 Q4 to 2018 Q2; Ofcom's Annexes to the Provisional Conclusions (for data on the price of standalone superfast broadband from Sky in 2016 Q4); and Ofcom's Pricing Trends Communications Reports for 2019 and 2022.

363. What these tables show is that there was a differential between SPC pricing and dual play bundle pricing for standard broadband of ■% and ■% where the comparator was list pricing and ■% and ■% where the comparator was promotional pricing. The differentials in relation to superfast broadband were ■% and ■%, respectively. Obviously, these were far more modest differentials than was shown in relation to the position of SPCs who used BT or TalkTalk as the broadband provider, but from a SSNIP point of view, they are still significant. Indeed, when Ofcom included Sky broadband pricing in its comparisons on a weighted average basis, it still found a monthly differential of £14.57 when compared with promotional pricing and £8.01 when compared with list bundle pricing.
364. Accordingly, we do not consider that the Sky data and its implications are fatal to Mr Parker's differential analysis here.

365. BT made a further, more general, point, questioning whether Mr Parker should have relied upon promotional bundle pricing. This was on the basis that list prices still applied to “back book” customers. Mr Parker disagreed on the basis that the bundle providers must have thought that the promotional prices were still remunerative. The CR also here relies upon the increasing prevalence of discounting in bundles, as observed by Ofcom in its 2016 Communications Market Report, where it stated that 94% of all dual play plans had some discount element in 2015. Dr Jenkins herself had also emphasised, in HJ1, that large promotional discounts on bundles were a key driver of strong price competition. This was in the context of suppliers like BT encouraging customers to take both services from a single supplier, and the role played by bundles in relation to SFV Services pricing—see paragraphs 5.40 - 5.42. The CR therefore submits that it is realistic to use promotional pricing as a relevant comparator.
366. We follow all of that, although, of course, back book pricing still remains, and the fact that 94% of dual play plans had some discount element does not mean that that 94% of customers benefited from such discounts. Ofcom’s 2020 report titled “Pricing Trends for Communications Services in the UK” noted, for example, that around half of all standard broadband customers were out of contract in 2019, which indicates that the discounted offers available on new deals are not representative of prices across the market. The same Report also showed that the price gap between list and promoted prices for standard dual play contracts fluctuated between £5 and £10 per month, on a typical promoted dual play price of around £20 per month. In that context, one might expect the lower margins earned through promotional pricing to be offset against the higher margins obtained on list prices, and it is not obvious that any one bundle supplier could sustain a viable operation by selling exclusively at promoted prices. Hence, whilst it is clearly reasonable to refer to promotional pricing, a proper assessment of market prices should include some consideration of both promotional and back book/out of contract price levels.
367. Allied to that general point was the suggestion that there was a mismatch in the comparison between SPC pricing and bundle pricing. On SPC pricing, Mr Parker simply took the average. But when it came to bundle pricing, he took the average of the lowest of the list, and promotional prices of each of the relevant suppliers. Mr Parker defended what he had done on the basis that the SPC prices he used reflected what the supplier could achieve in the market. That is true, but again the focus of his analysis on promoted prices when around half of all bundle customers pay list prices does present only a partial picture.
368. It was also suggested that Mr Parker’s analysis was defective because it did not take into account call charges. However, he expanded his analysis in DP5 to include calls. The overall differential result was, not affected. See paragraphs 3.6-3.3.13.

369. We should note here that even on the basis of a significant price gap between standalone and bundle prices, Dr Jenkins said that an absolute price difference between the focal product and the closest substitute cannot prove conclusive for the SSNIP test. Indeed, she argued that it is common for products within the same relevant market to have different price levels. This claim is clearly correct, but it is most relevant in cases where products are differentiated from one another. For split service (i.e. those who bought both voice and broadband from BT) SPCs, it is hard to see how any differentiation between the bundle and the standalone combination could justify a significant and sustained price gap. Where SPCs chose different providers for the two products, there is more scope for actual or perceived service quality differentiation to play some part, so there is some potential for this criticism to apply. However, this possibility does not render the CR's focus on significant and sustained price differentials invalid, and beyond the point of principle made here by Dr Jenkins, BT offered little evidence in this context to explain the differentials in quality terms.
370. A further point made by Dr Jenkins in the hot tub discussion was that the price differential might be explained by SPCs purchasing an SFV Service on the one hand and then broadband without voice, but coupled with another service like TV, on the other. She suggested that Virgin Media for example would do this. However, she produced no detailed evidence on this and Ofcom data showed that the vast majority of bundles included landline. For example, in 2017 only 7% of households overall were taking broadband and another non-voice service. Dr Jenkins suggested in cross-examination that this 7% could be SPCs but in truth, this was just speculation with no proper evidence behind it. So we do not think that this further point goes anywhere.
371. Having considered all of the matters above, we take the view that, notwithstanding the points made against his analysis, Mr Parker has established that there was a price differential between SPCs and dual play bundle pricing that exceeded the 5-10 per cent significance threshold that is normally used in the SSNIP test.

#### *Line Rental Price Increases*

##### Introduction

372. See Tables 1 and 2 from the CR's Opening which are based on Tables 13 and 14 in DP3:



Table 1: BT Standard Line Rental price increases pre-Commitments<sup>46</sup>

Date	Price Increase Name	BT SLR		
		Price	Change (£)	Change (%)
01/04/2009	Bordeaux	£12.50	£1.00	9%
01/10/2010	Pacific	£13.29	£0.50	4%
28/04/2011	Atlantic	£13.90	£0.30	2%
03/12/2011	White	£14.60	£0.70	5%
05/01/2013	Beech	£15.45	£0.85	6%
04/01/2014	Pegasus	£15.99	£0.54	3%
01/12/2014	Window	£16.99	£1.00	6%
20/09/2015	Laika	£17.99	£1.00	6%
03/07/2016	16/17 Price Change	£18.99	£1.00	6%

Table 2: BT Standard Line Rental price increases post-Commitments<sup>47</sup>

Date	Name	BT SLR (for SPCs)			BT SLR (for VOCs)		
		Price	Change (£)	Change (%)	Price	Change (£)	Change (%)
01/04/2018	Commitments Introduced	£18.99	£0.00	0%	£11.99	-£7.00	-37%
16/09/2018	18/19 Price Change	£19.99	£1.00	5%	£11.99	£0.00	0%
31/03/2020	Price Change 2020	£20.20	£0.21	1%	£12.14	£0.15	1%
31/03/2021	Price Change 2021	£21.10	£0.90	4%	£11.73	-£0.41	-3%
31/03/2022	Price Change 2022	£23.05	£1.95	9%	£11.73	£0.00	0%
31/03/2023	Price Change 2023	£26.35	£3.30	14%	£11.73	£0.00	0%

373. On the basis that most of these increases are 5% or more, Mr Parker says that the SSNIP has been passed by BT. In particular, the figures from the Tables shown under paragraph 372 above, yield the following:

- (1) VOCs: Between January 2009 and March 2018, while BT's main direct input cost (wholesale line rental) was declining, BT increased the price of standard line rental charged to VOCs by 65%, from £11.50 to £18.99;
- (2) SPCs: Between January 2009 and April 2023, BT increased the price of standard line rental charged to SPCs by 129%, from £11.50 to £26.35;
- (3) Many of the "routine" annual price increases that BT imposed for standard line rental were also individually above a SSNIP.

374. These figures, as figures, were not disputed by BT, nor could they be. However, Dr Jenkins made the following objections to this analysis:

- (1) The relevant period to consider is the claim period and not a period starting any earlier;
- (2) Line Rental is the incorrect metric; it should be ARPU.

### The Relevant Period

375. Dr Jenkins said that the period for considering the various price increases must be confined to the claim period. On that basis, there was only a 5.6% increase in total between 2015 and 2018 for VOCs. Of course, that is still more than 5%, but the key point is that there is no reason to restrict the period under consideration to the claim period. Here, in the period immediately before, BT was raising line rental prices frequently (see Table 1 under paragraph 372 above), and we have observed that in the pre-claim period BT substantially increased the gross profitability of its SFV Services from 35% to 65%. As a matter of general principle, a hypothetical monopoly supplier that imposed a unilateral 5-10% price increase above the competitive level in period 1 and then held that elevated price level constant in period 2 could not validly argue that its constant prices in period 2 meant that it could not sustain prices above the competitive level in that period. So we reject this objection.

### The Correct Metric

376. Dr Jenkins also says that Mr Parker has used an incorrect metric for this exercise, namely Line Rental. She says that the correct metric should be ARPU. But if so, then there is no overall increase at all – see the Tables at paragraphs 135 - 136 above. It is true that the experts did use ARPU as the proxy for price in the Limb 1 exercise. However, as we say below, that is a different exercise. Indeed, for the purpose of her actual loss calculations which form part of her CLA, Dr Jenkins herself uses line rental “because the line rental does not depend on usage patterns, so it would affect all customers the same and it is this change in price, which is most obvious to the customer.” We address this further in the discussion of Dr Jenkins’ CLA in paragraph 404 below.
377. To deal with Dr Jenkins’ objection to the use of line rental here, in the context of market definition, it is necessary to take stock of the purpose of the SSNIP test. The point is to try and ascertain customer reaction to a significant unilateral increase in price that entails an attempt by the hypothetical monopolist to exercise market power. This change is normally embodied in a 5-10% price increase, holding all other factors constant. However, in the case of SFV Services and Line Rental changes, we know from the flat ARPU patterns that other things were not constant, and indeed BT’s line rental increases served only to compensate for other factors, such as the fall in call volumes and the numerous changes that occurred in the way that calls were priced, that reduced revenues per user. The fact that other parameters of cost, revenue and volume changed simultaneously with BT’s changes in Standard Line Rental make this a more complex pattern, and undermines the simplicity of Mr Parker’s claim that each change in BT’s Line Rental prices simulated a series of discrete SSNIPs.
378. However, this criticism of Mr Parker’s Line Rental SSNIP argument does not deprive his analysis of all its value. As we have already noted, while SFV ARPU remained broadly flat over the period

from 2007 to the end of the claim period, the gap between ARPU and direct costs (i.e. gross margins) increased from around £8 to £15 per line in real terms between 2007 and 2015, representing an increase in percentage terms from around 32% to 63% - see paragraph 141 above. This elevation of gross margins to 63% during this pre-claim period seems best to show the increase in SFV profitability that occurred. This factor, rather than potentially incomplete comparisons of wholesale and line rental prices is a more persuasive basis for the CR's claim that BT successfully imposed a significant worsening of competitive terms on SFV customers over this period. Indeed, and as explored in the hot tub discussion on Day 28/92, effectively this ability of BT to increase gross margins can be seen as a form of SSNIP in fundamental terms. It can also be seen as BT being able to exercise a significant amount of price discrimination against SFV customers.

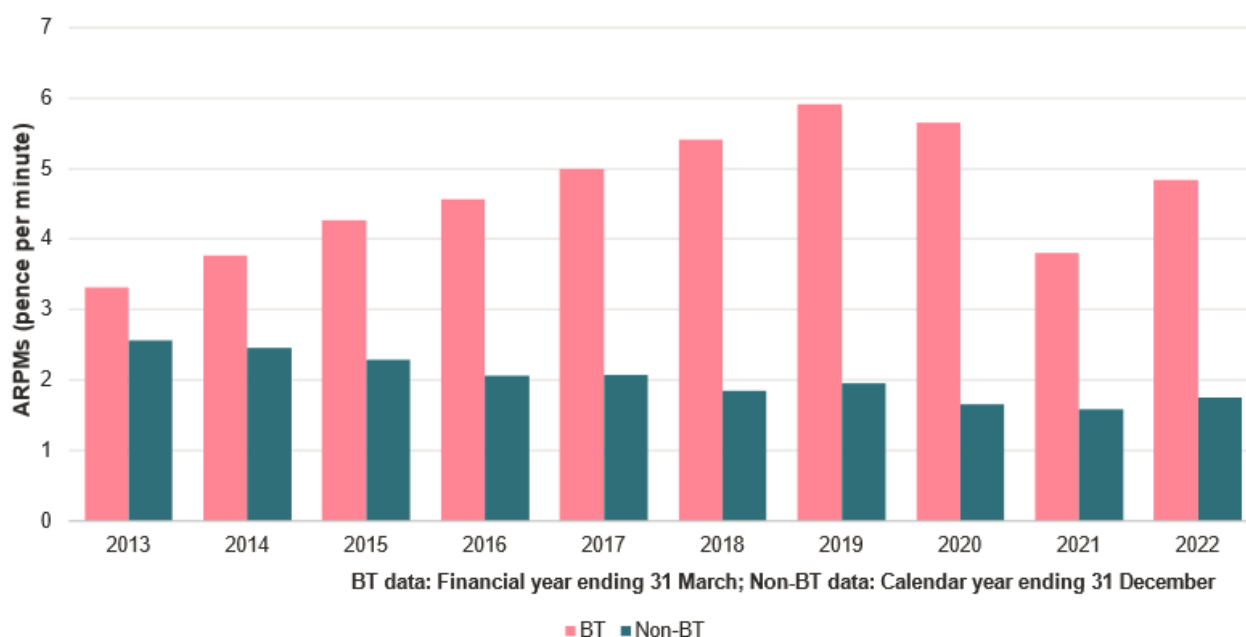
### Conclusion

379. Overall, we think that, while it is clearly inappropriate to focus on line rental price changes in isolation and therefore we do not accept Mr Parker's analysis of line rental price increases in its simplest form, there is significant force in Mr Parker's line rental increase analysis provided that we build into it the further points just made at paragraphs 377 - 378 above.

### *Call Price Increases*

380. The ARPMs relied upon by Mr Parker are set out in Chart 2 of the CR's Opening, as drawn from his Figure 1 in Annex A2 to the JES:

**Chart 2: BT's ARPM for calls made by BT and non-BT SFV Customers, 2013-2023**



381. According to this chart, BT's ARPM - a proxy for the average unit call prices paid by BT customers - has increased significantly over time. BT's ARPMs increased by 46% from 3.32p/minute to 4.84p/minute between 2013 and 2022. In contrast, ARPMs for other providers declined by 32% over the same period, from 2.56p/minute in 2013 to 1.75p/minute in 2022. As of 2022, BT's ARPMs were more than two and a half times higher than those of other providers. The CR therefore submits that, again, the size of the price increases suggests that the SSNIP test has been passed; this outcome therefore corroborates Mr Parker's earlier conclusions based on the differential between SPC pricing and bundle prices, and online rental price increases.

382. However, as we see it, there are two significant problems with this analysis.

383. First, there is a question as to whether ARPM is an appropriate proxy for pricing in this context at all. This is because of the existence of the various call packages offered by BT and its competitors. As Dr Jenkins pointed out at paragraph 4.46 of HJ2:

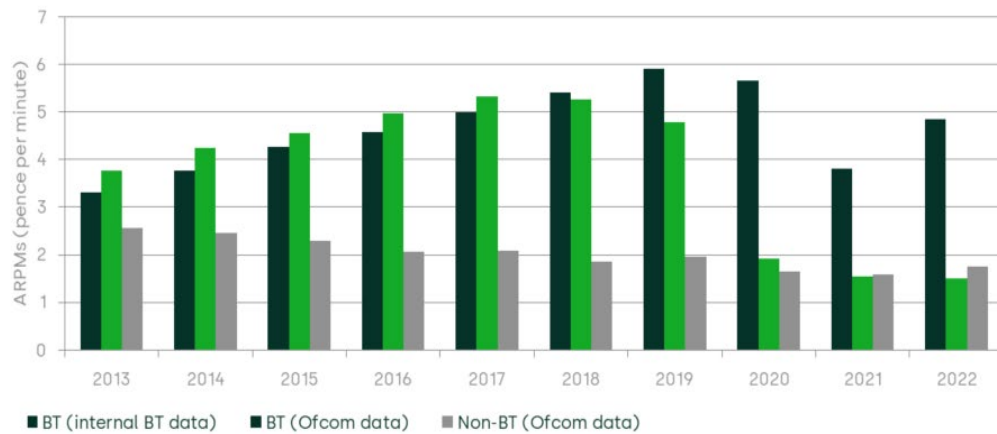
"The presence of call packages, which provides a set allowance of calls for a fixed price irrespective of the actual level of consumption within the inclusive allowance, means that an ARPM measure will provide a distorted view of the underlying average per minute call prices. By way of example, if all fixed voice customers of BT and its rivals purchased an unlimited call package at the same price, but BT's customers consumed fewer minutes than its rivals' customers, the ARPM measure would imply that BT was more expensive than its rivals, despite them charging the same price for the same package of calls."

384. Instead, it is more appropriate here to focus on the actual prices charged by BT and its rivals for call packages and out-of-plan calls. This is what Dr Jenkins did in her analysis at paragraph 7.73-7.77 of HJ2. These comparisons show that overall, BT's prices for call plans and out-of-plan calls were largely comparable with and sometimes exceeded by the prices of its comparators.

385. We think that Dr Jenkins' approach of using the actual charges rather than ARPM is more appropriate here. This conclusion is fortified substantially by the next point.

386. Second, it is now doubtful whether the ARPMs of BT and its rivals were compared on a like-for-like basis anyway. This emerged as a result of an analysis carried out by Dr Jenkins which included, as an extra column, Ofcom's data as to BT's ARPMs, as opposed to those generated by BT's own internal data. Figure 1, in Section B3b of the Annex to the JES shows as follows:

**Figure 1 ARPM for calls made by BT and non-BT customers (2013–2022)**



Note: The BT (Ofcom data) and Non-BT (Ofcom data) ARPMs are presented on a calendar year basis. The BT (internal BT data) ARPMs are presented on a financial year basis.

Source: Oxera analysis based on Parker 3 datapack, 'SDP – Calls Analysis – submission', Ofcom ARPMs and BT Internal ARPMs worksheets.

387. At paragraph 4.49 of HJ2, and in response to issues 6.3.1 and 6.3.4 in the JES, Dr Jenkins noted that the Ofcom-derived BT ARPMs were similar to its competitors' ARPMs for the period 2020-2022. The explanation for that result, as amplified in the letter from Simmons & Simmons ("S&S") dated 9 March 2024 and the note from Dr Jenkins attached ("the 9 March Letter") appears to be this: when BT reported its core revenue, it included the revenue derived from the sale of its call plans as well as from the per call charges obtained from calls made out-of-plan. The reallocation performed by Ofcom from 2020 onwards appears to have stripped out the call-plan revenue, not least because the figures used by Ofcom for BT's competitors' ARPMs were also "net" of call plan revenue, as it were. So, from 2020 onwards, the ARPMs of BT and its competitors were being compared on a direct basis. On that basis, BT's ARPMs were not significantly higher, and indeed was slightly lower for 2 years.
388. It would follow that if BT's call plan revenue was removed from its ARPMs for the previous years, the revenue would very significantly decrease as would, obviously, its ARPM.
389. The CR has objected to BT's reliance on the 9 March Letter on the basis that this amounted to new evidence and was inadmissible. We disagree. It made obvious sense to try and explain the discrepancy in the ARPM figures after 2020 and to understand how Ofcom's reallocation exercise was likely to have worked. The CR could have put in its own riposte to all of this, if he thought that the analysis was wrong, but he did not do so.
390. In the event, and for the reasons given above, we do not consider that Mr Parker's ARPM analysis in relation to call pricing can be safely relied upon in the context of market definition and the SSNIP test.

## Analysis: Dr Jenkins' Approach

### *Switching per se*

391. Dr Jenkins' first argument is that the phenomenon of switching itself suggests that bundles acted as a price constraint - see paragraphs 4.51 and 4.54 of HJ1. This is on the basis that voice-only customers who switch to bundles must regard the latter as close substitutes for the former and that in turn leads to the inference that (a) bundles represent a significant pricing constraint and (b) the relevant market is SFV Services and bundles together.
392. However, we fail to see how the existence of switching without more can entail these conclusions. Indeed, we have already concluded that the main reason for switching was not price-related. See paragraphs 216 - 303 above.
393. However, Dr Jenkins made a related argument which was that even if switching was not price-related, but could be driven by quality improvements this would still be relevant for market definition. In the hot tub discussion, she put it in this way on Day 9/125-126:
- “It is a meaningful competitive attribute, perhaps is a better way of putting it. That a SSNIP analysis or a hypothetical monopolist test, as we both agree, it is a framework of thought that is trying to capture changing -- worsening the competitive conditions, actually, is what the HMT does, and does it via increasing price. But that can be worsened in other ways, and the guidance does -- increasingly you see in the guidance given by competition authorities a recognition that, in thinking about substitution behaviour, it may not only be price that you want to take into account, it can be other features, and that is coming to the fore because we have, increasingly, products that have zero price. So when people are contemplating that, they go, well, does that mean, you know, there is never anything to monopolise? Well, we monopolise in a different way. I think that is just recognising that what is being offered and what you have to think about is not -- we economists are terrible at just saying, well, you can turn everything into a price, and that is why we do this as a shortcut, but it does not mean you ignore switching that is driven by these other competitive factors. It is relevant.”
394. We did not find this a particularly persuasive argument. The key point of the SSNIP test is to consider customer reaction to a small but significant increase in price, not some other criterion, and of course, Dr Jenkins accepts the value of such a test because her own CLA is, according to her, one manifestation of it. Yet further, in the context of discussing secular trend, Dr Jenkins accepted that if there was a secular trend it was, by definition, not related to price and had to be taken into account. As we have already noted, the fact that the SSNIP test focuses on price (and holding other things constant) does not mean that it assumes price is the only factor that drives consumer behaviour. But in the current context where the attraction of broadband access increases over time, it is particularly important for the SSNIP test to filter out the switching that would have arisen without a price change.
395. It is also worth noting that the switching into bundles for quality reasons adverted to by Dr Jenkins appeared to contradict the point she made in a different context when she rejected the idea that SPCs were in some way inert or disengaged. She said that they may be positively wishing to remain because there were some quality advantages in having two contracts rather than a bundle. When this question was put to her, she said as follows:

“Well, through this period, because what I am basing this on is the actual evidence of what was going on, so I mean, so we are framing it as a hypothetical monopolist but we are basing it on the switching that BT observed on its customer base. Now, it may be that it was serving some SFV customers with a Voice Only contract because they got a really great deal for TV and broadband from Sky. BT then introduces TV and sport and all of a sudden for that customer they go, oh, okay, now I would prefer to switch to BT for my bundle because I am going to get BT Sport, I can still get the Sky channels through my TV package and that makes sense to me now. That type of switching behaviour could be what is underpinning this.”

396. We did not find that especially convincing either.
397. Overall, therefore, we reject the notion that the mere existence of switching in the way in which it happened here, itself evidences a price-related phenomenon or a wider market.

#### *CLA*

##### The detail of Dr Jenkins' CLA

398. The critical loss is a way to identify how much switching away from a candidate product would need to occur in response to a SSNIP in order for that switching to provide an effective competitive constraint on the pricing of the hypothetical monopoly supplier. It is derived from a mathematical equation based on the firm's gross margin and a hypothetical increase in price of 5-10%.

399. The equation is this:

$$\text{critical loss} = \frac{\text{SSNIP}}{m + \text{SSNIP}}$$

where all the units are in percentages, the SSNIP percentage being the postulated price increase e.g. 5%, and  $m$  being the firm's gross margin prior to the increase. By way of example, if the SSNIP was 5% and the gross margin was 35%, the critical loss would be 12.5% of the original customer base. The higher the margin, the lower the critical loss percentage and vice-versa.

400. Having established the critical loss, it is then necessary to assess how much actual switching away from the candidate product occurred or would occur in response to observed price changes. The actual loss must be assessed, based on some kind of data concerning customer movement. The data could be from customer surveys, for example. In this case, the data set used by Dr Jenkins is based on the actual switching data for the SFV Service customers referred to above, but adjusted to take account of a number of non-price factors.
401. If the actual loss of customers exceeds the critical loss, it indicates that the SSNIP test has failed, because the HM firm is worse off, compared to the position without the price increase. Where the actual loss is equal to the critical loss, this is the breakeven point. The critical loss of customers is thus the maximum amount that the firm could afford to lose before the SSNIP becomes unprofitable.
402. The ultimate point is that if the actual loss exceeds the critical loss, it suggests that the fear of switching exerts an effective competitive constraint on pricing and therefore supports a wider

market. If the actual loss is less than the critical loss, it shows that the SSNIP is profitable and this supports the existence of a narrow market. See generally, paragraph 4.67-4.76 of HJ1.

403. In order to ascertain the critical loss at any moment in time, Dr Jenkins needs a gross margin of the HM. For this purpose, she takes BT's own gross margin. There is a detailed calculation of this in Annex 1 to HJ1, in which she extracts BT's relevant revenue and costs of sales. Once a particular price increase is chosen, for example, 5%, the critical loss in terms of percentage of customers can be calculated using the equation.
404. As against that, Dr Jenkins then determines the actual loss for that period. The foundational data for this is the actual loss of BT SFV customers over 6 particular periods. In relation to each period she calculates a price elasticity based on the number of customers lost over that period and BT's actual price increases. The price increases she uses are those of line rental then expressed as a proportion of ARPU. At footnote 119 to HJ1, she explains that she focuses on the headline changes to line rental as the numerator for her percentage price change in each period because the line rental does not depend on usage patterns, so it would affect all customers the same and it is this change in price, which is most obvious to the customer. The price elasticity calculation from which the actual loss is derived is complex (see paragraph 4.73 of HJ1, and paragraphs A1.47-A1.49 of Annex 1), but there is no need to go into the detail. This is first, because the CR's criticisms of her CLA model do not focus on this aspect of it, but also because at the end of the day, the actual loss figures are still derived from the actual observed switching data.
405. The results of Dr Jenkins' analysis are shown in Table 4.1 below. The comparison between the actual loss percentage and the critical loss percentage of customers is made over the 6 periods, running from January 2014 through to October 2020 and in each period, there has been an actual price rise by BT. These periods do not - and do not need to - coincide precisely with the claim period. This is because the point of the exercise is to determine the question of market definition rather than, for example, whether any price charged by BT within the claim period was excessive and if so, by how much.



**Table 4.1 CLA results**

Price Change #	1	2	3	4	5 <sup>2</sup>	6 <sup>2</sup>
1st month	Jan-14	Dec-14	Sep-15	Jul-16	Sep-18	Apr-20
Last month	Nov-14	Aug-15	Jun-16	Jun-17 <sup>1</sup>	Mar-20	Oct-20
# of months	10	8	9	11	19	7
<b>5% SSNIP</b>						
Actual loss	26.8%	13.2%	13.5%	15.1%	26.7%	26.7% <sup>3</sup>
Critical loss	8.4%	7.6%	7.3%	7.2%	7.2%	7.6%
Implication ("W" for wide; "N" for narrow)	W	W	W	W	W	W
<b>10% SSNIP</b>						
Actual loss	53.7%	26.3%	26.9%	30.2%	53.4%	53.4% <sup>3</sup>
Critical loss	15.6%	14.1%	13.5%	13.4%	13.5%	14.2%
Implication ("W" for wide; "N" for narrow)	W	W	W	W	W	W

406. The percentage actual loss figures shown in this Table were arrived at after making certain adjustments to the “gross” actual loss figures. First, Dr Jenkins excluded customers who in fact had switched to another SFV service provider, because if BT is here seen as the HM, there would not be such other SFV services available. See paragraph 4.90 of HJ1. As we know, the percentage of BT SFV Services customers who migrated to other SFV Service providers in the real world, as it were, was small. This is because most migrated to bundles. Second, Dr Jenkins excluded departures due to clearly non-price-related factors, such as bereavement or home-moving. For the purpose of making both of these adjustments, Dr Jenkins used BT’s cessation codes.
407. After making these deductions. Dr Jenkins arrives at what may be described as her primary figures for actual losses in the relevant periods.
408. However, Dr Jenkins then makes a further adjustment to cater for departures that may still be unrelated to price, and in particular due to the “secular trend”. She herself rejects the proposition that there is such a trend. But, in order to make her figures conservative, she reduces her primary figures by 20% to take account of this. See paragraphs 4.93 and 4.94 of HJ1.
409. The detailed calculations for all of this can be found in paragraphs A1.30-A1.59 of the Annex to HJ1. One relevant percentage is the number of customer departures excluded as a result of making the above adjustment expressed as a percentage of the total number of customer departures. This is 69.4% over the first four periods. See paragraph A1.43. She then uses that percentage exclusion for the SPCs in last two periods as well. See paragraph A1.44.
410. Dr Jenkins then expresses the actual customer cessations which are deemed responsive to price changes as a percentage of the customers at the beginning of the period and this will yield the

customer reduction in percentage terms. That percentage is then divided by the actual percentage change in price for the relevant period which will yield the price elasticity figure for that period. That price elasticity is then used to generate a percentage customer loss deemed due to price, by reference to the notional 5% and 10% SSNIP.

411. The figures which result are the ones shown in Table 4.1. See also Figure A1.2, and paragraphs A1.45-A1.47 in Annex 1.
412. On the basis of Table 4.1, the actual losses for each period where there was a notional 5% price increase clearly exceeded the critical loss. This yields the inference that there was a wider market consisting of (at least) SFV Services and bundles. The absolute differences are (obviously) even greater with a 10% increase.
413. What Dr Jenkins then does is to adjust her figures further by way of two “sensitivity checks” to the actual losses shown in Table 4.1.
414. One adjustment is to give greater credence to the secular trend argument by allowing 40% rather than 20% for it. The results of this allowance are shown in Table 4.2 at paragraph 4.100 of HJ1. As one would expect, the actual losses are now more modest, but they still are more than the critical losses, although in some cases, the difference between them is only a few percentage points.

**Table 4.2 CLA results: scenario with a low proportion of price related switchers**

Price Change #	1	2	3	4	5 <sup>2</sup>	6 <sup>2</sup>
1st month	Jan-14	Dec-14	Sep-15	Jul-16	Sep-18	Apr-20
Last month	Nov-14	Aug-15	Jun-16	Jun-17 <sup>1</sup>	Mar-20	Oct-20
# of months	10	8	9	11	19	7
<b>5% SSNIP</b>						
Actual loss	20.1%	9.9%	10.1%	11.3%	20.0%	20.0% <sup>3</sup>
Critical loss	8.4%	7.6%	7.3%	7.2%	7.2%	7.6%
Implication (“W” for wide; “N” for narrow)	W	W	W	W	W	W
<b>10% SSNIP</b>						
Actual loss	40.3%	19.8%	20.2%	22.6%	40.0%	40.0% <sup>3</sup>
Critical loss	15.6%	14.1%	13.5%	13.4%	13.5%	14.2%
Implication (“W” for wide; “N” for narrow)	W	W	W	W	W	W

415. Dr Jenkins then addresses the Cellophane Fallacy point. The Cellophane Fallacy will apply if the starting price was itself the product of market power, and of course that is the CR’s entire case here. BT, on the other hand, says that its prices were not excessive (or unfair) to begin with, so to adjust for the Cellophane Fallacy would be to assume the outcome of the dispute. We discuss that point

further below, but at this stage, the relevance of the Cellophane Fallacy is that Dr Jenkins has performed a further sensitivity check based upon it. What she does is to alter the starting price and margin to that of the HPS product. This is lower than the “normal” price and therefore BT’s gross margin on it is lower.

416. She uses the HPS price/margin because in his plea of unfairness (at paragraph 1.36 (B) of the Claim Form), the CR compares BT’s actual prices to those of HPS, thereby impliedly asserting that the HPS price was itself not unfair.
417. Using a lower gross margin base means that the critical loss figure will be higher than shown in Table 4.1. This means that there is a greater chance that actual losses will not exceed critical losses which would then suggest that the market is narrow. The results of that particular exercise are shown in Table 4.3. They are not that much different from Table 4.1 and the actual losses still exceed the critical losses.

**Table 4.3 CLA results: scenario based on Home Phone Saver ARPU as an alternative price path**

Price Change #	1	2	3	4	5 <sup>2</sup>	6 <sup>2</sup>
1st month	Jan-14	Dec-14	Sep-15	Jul-16	Sep-18	Apr-20
Last month	Nov-14	Aug-15	Jun-16	Jun-17 <sup>1</sup>	Mar-20	Oct-20
# of months	10	8	9	11	19	7
<b>5% SSNIP</b>						
Actual loss	26.8%	13.2%	13.5%	15.1%	26.7%	26.7% <sup>3</sup>
Critical loss	11.1%	8.4%	8.1%	7.8%	8.0%	7.9%
Implication (“W” for wide; “N” for narrow)	W	W	W	W	W	W
<b>10% SSNIP</b>						
Actual loss	53.7%	26.3%	26.9%	30.2%	53.4%	53.4% <sup>3</sup>
Critical loss	20.0%	15.5%	15.0%	14.5%	14.8%	14.7%
Implication (“W” for wide; “N” for narrow)	W	W	W	W	W	W

418. Finally, Dr Jenkins applies both of her sensitivity checks. The results are shown in Table 4.4. As one would expect, this shows the least difference between actual and critical losses, although, in each case, the former still exceed the latter. However, for Periods 2 and 3, the difference was only 1.5 and 2 percentage points.

**Table 4.4 CLA results: Low proportion of price-related switchers and CR's alternative price path**

Price Change #	1	2	3	4	5 <sup>2</sup>	6 <sup>2</sup>
1st month	Jan-14	Dec-14	Sep-15	Jul-16	Sep-18	Apr-20
Last month	Nov-14	Aug-15	Jun-16	Jun-17 <sup>1</sup>	Mar-20	Oct-20
# of months	10	8	9	11	19	7
<b>5% SSNIP</b>						
Actual loss	20.1%	9.9%	10.1%	11.3%	20.0%	20.0% <sup>3</sup>
Critical loss	11.1%	8.4%	8.1%	7.8%	8.0%	7.9%
Implication ("W" for wide; "N" for narrow)	W	W	W	W	W	W
<b>10% SSNIP</b>						
Actual loss	40.3%	19.8%	20.2%	22.6%	40.0%	40.0% <sup>3</sup>
Critical loss	20.0%	15.5%	15.0%	14.5%	14.8%	14.7%
Implication ("W" for wide; "N" for narrow)	W	W	W	W	W	W

419. In HJ2, Dr Jenkins ran two yet further sensitivities in the light of the fact that Mr Parker claimed that the sensitivity check for the Cellophane Fallacy was not enough because his view was that even the HPS price was excessive. What Dr Jenkins did was to run the two further sensitivities on the basis, not of the HPS price, but the Commitments price. The first sensitivity simply reruns the previous sensitivity check based on the HPS price. This is shown at Table A2 .1 of Annex 1 to HJ2. It shows that in all cases, actual losses still exceed critical loss.

**Table A2.1 CLA results: scenario using Mr Parker's suggested alternative price path**

Price Change #	1	2	3	4	5 <sup>2</sup>	6 <sup>2</sup>
1st month	Jan-14	Dec-14	Sep-15	Jul-16	Sep-18	Apr-20
Last month	Nov-14	Aug-15	Jun-16	Jun-17 <sup>1</sup>	Mar-20	Oct-20
# of months	10	8	9	11	19	7
<b>5% SSNIP</b>						
Actual loss	26.8%	13.2%	13.5%	15.1%	26.7%	26.7% <sup>3</sup>
Critical loss	12.2%	9.9%	9.0%	8.8%	9.3%	11.3%
Implication ("W" for wide; "N" for narrow)	W	W	W	W	W	W
<b>10% SSNIP</b>						
Actual loss	53.7%	26.3%	26.9%	30.2%	53.4%	53.4% <sup>3</sup>
Critical loss	21.7%	18.1%	16.5%	16.1%	16.9%	20.3%
Implication ("W" for wide; "N" for narrow)	W	W	W	W	W	W

420. The second sensitivity is to now combine the new Cellophane Fallacy adjustment with the prior sensitivity based on the 40% deduction for switching based on secular trend. This is shown in Table A2.2 of Annex 1 to HJ2, below. Even here, in all but one case, actual loss exceeds critical loss,

although by lower amounts. The exception is Period 2 on a 5% SSNIP where the actual loss is 9.9% and the critical loss is 9.9%.

**Table A2.2 CLA results: Low proportion of price related switchers and Mr Parker's suggested alternative price path**

Price Change #	1	2	3	4	5 <sup>2</sup>	6 <sup>2</sup>
1st month	Jan-14	Dec-14	Sep-15	Jul-16	Sep-18	Apr-20
Last month	Nov-14	Aug-15	Jun-16	Jun-17 <sup>1</sup>	Mar-20	Oct-20
# of months	10	8	9	11	19	7
<b>5% SSNIP</b>						
Actual loss	20.1%	9.9%	10.1%	11.3%	20.0%	20.0% <sup>3</sup>
Critical loss	12.2%	9.9%	9.0%	8.8%	9.3%	11.3%
Implication ("W" for wide; "N" for narrow)	W	N	W	W	W	W
<b>10% SSNIP</b>						
Actual loss	40.3%	19.8%	20.2%	22.6%	40.0%	40.0% <sup>3</sup>
Critical loss	21.7%	18.1%	16.5%	16.1%	16.9%	20.3%
Implication ("W" for wide; "N" for narrow)	W	W	W	W	W	W

421. Accordingly, Dr Jenkins maintains that even under these very conservative scenarios, the SSNIP test conducted under the CLA fails, and the market must be the wider one.

#### Analysis of the CLA

422. The CR makes a number of criticisms of the CLA so as to contend that it is fundamentally flawed.
423. The first is that Dr Jenkins' use of BT's gross margin data (as opposed to that of an HM) is incorrect, because she has thereby conflated the HM with BT, and ignored the incentive that BT has to charge higher SFV prices than the HM would, due to the recapture effect. This, of course, was the very same basis as the criticism that Dr Jenkins made of Mr Parker's market definition analysis. In fact, as we have observed above, it seems clear that BT does have some recapture incentive that one would expect to be priced in to its SFV price, and in the JES, Dr Jenkins accepted that as a multi-product firm BT is likely to set a higher SFV price than it would if it were an HM of SFV. She argued against the criticism that it would not have a significant effect on her findings because Mr Parker had denied that the recapture effect existed, but that is not a logical position to take. She also said that the allowances she already made to account for the Cellophane Fallacy problem would offset this concern to some extent and that the very large amount of observed switching away from SFV in any case gave her a large margin for error in the CLA calculations. None of these points in our view provides a convincing response to the issue.
424. That said, there is in any event the entirely separate criticism about Dr Jenkins' critical loss figures which relates to the Cellophane Fallacy. In this context, the Cellophane Fallacy problem has two

facets. First, the use of pricing (via gross margin) that may already be excessive, and second, Dr Jenkins' use throughout the CLA of switching rates which are themselves drawn from switching in relation to the actual prices charged and increased by BT over the relevant period. The first facet arises in the context of critical loss and the second in the context of actual loss.

425. As for the critical loss, Dr Jenkins seeks to cater for this by her first sensitivity which uses HPS pricing (see paragraphs 415-418 above) and then the lower pricing entailed by the Commitments (see paragraphs 419-420 above).

426. However, one cannot be certain that such adjustments address the Cellophane Fallacy sufficiently. The problem is that the existence of the Cellophane Fallacy just makes it very difficult to conduct a reliable SSNIP test which would show a wider market. The problem is compounded if one takes into account Dr Jenkins' recapture effect point – see paragraph 334 above.

427. As the Commission noted in *Slovak Telecom*

“158. In cases which are brought under Article 102 of the Treaty, the SSNIP test would need to be applied using the competitive price as a starting point for the measurement of margins and demand elasticities. A SSNIP test which starts from observed prices would tend to lead to market definition that is wider than what one would find if the SSNIP test was performed at the (lower) competitive price if, as it will be typical in cases brought under Article 102 of the Treaty, the observed price is already inflated relative to the competitive price. This is because margin and demand elasticity faced by the hypothetical monopolist would typically be lower at the competitive price than at the observed price. A SSNIP analysis starting from the correct competitive price would therefore tend to find narrower markets than the SSNIP analysis which (wrongly) starts from the (inflated) observed price. The fact that a SSNIP test analysis starting at an already inflated price will tend to lead to the wrong conclusion of wide relevant markets is called 'cellophane fallacy'. For this reason, the Commission does not normally rely on the SSNIP-test exercise in the context of cases which are based on Article 102 of the Treaty.”

428. However, even if an adjustment could be made for a notional, competitive price, as the starting point for critical loss, this would not itself cater for the second facet of the Cellophane Fallacy, which is that the switching rates (which yield the price elasticity to be used in computing actual loss) must also be those related to the competitive price. Yet that has not happened here, because, regardless of her adjustments, Dr Jenkins has used the switching rates (and hence price elasticities) based on BT's actual pricing. She accepted that her Cellophane Fallacy adjustment was only partial, and that she could not control how observed switching may have been different. (Indeed, it is almost certain to have been different, since demand elasticity will typically be lower at competitive prices - see paragraph 158 of *Slovak Telecom* referred to above). Dr Jenkins also accepted that she did not have good counterfactual data about switching.

429. It is true that Dr Jenkins sought to deal with this element of the Cellophane Fallacy by using the smallest observed price elasticity which emerged from the 6 periods, which was -2.63 in respect of the second period, and apply it throughout. However, the problem remains that this is still an elasticity based on a demand reaction to the prices actually charged by BT.

430. For those reasons, we do not think that the adjustments Dr Jenkins has made to her CLA to address the Cellophane Fallacy problem can be relied upon.
431. A second major criticism made by the CR is that even with a further 20% sensitivity to cater for customers whose switching was not price related, this does not mean that the CLA is underpinned by an accurate market data point on the extent of price-related switching here, as opposed to the effect of the secular trend.
432. Indeed, this is borne out by the fact that even using the lowest supposed price elasticity, on Dr Jenkins' primary figures at Table 4.1, BT's actual loss would be 13.2% and 26.3% at a 5% and 10% SSNIP, respectively. However, if this really was price-related, it is very hard to see why BT would have raised its prices at all over the 6 periods unless there was a very clear expectation that BT would gain bundle customers and profits when losing SFV customers. As we have noted above, there is in fact no contemporaneous support for the view that BT factored any migration intent into its SFV pricing decisions. It is true that on Dr Jenkins' most conservative scenario, under Table A2.2, there is either no gap or only a very small gap between actual and critical loss, so the previous point would not apply. But once one reaches that level and allows for some margin for error, the result is really that the SSNIP has now been passed.
433. Further, Mr Parker criticised the way in which Dr Jenkins had reached her assessment of price-based switching in the CLA, arguing that it contained no evidence that would identify the distinction between the secular trend and price-based switching. Even where Dr Jenkins had discounted large amounts of switching, there could be no assurance that her approach was conservative, since to make that assessment one would need to have a proper measure of actual SFV demand elasticity, holding other things constant. We substantially agree with this important criticism, noting that the (imperfect) evidence that does exist on actual demand elasticity does not support the existence of a high rate of price-based switching.
434. Finally, Mr Parker took issue with Dr Jenkins' "event study". This is dealt with at paragraphs 240 - 244 above. We concluded there that the consequences of the event study amount to important evidence to show that switching is not primarily related to price. It also ran against Dr Jenkins' CLA.
435. For all of those reasons, we consider that the CR's principal criticisms of the CLA are well-founded and we do not feel able to place any reliance upon it.

#### *Bundles as Constraints on SFV Pricing*

436. Here, it is necessary first to establish the underlying facts. It is clear that line rental increases were the same for SFV Services and bundles. So that part of the overall costs of each would be the same.

However, as Mr Bunt explained when dealing with the January 2021 document which set out the history of pricing, average bundle prices were falling, and so the broadband component of the total bundle price fell as well. Thus, even though line rental prices were going up, if the broadband component dropped sufficiently, the average price of the bundle would fall as a result. Later, in reply to questions from the Tribunal, Mr Bunt confirmed that, regardless of what customers saw, if one took the overall revenue from a bundle, there was (apart from line rental) another significant element to play with, namely the broadband charge.

437. Further, because of the way charges were shown on bills after the ASA Ruling in 2016, a bundle customer would only see the overall total charge. In that context, where a price increase of £2.50 was proposed for a bundle, that in fact included the line rental element of £1, and the rest, one could say, was attributable to the broadband charge. But in reality, there was one overall price to play with, as it were.

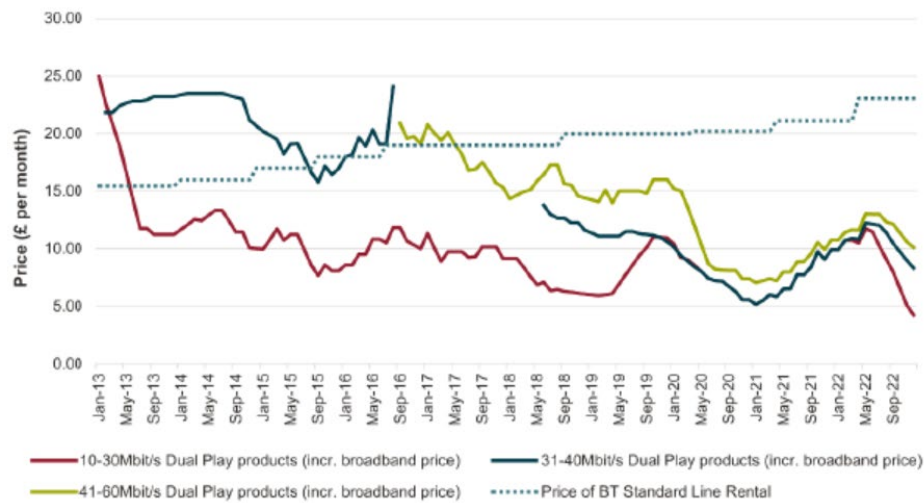
438. Dr Jenkins used the undisputed fact that BT's line rental prices (and increases therein) were applied as much to the voice element of bundles as to SFV Services to infer (at paragraph 4.45 of HJ1) that:

“On this basis, the competitive dynamics relating to the sale of fixed voice services as part of a bundle would therefore have been an important consideration with respect to the price that BT, or any provider, set for fixed voice services. Too high a price for fixed voice services could have led to an increase in the overall price BT charged for bundles including fixed voice services and lead to a reduction in the number of customers choosing BT for their fixed voice services supplied in a bundle.”

439. However, this assumes that any line rental price increase would automatically increase the overall bundle price by that amount i.e. that it is passed on in full. In fact, it need not be, as explained above, because there are other elements in the bundle price and in particular, BT could adjust the price of the broadband element of the bundle price (referred to as “the incremental broadband price”) to absorb some of the increase. Indeed, that this was the position is shown by Figure 1 from DP4 under paragraph 3.23:



**Figure 1** Changes in the price of BT fixed voice services compared to the price of incremental broadband sold as part of BT Dual Play bundles (six month-rolling average), January 2013 – December 2022

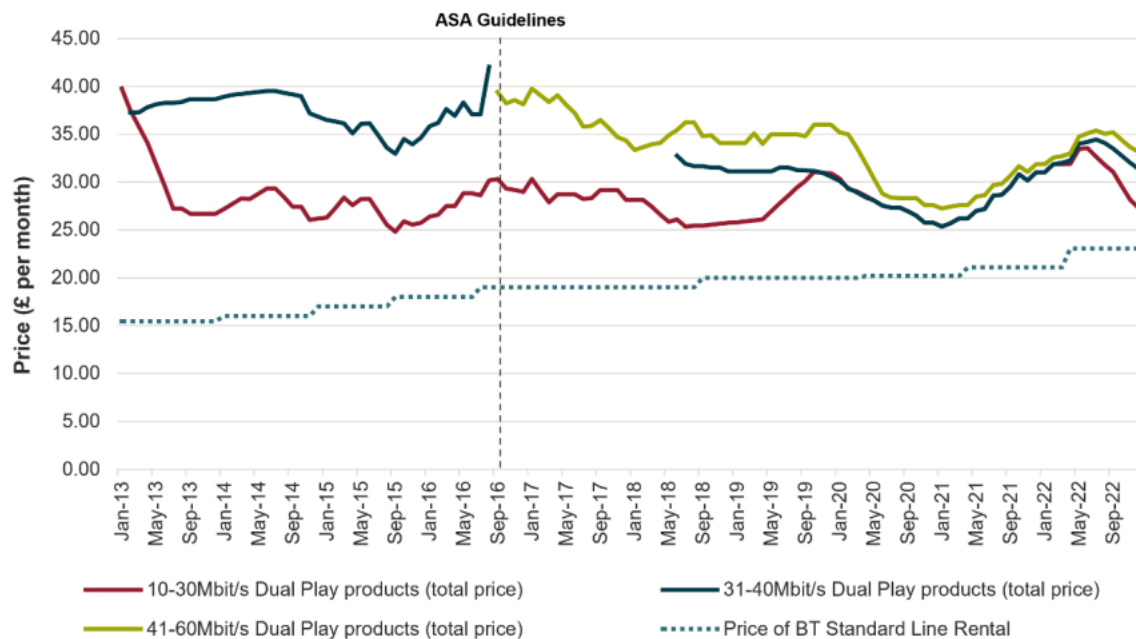


Source: Frontier Economics based on Dr Jenkins's analysis of the six-month rolling average monthly price of incremental broadband for different BT Dual Play bundles (see Dr Jenkins's Dominance – pricing R analysis, (Script '2. Tracking by Speed \_ Data Pack) and Dr Jenkins's analysis of BT's pricing of Standard Line Rental (see Dr Jenkins's CLA model – Excel, Sheet(Landline access prices). Data on the monthly price of incremental broadband for different BT Dual Play bundles is presented in Dr Jenkins's report in Figures 5.5, 5.6, and 5.7).

Note: Prices are reported inclusive of VAT. Gaps in the chart reflect periods where Dr Jenkins is unable to identify a product in that broadband speed category (see Jenkins 1, Figure 5.6, Figure 5.7).

440. The same point can be illustrated by the reference, not to the incremental broadband price within a bundle, but the overall bundle price. Figure 2 at paragraph 3.25 of DP4 shows this:

**Figure 2** Changes in the price of BT fixed voice services compared to the total price of BT Dual Play bundles (six month-rolling average), January 2013 – December 2022



Source: Frontier Economics based on Dr Jenkins's analysis of the six-month rolling average total monthly price of different BT Dual Play bundles (see Dr Jenkins's Dominance – pricing R analysis, (Script '2. Tracking by Speed \_ Data Pack) and Dr Jenkins's analysis of BT's pricing of Standard Line Rental (see Dr Jenkins's CLA model – Excel, Sheet(Landline access prices). Data on the total monthly price of different BT Dual Play bundles is presented in Dr Jenkins's report in Figures 5.12, 5.13, and 5.14).

Note: Prices are reported inclusive of VAT. Gaps in the chart reflect periods where Dr Jenkins is unable to identify a product in that broadband speed category (see Jenkins 1, Figure 5.13, Figure 5.14). {E/17/140-141}

441. In other words, there is not a direct correlation between any line rental increase and the price of the incremental broadband element or the price of the bundle as a whole.
442. This error on the part of Dr Jenkins has been referred to by the CR as the “bundle pricing fallacy”.
443. At paragraph 3.1.3 of the JES, Dr Jenkins suggests that she had never said that there was a direct link between the two. She said that:

“There is a link between the prices of SFV Services and fixed voice services sold in bundles, and this is relevant to the assessment of how competitive conditions facing fixed voice services sold in bundles had an impact on SFV pricing. For this competitive interlinkage to be relevant, I do not agree that it is a requirement for the total price of a bundle including fixed voice services to increase one for one with a change in the price of SFV services, nor did I ever state this as my view. Mr Parker’s statement that I have committed a ‘bundle pricing fallacy’ is itself fallacious. In terms of the pricing mechanics, the following linkages are necessarily present:

- a) The price of a bundle is necessarily bounded below by the price of SFV services.
- b) If the price of SFV services increases, then (taking the example of a dual play bundle) BT Consumer must either raise the price of the dual play bundle; lower the incremental price of broadband within a bundle or some mix of the two. Hence the two are inter-related....”

444. However, once Dr Jenkins has accepted (as she seems to do here) that there is no automatic linkage between line rental price increases and bundle prices, it simply cannot follow that the pricing of bundles needs to act as a constraint on SFV Prices at all.

445. In the hot tub discussion, in answer to a question from Mr Ridyard, Dr Jenkins said that the constraint on BT was not automatic; they may choose to pass on any part of the increase, but they do not automatically do so, and they have to think about the choice. However, we fail to see how that can properly be characterised as a constraint on SFV pricing by bundle pricing. Equally, when Dr Jenkins added that there was a sense in which narrowing the gap was part of the constraint from the bundle market, in the sense of wanting to structure those prices to be as attractive as possible for choosing BT, we fail to see how this has anything to do with the existence of a pricing constraint upon SFV pricing constituted by the bundles.
446. In this context, it is, finally, worth adding that both sides agreed (see paragraph 6.1.1 of the JES) that while SLR prices were increasing between 2013 and 2022, BT's overall prices for dual play bundles were generally stable or declining over the same period.
447. Accordingly, we do not accept that Dr Jenkins' points about bundles acting as a constraint on SFV pricing are correct and thus they do not assist BT and market definition.

### **Conclusion on Market Definition**

448. Having considered all of the evidence and arguments discussed above, we have concluded that SFV Services are indeed in a separate market. There is some competitive interaction between SFV and bundles, but not sufficient to reject the hypothesis that SFV Services form a separate market. The pricing of SFV Services is not effectively constrained by the threat that SFV consumers could switch to other products such as bundles. On that basis, it is necessary to move to the next issue which is whether BT was dominant in that market.

## **DOMINANCE**

### **The Law**

449. We did not understand the law in relation to the assessment of dominance to be in dispute. However, we have in any event set out the relevant principles below, drawn largely from paragraphs 224-228 of the CR's Closing, which we consider to be accurate.
450. The general position is as set out in *United Brands* as follows:

“[65] The dominant position referred to in this Article relates to a position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained on the relevant market by giving it the power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers.

[66] In general a dominant position derives from a combination of several factors which, taken separately, are not necessarily determinative.

[67] In order to find out whether USC is an undertaking in a dominant position on the relevant market it is necessary first of all to examine its structure and then the situation on the said market as far as competition is concerned.”

451. However, and as implied by the words “to an appreciable extent” in paragraph 65, it is not necessary to show that the undertaking has the power to behave independently of customers or competitors in all respects - see paragraph 134 of *Socrates v Law Society* [2017] CAT 10.
452. As for the question of market share specifically, this is an important indicator of market power and plays a central role in the assessment of dominance. See *Albion Water v Ofwat* [2006] CAT 36 at paragraphs 118 and 123. The possession of market share above 50% is *prima facie* evidence of a dominant position. See *Churchill Gowns v Ede & Ravenscroft* [2022] CAT 34 at paragraph 55. Indeed, in *AstraZeneca v Commission* Case [2013] 4 CMLR 7, the Court of Justice stated at paragraph 176:
- “The Court has already clarified that, although the importance of the market shares may vary from one market to another, the possession, over a long period, of a very large market share constitutes in itself, save in exceptional circumstances, proof of the existence of a dominant position (Hoffman-La Roche at [41]) and that market shares of more than 50 per cent constitute very large market shares (AKZO Chemie at [60]).”
- On any view, therefore, a market share of above 50% raises a presumption of dominance which needs to be rebutted.
453. As for other factors going to the question of dominance, these can include constraints from existing supplies from actual competitors and constraints from the credible threat of future expansion/entry – see paragraph 259 of *Hydrocortisone*.

### **Market Share**

454. The detail of BT’s market share of the SFV Services market is set out at paragraphs 116 - 117 above.
455. Given the size of those market shares, this gives rise to a presumption of dominance. Mr Parker’s view was that this was a strong indication of significant market power and at this level, the evidence required to show total absence of barriers to entry and expansion would need to be very strong to avoid dominance. In addition, and it naturally follows, that all of those market shares were very substantially higher than those of BT’s competitors.
456. BT’s market share did decline, but only very slowly over the relevant period. Its share for VOC declined by 2 percentage points per year and by 0.3 percentage points for SPCs. The converse is that its competitors did not significantly increase their respective market shares.
457. In evidence, Dr Jenkins sought to suggest that these high market shares were insufficient to show dominance, but her arguments here were essentially a re-run of her arguments in favour of a wider market on the issue of Market Definition.
458. So she said this at Day 11/93-94:

“But what is actually happening is a big chunk of the customers that are there as voice only customers in 2013/14 are actually responding to the competitive offers from the rivals in this market, so the TalkTalk, Virgin Media, Sky and BT itself, and their competitive activity is to actually change the product that they buy and

move out of this market that we are seeing here and move into another market as we defined it now. So that is a constraint on your behaviour in that market.

If your customers are constantly voting with their feet to go and do something different, then the fact that you may have —you have a large market, a large share of an ever declining market, can still be a sign that you are constrained in what you can do in that market as so defined, because it is not really meeting the underlying needs of those customers because they are basically shifting to something else.”

459. However, for the purposes of assessing dominance, we fail to see why the movement into bundles makes a difference. Equally, the fact that the market is declining does not mean that BT was not dominant in it over the relevant period.
460. Dr Jenkins also made a different point as to SPCs at Day 11/123, which was that where the market share here was almost 100%, that is a sign that the market was wrongly defined because it meant that there was a set of customers without any constraint upon them and they were rapidly declining during this period. Again, that is simply repeating the argument about market definition where we have already rejected BT’s claimed wider market.
461. Accordingly, thus far, we see no reason not to give the very high market share held by BT its full weight leading to a finding of dominance.

## **Other Factors going to Dominance**

### *Barriers to Expansion*

462. The CR contends that the fact of little movement in the overall market shares of BT on the one hand, and its competitors on the other, shows that there were significant barriers to expansion. In particular, competitors faced high acquisition costs to win over customers from BT. According to Mr Parker, this was because BT was a legacy provider that had in effect inherited a large proportion of its customers upon privatisation. Thus, for example, TalkTalk ceased to offer SFV Services to new customers in 2014. It told Ofcom in 2016 that there was no internal appetite for re-entering the market, even though the margins looked quite high because of the low number of customers who were likely to switch to TalkTalk and so the costs and complexity of pursuing this business were not justified. Reference was also made to customer inertia and the declining market. Indeed, TalkTalk exited the voice-only market altogether by the end of 2016.
463. Dr Jenkins disagreed, but again, her focus was the interaction between SFV and bundles. Thus, she said that supply-side barriers to entry were low and providers had an incentive to achieve economies of scope by encouraging customers to purchase bundles. We accept that the existence of very low barriers to entry from a neighbouring market could in principle counteract a presumption of dominance arising from a high market share, but that would be something that would need to be established rather than merely asserted. The evidence from TalkTalk (and indeed from Ofcom’s analysis of the market) indicates that there were real costs associated with entering the SFV market from the bundles market.

464. It is indeed the case that many SFV customers had been long-standing. Figure 8.54 of the 2017 Provisional Conclusions says that 77% of BT customers said they had been with BT for more than 10 years. This data was taken from Ofcom's Switching Tracker July-August 2016. On Dr Jenkins' figures, at least 78.5% of those who were still SFV customers in 2022 (a much reduced figure overall, of course) had been there in December 2014. This suggests that the figures on those who joined BT during the claim period (see paragraphs 169 - 171 above) may not be accurate, as already noted.
465. In the end, Dr Jenkins did accept in the hot tub discussion (Day 11/96) that there were at least some customer acquisition costs for a bundles provider which sought to supply voice only services.
466. The declining volumes of customers for voice services, noted as a reason by TalkTalk for not seeking new customers, is of some significance. This is not because this decline can be attributed to BT, but rather because it meant that there was a separate disincentive to enter into this market which would have enabled BT to maintain its dominant position.
467. There were therefore at least some barriers to expansion in respect of BT's competitors. That said, this was not because of high infrastructure costs (not least because Ofcom's regulation of Openreach and its WLR pricing) but rather because of the perceived difficulty of encouraging BT's customers away from it in a declining market. In this case, whilst such barriers are not overwhelming, they do provide a material degree of protection to BT's position as the leading supplier of SFV services, affording it some insulation from effective competition.

#### *The Position of the Post-Office*

468. The facts relating to the Post Office's pricing in comparison to BT's and that of other competitors over the period 2014-2021 is set out in the Table and Figure under paragraphs 131-132 above.
469. These show how the Post Office priced beneath BT and its competitors to a significant extent from 2014 to late 2016 and to a lesser extent from late 2016 until the first part of 2017. At that point it froze its line rental ("LR") prices until the Commitments took effect. It then dropped its price to 50p below the Commitments price until April 2020 when it raised its prices significantly and this remained the position until the Post Office sold off the business in 2021.
470. Dr Jenkins said that the Post-Office acted as a strong constraint upon BT. However, the threat posed by the Post Office did not stop BT from increasing LR prices, and between 2015 and 2017 the Post Office's market share rose only by 2 percentage points in terms of revenue and 3 percentage points in terms of lines. According to Ofcom, the Post Office gained only 1,700 customers per month from 2013-2017 which was less than 5% of the SFV customer losses suffered by BT over that period. It is true that the Post Office then undercut the LR price after the Commitments, but at this point the

SFV market that is of interest to us comprised only SPCs, and there is no evidence that the Post Office's offer was effective in competing for these customers.

471. BT pointed to the fact that the Post Office's share of VOCs increased from 13% in 2015 to 15% in 2016 and then to 16% in 2017. But these are still modest figures overall. BT also suggests that proof of the Post Office acting as a constraint is the fact of the introduction of HPS. However, while we accept that one aim of HPS was to address competition from the Post Office, that was not the whole story - see paragraphs 268 and 270 - 302 above.
472. As for the views of the Post Office itself, in a s135 response to the 2017 Provisional Conclusions, it said that its two latest campaigns to market to current BT customers had not succeeded. At a meeting with Ofcom in October 2016, it said that there were unlikely to be significant gains, and that view was proved correct, even though it did undertake further campaigns.
473. It is, of course, true that BT did, on occasion, refer in internal documents specifically to the question of churn to the Post Office. We have dealt with such documents at paragraphs 277 - 281 above. As those documents show, the predicted figures for churn to the Post Office do not seem always to be consistent with each other but in any event, it remains the case that overall, the Post Office did not make much of a dent in BT's overall position in the market.
474. In any event, the existence of some competition from the Post Office does not prevent a finding of dominance, because a dominance finding does not require that BT was able to act entirely without constraints; see paragraph 451 above.

#### *Constraints from Bundles*

475. BT relies upon the fact that it had to be mindful that fixed voice price increases might push SFV customers to a rival's bundle rather than its own. We see that, but of course it did not stop BT from increasing line rental prices. It was then said that to lower the price might then increase the cost of the "step" from an SFV Service to a bundle. BT said that the answer could not then be to reduce the price of the bundles as well, because of the very large drop in revenue which this would entail, and the bundle price was already set at the competitive level.
476. However, while considerations of that kind might show that the situation facing BT was a complex one, we still do not see how, for the purposes of assessing dominance, this means that there was an effective constraint, just as bundles did not act as an effective constraint for the purpose of market definition; see paragraphs 436 - 447 above.

### *Price Leadership*

477. Both Mr Parker and Dr Jenkins accepted that in principle, the existence of price leadership can be a factor tending to show dominance. The discussion of price leadership was confined to the tendency for BT to announce line rental price changes and for other retailers (except the Post Office) to follow.
478. We have established three important points that set the background to the assessment of price leadership. First, that in implementing successive line rental price increases, BT considered the risk of losing customers (described as “churn” in BT’s documents) but made the assessment that the revenue-increasing aspects of each line rental price increase would outweigh the losses to revenue caused by any such churn. Second, that although the line rental price increases took place against falling or static wholesale line rental costs paid by BT to Openreach, BT’s line rental increases were almost entirely offset by other changes that took place in call volumes and prices such that the ARPU for SFV customers was broadly flat from 2007 until the end of the claim period. Third, that this neutral ARPU result masks a substantial increase in SFV profitability (as measured by BT’s gross margin) which increased from 30% to more than 60% in the years prior to the claim period and was maintained at that level thereafter.
479. These established facts are all relevant to evaluating BT’s market power over SFV customers. The question now is whether any aspects of price leadership by BT in the SFV market add to that picture. Its ability to do so must rest on some tendency for rival suppliers to follow BT’s market lead in a way that made market outcomes less competitive than they would be under BT’s purely unilateral conduct.
480. At a purely factual level, the extent to which BT’s line rental price changes were followed by rivals is reasonably clear. If one returns to the Table and Figure produced under paragraphs 131-132 above, one can see how close the line rental pricing of BT’s competitors (other than the Post Office) was to its own pricing. They also show how BT’s line rental price increases tended to precede those of the others. It can also be seen from the first tab of the pricing spreadsheet annexed to BT’s written closing submissions, itself drawn from Figures 7.5-7.8 of HJ1.
481. As far as the post-Commitments period is concerned, there is not the same price leadership, since the Class now consisted only of SPCs, and Mr Parker accepted that BT did not act as a price leader in this period. However, this is the point at which BT’s market share is at its highest.
482. As to all of that, BT’s first point is that its price leadership (if that is what it was) was confined to line rental; it could not be said to be a price leader on call charges. We accept this, and it is noteworthy that the position with respect to call charges is complex and does not yield any clear picture as to the competitive positions of rival operators.



483. BT says that all of this is connected with the notion that the most effective way to compete for customers now was to put line rental prices up so as to drive them into bundles. However, that is really just a reflection of the “migration intent” point which we have rejected (see paragraphs 294 - 303 above). Equally, that question is not affected by BT’s motivation in increasing line rental prices, for example, whether it was deliberately targeting SFV customers or because it needed to meet revenue targets in any event.
484. It is also worth noting BT’s own view of the position.
485. Thus, in the Project Robin 2014/2015 Pricing document dated 29 November 2013, it stated:
- “Medium risk plan delivers £76m
  - 7% is PR recommended ceiling on price changes
  - Line rental at £16.99 will make us £1 clear of nearest competitor; however, competitors have historically followed us...”
486. As to that, Mr Bunt accepted that this showed that BT expected that its competitors would continue to follow it. However, this expectation applies to the line rental price changes that BT actually chose to implement, and which did not lead to any increase in SFV ARPU. It does not mean that rivals would have followed any conceivable line rental price increase that BT might have chosen to implement. Moreover, to the extent that BT chose not to implement some of the higher line rental price changes that it considered due to concerns about increased churn (though we have noted that these churn concerns were not the only consideration) the evidence is silent on whether that increased churn would have arisen because some or all rivals might not have followed these changes had they occurred.
487. There is then the 2015/2016 Pricing Plan document from 12 December 2014 which we referred to at paragraph 188 above. Here, Mr Bunt agreed that he was saying that this price change created significant headroom for BT’s competitors to do the same, i.e. price up to BT.
488. Further, in Mr Bunt’s Annual Price Change document dated 11 June 2015, ahead of the 2015/16 price change which would increase line rental by £1, he said this:
- “Each year BT changes its prices. Historically this has been approximately inflationary, but increasingly super-inflationary price rises on largely inelastic products has provided significant upside for our business. This capital provides the oxygen for our business in the sense of its investment in content, spectrum etc. These changes are reported to different degrees in the media, usually defined by our transparency and clarity as well as how compelling our gives are. Reporting of these changes very much drives our thinking on timing (we try to only go once a year) and scale (we choose 6.94% because this is less than 7% which is associated with negative energy company price rises)... Our competitors have increasingly aligned their price changes with our in timing and scale:...”
489. In relation to the last sentence, Mr Bunt accepted that the increasing alignment of BT’s competitors was a trend which he was seeing and it would not have been a surprise if they continued to follow BT.

490. Finally, there is the Consumer Voice Strategy document from 10 March 2015. This is noted at Slide 2 that BT's price change "leads the market enabling increases of the same scale". When asked about this as an indication of price leadership, Mr Bunt said that he did not really know what a price leader was, but certainly this sentence was acknowledging price leadership. See Day 6/31-48.
491. There is a separate point as to whether BT misled Ofcom in its Response on the question of price leadership. We deal with this below at paragraphs 1215 - 1217 below.
492. Taking all these considerations into account, we do not consider that descriptions of BT as a price leader add anything to the assessment of dominance that are not already included in the findings we have already made about BT's SFV pricing and margins. It is evident that most of BT's rivals followed BT's line rental price increases in the relevant period, but line rental is only one component of SFV pricing (just as is it only one component of bundle pricing, where no dominance or price leadership concerns have been raised by the CR). Further, we cannot assess whether rivals' decisions to adopt similar line rental price increases allowed them to earn excessively high prices or profits on their SFV customers, since there are strong indications that rivals faced higher costs than BT in this market. The fact that one of the main competitors, TalkTalk, had chosen not actively to pursue SFV customers, even prior to the Commitments, does not suggest that this was a market segment that provided high returns.
493. The most that can be said is that BT cannot legitimately point to the similarity of line rental prices across the SFV market as a positive argument against its ability to operate independently of the competition, but that does not take matters very far.

### **Conclusion on Dominance**

494. On the basis of all of the above, it is plain that BT had a dominant position in the market for SFV Services at all material times in the claim period. The very size of its market share entails that result and the other factors referred to above either support, or do not displace, that conclusion.
495. This means that it is now necessary to see whether its pricing was excessive, under Limb 1.

## **LIMB 1 METHODOLOGIES: DESCRIPTION**

### **Introduction**

496. The parties have each used very different methodologies to ascertain what they say is the relevant competitive benchmark against which BT's prices must be judged. The outcomes of these methodologies are also radically different. For example, according to the model employed by Mr Duckworth, the price for 2015/2016 clearly exceeded the competitive benchmark and across the 3 different line rental products, by a weighted average of 82%, and in the case of the main product, Standard Line Rental, by 74%.

497. A summary of Mr Duckworth’s outcomes can be found in the Limb 1 spreadsheet provided by the CR on 22 March 2024 (“the CR Spreadsheet”). We reproduce below the figures for SLR and the weighted average for all three line rental products:

Difference between Benchmarks and Charges on Standard Line Rental:

	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
SLR SFV Services benchmark (£ per line)	144.22	148.13	149.91	151.35	149.46	148.53	156.69
SLR SFV Services ARPU (£ per line)	250.85	275.00	284.37	270.49	270.29	261.60	250.15
Difference, above benchmark	74%	86%	90%	79%	81%	76%	60%

Weighted Average (WA) of three product-specific benchmarks:

	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
WA SFV Services benchmark (£ per line)	144.45	148.33	150.16	151.81	149.96	148.92	157.06
WA ARPU (£ per line)	262.38	285.58	295.03	278.72	279.44	272.08	263.44
Difference, above benchmark	82%	93%	96%	84%	86%	83%	68%

498. The competitive benchmark used is broken down as follows:

Standard Line Rental:

	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
SLR direct costs (£ per line)	96.53	99.15	99.90	100.45	98.41	97.01	101.01
Indirect costs (£ per line)	34.80	35.74	36.61	37.37	37.69	38.24	41.68
SLR total costs (£ per line)	131.33	134.89	136.51	137.83	136.10	135.26	142.69
SLR net margin (£)	12.89	13.24	13.39	13.52	13.35	13.27	14.00
SLR SFV Services benchmark (£ per line)	144.22	148.13	149.91	151.35	149.46	148.53	156.69

Weighted Average (WA) of three product-specific benchmarks

	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
SFV average direct costs (£ per line)	96.74	99.34	100.13	100.87	98.88	97.37	101.35
Indirect costs (£ per line)	34.80	35.74	36.61	37.37	37.69	38.24	41.68
WA total costs (£ per line)	131.55	135.08	136.74	138.25	136.56	135.62	143.03
WA net margin (£)	12.91	13.25	13.42	13.56	13.40	13.31	14.03
WA SFV Services benchmark (£ per line)	144.45	148.33	150.16	151.81	149.96	148.92	157.06

499. It can be seen that, taking 2015/2016 as an example, and on the basis of SLR, the annual price of £250 was some £105 more than the cost benchmark of £145 (using rounded figures).

500. By contrast, the outcome of Dr Jenkins’ “baseline” case is that, for every relevant year, the price was actually less than the competitive benchmark, so that no question of any excess could possibly

arise. See the summary of monthly prices in the Output tab of the spreadsheet provided by BT on 18 March 2024 (“the BT Spreadsheet”) reproduced in short form below.

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
<u>Using SAC Combi, 25% margin, and baseline common costs:</u>	23.32	26.13	28.47	28.64	33.11	35.24	35.61
<u>SFV Services ARPU:</u>	21.86	23.80	24.59	23.23	23.29	22.67	21.95

501. If, by way of example, the monthly figures for 2015/2016 are converted into annual figures, they become £279.84 for the benchmark and the lesser sum of £262.32 for the price.
502. It will be noted that the monthly figures for the benchmark and price used by Dr Jenkins’ BT Spreadsheet, as set out above, differ slightly from those used at Figure 6.10 of HJ1 (shown at paragraph 551 below). There are two reasons for this. First, the competitive benchmark has changed slightly because BT has now agreed the direct costs figures used by Mr Duckworth. Second, and in relation to ARPU, the economic experts later agreed that the ARPUs used should exclude BT employees, which has the effect of slightly reducing the monthly ARPU.
503. It is common ground that any proposed competitive benchmark must consist of the following elements:
- (1) Direct costs;
  - (2) Indirect costs; and
  - (3) A reasonable profit margin.
504. It is also agreed that indirect costs consist of two elements. The first element consists of indirect incremental costs. The second is concerned with common costs. Dr Jenkins has defined these terms in Table 6.1 of HJ1. A shortened version of those definitions follows:
- “Direct costs: Costs that can be directly and exclusively attributed to the particular service in question (e.g. cost of network access).  
Indirect costs: Costs that support the provision of multiple services and are not exclusively attributable to one particular service only (e.g. marketing costs, IT costs and other overheads).  
Incremental costs: Costs directly caused by producing a specified additional product, service or increment of output over a specified time period. The incremental costs of a service can be estimated as the difference between the total costs of a firm in a scenario where the service is provided and the total costs in another situation where the service is not provided. In other words, they are the costs that would be avoided in the long run if a given service is no longer produced.  
Common costs: Costs which arise from the provision of a group of services but which are not incremental to the provision of any individual service, as they are not directly caused by any individual service.”
505. It should be added that both direct and indirect costs can be either incremental costs or common costs.

506. We did not understand Mr Parker or Mr Duckworth to disagree with the above. The descriptions given by Mr Duckworth at paragraph 3.6 and 3.8 of MD1, on the key aspects of these terms, seem to us to be the same.
507. In this case, the relevant agreed direct costs consist principally of the WLR charges paid by BT to Openreach. BT said that, in its case, these direct costs were entirely incremental to the provision of voice services, but that different arrangements applied to the wholesale products purchased by other retailers. The agreed figures are now reproduced in the Direct Costs table of the CR's Spreadsheet as follows:

	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
SLR direct costs (£ per line)	96.53	99.15	99.90	100.45	98.41	97.01	101.01
LRP direct costs (£ per line)	96.87	99.26	100.13	101.31	99.46	97.98	102.54
LRS direct costs (£ per line)	99.21	103.62	105.04	106.72	105.92	105.73	105.57
SFV average direct costs (£ per line)	96.74	99.34	100.13	100.87	98.88	97.37	101.35

508. So, by way of example, for 2015/2016 and on an annual basis, the direct costs of providing SLR were £96.53 or £96.74 on average SLR costs. The latter yields a monthly figure of £8.06.
509. As for indirect costs, for the reasons given below, Mr Duckworth's methodology did not distinguish between the incremental costs and common costs elements of indirect costs. Dr Jenkins' methodology did. To use 2015/2016 again as an example, Mr Duckworth's model included £34.80 as the total indirect costs figure on an annual basis. By comparison, Dr Jenkins' total indirect costs figure came to £113.51, so over 3 times as much as Mr Duckworth's. That figure of £113.51 was split into £21.17 for incremental costs and £92.34 for common costs. This would yield monthly figures of £1.76 for incremental costs and £7.69 for common costs.
510. The final element is the reasonable profit margin. This is considered to form a part of the economic cost of supply, since any sustainable competitive price must include sufficient reward to investors to justify the allocation of their assets to the activity in question. The CR's case is that such a margin would be no more than 8.9% on a return on sales (i.e. profit divided by revenue) basis. In those circumstances, Mr Duckworth accepted that one could take the maximum reasonable margin on the CR's case as being 10%. For her part, Dr Jenkins says that a reasonable margin would be 25%, with 20% as a conservative fallback.
511. Table 5.1 of HJ2 (an updated version of Table 6.11 of HJ1) sets out a comparison between Mr Duckworth's and Dr Jenkins' results using annual figures (some of the inputs like direct costs are

slightly different because of agreement over direct costs but the differences are immaterial for these comparative purposes):

**Table 5.1 Comparison between Mr Duckworth's and my 'cost plus' benchmark for SFV Services (£/line/year, excluding VAT)**

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21 <sup>1</sup>	2021/22 <sup>1</sup>
<b>(A) Cost of Sales per line</b>							
Mr Duckworth	96.68	99.22	99.96	100.52	98.36	96.70	100.49
Dr Jenkins	92.05	99.22	100.16	100.52	98.36	96.70	100.50
<b>(B) Relevant Indirect (SG&amp;A and D&amp;A) costs per line</b>							
Mr Duckworth	34.80	35.74	36.61	37.37	37.69	38.24	41.68
Dr Jenkins	113.51	133.60	153.02	151.08	191.94	212.68	212.88
Of which:							
Incremental SG&A and D&A	21.17	20.30	21.21	22.23	22.69	23.31	24.96
Contribution to common costs	92.34	113.30	131.80	128.85	169.25	189.38	187.92
<b>(C) Total costs per line (A + B)</b>							
Mr Duckworth	131.48	134.96	136.57	137.90	136.05	134.95	142.17
Dr Jenkins	205.56	232.82	253.17	251.60	290.30	309.39	313.38
<b>(D) EBIT margin per line</b>							
Mr Duckworth (8.9%)	12.90	13.24	13.40	13.53	13.35	13.24	13.95
Dr Jenkins (25%)	68.52	77.61	84.39	83.87	96.77	103.13	104.46
<b>(E) "Cost plus" benchmark (C + D)</b>							
Mr Duckworth	144.38	148.21	149.97	151.43	149.40	148.19	156.12
Dr Jenkins	274.08	310.43	337.56	335.47	387.07	412.52	417.84

## Mr Duckworth's Methodology

512. Mr Duckworth's starting point is that what is needed, to reach the competitive benchmark (excluding the reasonable margin element), is the "LRIC+" of the SFV Services. "LRIC" are "long run incremental costs", which comprise all incremental costs, whether direct or indirect, which would be avoided if the product in question was not, or was no longer, supplied. The "+" denoted a further costs element which is not itself incremental. This comprises such proportion of the common costs of the product in question and other products, as is to be borne by the product in question. Since, by definition, common costs cannot be attributed to any particular product, the amount of such costs to be borne by the product in question cannot be determined with the same degree of certainty as the other costs. This, according to Mr Duckworth, is the appropriate starting point, since it gives effect to the "costs plus" determination required under the case-law. We should interpose here to add that Dr Jenkins, while also seeking to establish the competitive benchmark, says that the

LRIC+ approach, in this particular context, is inapposite, because it does not take account of the demand and supply side interrelationships between SFV Services and other products and is therefore insufficiently flexible (see JES 7.1.1).

513. As already noted, the Communications Act 2003 gave Ofcom the power to declare that a given telecoms operator has significant market power in a particular market. Where it did so, it could impose “ex ante” remedies. These included caps on charges. BT was designated as having SMP in 8 separate residential retail fixed voice service markets. From 2003-2006, Ofcom imposed price caps upon it. Another available remedy was a requirement for the body concerned to produce cost accounting statements to ensure that its obligations to customers were being met. This requirement was imposed on BT which had to produce annual Regulated Financial Statements (“RFS”) between 2005 and 2009. The RFSs included:

- (1) Primary Accounting Documents (“PAD”) which explained the principles applied in formulating the RFS;
- (2) Secondary Accounting Documents (“SAD”) which, among other things, set out how costs and revenues were attributed to particular services; and
- (3) Current Cost Financial Statements; these included the published cost accounting information and a statement from Ofcom, a Statement of Responsibility from BT, and an auditor’s opinion. For 2009, the latter was provided by PricewaterhouseCoopers LLP (“PWC”).

514. The Current Cost Financial Statements in question (“the CCFS”) contained an opinion that they had been prepared in accordance with the PAD and the SAD.

515. Section 1 of the PAD sets out a number of relevant principles which govern the formulation of the CCFS. The following are material here:

“Principle 3 - Cost Causality

Revenue (including appropriate transfer charges), costs (including appropriate transfer charges), assets and liabilities shall be attributed to network components, wholesale services and retail products in accordance with the activities which cause the revenues to be earned or costs to be incurred or the assets to be acquired or liabilities to be incurred.

Where it is not possible to attribute revenues, costs, assets and liabilities in accordance with the preceding paragraph, the attribution shall be such as to present fairly the revenues, costs, assets and liabilities accounted for in the Regulatory Financial Statement for each SMP Market or Technical Area (as applicable), as disaggregated, where BT has a regulatory financial reporting obligation and to present fairly a comparison between the Markets or Technical Areas (as applicable) as disaggregated.

Principle 4 - Objectivity

The attribution shall be objective and not intended to benefit either BT or any other Operator, or any product, service or network component.

Principle 5 - Consistency of Treatment

There shall be consistency of treatment from year to year. Where there are material changes to the Regulatory Accounting Principles, the Attribution Methods, or the Accounting Policies that have a material effect on the information reported in the Regulatory Financial Statements of a Market or Technical Area (as applicable), BT shall restate the parts of the previous year’s Regulatory Financial Statements affected by the changes.”

516. As Mr Duckworth states in paragraph 5.69 of MD1, the first part of Principle 3 implies that where possible, costs are attributed on a causal basis so as to arrive at genuinely incremental costs. For non-incremental costs, which would include genuinely common costs, they were to be attributed on a “fair” basis. The PAD does not give any further detail as to what the “fair basis” entailed.
517. Section 2 of the PAD then sets out how those principles are applied, although even here, the description is at a fairly high level with much more detail coming later (bullet format omitted):

## “2. Attribution Methods

### 2.1 Introduction

The Regulatory Financial Statements is produced using the Accounting Separation (AS) system. The principal objectives of the AS system is:

To provide a high quality mechanism for the production of Regulatory Financial Statements

To provide the foundation for the derivation of LRIC Statement of Costs.

To provide visibility of cost attributions.

To demonstrate that the costs incurred in providing services and products in downstream Markets include charges equivalent to those paid by other operators and service providers for services supplied from upstream Markets.

That it should be an integrated platform for the production of all BT’s regulatory and internal product reporting requirements.

The fundamental feature of the approach applied to attribution is adherence to the principle of causality. Each item of income, cost and capital employed recorded in BT Group’s accounts is attributed to the products, services and components which make up the separate Markets in which BT operates.

Attribution methodologies are regularly reviewed and enhancements introduced to reflect, for example, changing technologies while the apportionment bases, which are the practical application of these methods to actual values, are updated at least annually. A BT process has been established to validate all attribution methods to achieve objective bases.

Each item of income, cost and capital employed is attributed to a “cost centre” according to the way in which the activity, element of plant or product gave rise to that income, cost, asset or liability. The pool of costs, assets and liabilities of each cost centre can then be attributed to further cost centres or products until each cost centre is exhausted and all revenue, costs and capital employed are associated with products and services.

### 2.2 Concepts of Attribution

The fundamental feature of this approach to attribution is adherence to the key principle of causality. Each item of income, cost and capital employed recorded in BT Group’s accounts is attributed to the network components, services and products which make up the separate Markets in which BT operates.

Income and cost items are attributed to the relevant activities and components by either allocation or apportionment.

Allocated income and costs represent items of income, operating costs and capital employed which can be assigned wholly to a particular component, service or product by virtue of information in the accounting records.

Apportioned income and costs represent items of income, cost and capital employed that cannot be identified directly to any one component, service or product, and are shared between two or more components, services or products on an appropriate basis.

BT’s approach to apportionment is to seek to identify the appropriate driver for each item and, as far as possible, to use objective operational and/or financial data relevant to that driver to generate apportionment bases.

This approach to the process of attribution of financial information to components, services and products can be summarised as follows:

Review each item of cost and revenue, assets and liabilities.

Establish the driver, i.e. the process that caused the cost to be incurred or the revenue to be earned.



Use the driver to attribute the cost to components, services or products.

Use the driver to attribute revenue to retail products or wholesale services.

The general concepts of attribution in Accounting Separation are set out below:

Revenue: Revenue is recorded in the accounting records in such a manner that it is usually possible to allocate it directly to wholesale services or retail products. Where it is not possible to allocate directly, revenue is attributed to the relevant service or product using information from BT's billing systems

Costs: Costs are drawn from the accounting records. The processes applied to the costs, which vary according to the nature of the costs and the way in which they are recorded, are set out below.

- o Allocation: Certain costs can be directly associated with particular activities and plant groups and, therefore, do not require apportionment. These costs include most of the provision and installation costs, maintenance costs and depreciation directly related to customer-facing activities, such as installation of private circuits or maintenance of customer premises equipment. They also include the direct plant costs, which are the prime operational costs of activities that relate to BT's network. Some of these costs can be directly attributed to primary plant groups, such as local lines, local exchanges, or transmission. There are other plant group costs, such as some of the costs of plant testing and power equipment costs, which are allocated to support plant groups and then apportioned to primary plant groups.

- o Apportionment: Other costs cannot be directly associated with particular activities and plant groups, and require apportionment. In the case of network costs this process makes extensive use of engineering data reflecting not only each plant group type (e.g. local lines, transmission equipment) but also the type of technology (e.g. metal and fibre local lines, PDH and SDH transmission equipment). Certain other costs can be identified within the accounting records as relating to a discrete function such as repair centre costs, computing or billing. A review of this function, often by the means of work/application analyses or a survey of staff activity, establishes the cost driver and is used to apportion its costs between activities and, if applicable, plant groups.

The remaining costs to be apportioned cover a number of central support units (e.g. motor transport, accommodation) and other specialist departments that support network activities, customer facing operations and head office functions (e.g. the legal department).

Hence costs are initially either linked to directly allocated costs or apportioned to support functions, activities or plant groups using appropriate cost drivers. BT uses a number of techniques and sources to apportion these costs, such as surveys of staff activity, analyses of research programmes, application analyses, or operational data such as space occupancy records.

- o Corporate Costs: Although BT utilises, wherever possible, objective data relating to these cost drivers, there is, however, some corporate expenditure for which no specific apportionment bases can be readily derived. These corporate costs are apportioned to activities and plant groups so as to reflect the value added by management effort as reflected in the pay and fixed assets within each activity or plant group. So, any individual Market will be charged on the basis of all corporate costs divided by pay plus a percentage of fixed assets multiplied by that Market's pay plus the percentage of fixed assets."

518. Mr Duckworth's view is that the methodology underlying the RFS was likely to produce accurate estimates of the LRIC+ cost of residential fixed voice services, because the production of the RFS was a regulatory requirement, and BT had to expend significant resources on determining costs in accordance with it. The footnote to paragraph 5.70 of MD1 recorded that in 2007, BT said that the regulatory financial reporting obligations cost it several million pounds each year. BT has not suggested to the contrary. Mr Duckworth also noted that there was the audit opinion referred to above. At paragraph 5.71 he said that he therefore considered that the operating cost categories in the RFS, on a per-line basis, provided an appropriate estimate of the LRIC+ cost of the corresponding activities for SFV Services (including access) for BT in 2009. Also, the CCFS dealt with voice services specifically and therefore, according to Mr Duckworth, they were an appropriate

proxy for the SFV Services, bearing in mind that in 2008/2009, BT was still not permitted to provide bundles.

519. Of course, the relevant starting point for these claims is not 2009, but 2015/16. There were no more RFSs (in relation to retail voice services) after 2009 which attributed costs specifically to voice services (or to any particular services within BT Consumer as a whole). Indeed, there were no further relevant RFSs at all. To deal with this issue of timing, what Mr Duckworth did was to update the 2009 figures for indirect costs on the basis of the CPI index, first to reach figures for 2015/16 and then figures for each succeeding year in the claim.
520. Dealing first with the figures for 2009, what Mr Duckworth does is to take the total costs of providing those voice services, excluding direct costs, in other words all indirect costs. The CCFS did not break these down further into incremental and common costs. See paragraphs 5.66 and 5.67 of MD1. Using the figures provided in Section 9.1 of the CCFS for 2009 (and also some information contained in BT's s135 Response to Ofcom in 2017), Mr Duckworth then calculated that the total access costs were £266m (see the first column in the CCFS p78) and the cost of calls were £174m (see the 2<sup>nd</sup> to 5<sup>th</sup> columns). The total is £440m. He then divides this by the number of lines, at the time being 14.73m. This means that the total "non-network" costs were £29.87 per line for 2009, on an annual basis.
521. Mr Duckworth then applied the CPI index to the £29.87 figure for 2009 to convert it into a figure for 2015/2016. He did this by increasing the £29.87 by 16.51%. This gave a figure of £34.80. He then made a year-on-year increase across the claim period, again using the CPI index. See Table 19 under paragraph 5.86 of MD1.
522. This is also shown in the table reproduced in the Benchmarks tab of the CR Spreadsheet. See also the comparative tables at Table 6.11 and Figure 6.12 of HJ1, which illustrate the radical differences between Mr Duckworth and Dr Jenkins on the extent of indirect costs (both incremental and common) attributed to SFV Services. Thus, Mr Duckworth's figure for 2015/2016 is £34.80, as noted above, while Dr Jenkins' is £113.51, of which £92.34 represented the common costs contribution from SFV Services.
523. Mr Duckworth's view was that there was no method other than using the RFS and updating it to determine indirect costs which was either appropriate or practical.
524. We should add that Mr Duckworth used a number of comparators, along with what Ofcom had said about BT's margin in 2006 (when it was about to be released from its price cap) to support his view. We refer to details of this below when discussing his reasonable margin analysis.

## **Dr Jenkins' methodology**

### *Derivation of BT Consumer Common and Incremental Costs*

525. Dr Jenkins' approach is quite different. Her starting point, insofar as data is concerned, consisted of the figures produced by BT Consumer for each of the relevant claim years and in particular its SG&A ("Sales, General & Administrative") costs and its D&A ("Depreciation and Amortisation") costs. These comprised all of the indirect costs for BT Consumer. Since they were not "disaggregated" further for each of BT Consumer's component services (which included SFV, bundles, Sport and TV, among others) Dr Jenkins undertook the following tasks:
- (1) For the whole of BT Consumer, identifying which of the indirect costs, in her view, were incremental and which were common; she did this by first ascertaining which of the costs were common – whatever was not said to be common was deemed to be incremental;
  - (2) Of the incremental costs so ascertained, estimating what part of them were incremental to SFV Services only;
  - (3) Of the common costs so identified, identifying what contribution to those costs should be made by SFV Services only.
526. Dr Jenkins' allocation of indirect costs to their incremental or common components is critical to her entire competitive benchmark analysis. She first considered each SG&A and D&A cost item shown in BT Consumer's Profit and Loss data, so as to establish a reasonable estimate as to which proportion of such costs were likely to be incremental and which were likely to be common across the board. This had to be done to avoid simply assuming that all of such costs were common. The exercise of apportioning incremental and common costs is set out in Annex 7 to HJ1. Put briefly, Dr Jenkins considered the descriptor given for each particular class of costs and "scored" it in terms of its likelihood of being a common or incremental cost. See the terms used as set out in A7.1 of Annex 7. It follows that the exercise undertaken by Dr Jenkins assumed that all of the common costs within the reported SG&A and D&A cost items were common to every aspect of BT Consumer. In other words she did not take account of the possibility that some indirect costs might be common as between voice and broadband services but not to (say) TV.
527. The result of this scoring exercise is at Tables A7.2 – A7.4. In each case, the amount of the relevant cost for the year is given and Dr Jenkins then states reasons for her particular score. The overall results of the scoring are then given in Table A7.5 for the SG&A costs and in Table A7.6 for the D&A Costs. In both cases, Dr Jenkins sets out her primary "Baseline" case, but then alternative "Low" and High" scenarios as well.

528. For all years, her baseline case for SG&A costs is that over 30% of them were common, and in the case of D&A, over 60% were common. On a combined basis, the common costs over the claim years ranged from 39% to 46% of BT Consumer's total SG&A and D&A costs. See Table A7.7.

**Table A7.5 Proportion of SG&A costs deemed common costs**

	2015/16	2016/17	2017/18	2018/19 <sup>1</sup>	2019/20	2020/21	2021/22
"Baseline" scenario	33%	32%	32%	33%	39%	40%	37%
"Low" scenario	21%	19%	20%	20%	25%	26%	24%
"High" scenario	46%	45%	45%	46%	54%	55%	51%

**Table A7.6 Proportion of D&A costs deemed common costs**

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
"Baseline" scenario	64%	65%	65%	65%	65%	65%	65%
"Low" scenario	49%	50%	50%	50%	50%	50%	50%
"High" scenario	79%	80%	80%	80%	80%	80%	80%

**Table A7.7 Proportion of Total SG&A and D&A (combined) costs deemed common costs**

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
"Baseline" scenario	40%	39%	39%	42%	45%	46%	43%
"Low" scenario	27%	26%	26%	29%	31%	31%	30%
"High" scenario	53%	52%	52%	56%	60%	61%	57%

529. Since the actual amounts for SG&A and D&A costs are given, Dr Jenkins' scoring exercise is then able to yield particular figures for common costs and incremental costs separately, applying the percentages she gave in the scoring exercise.
530. In this context, Dr Jenkins said that where there was no, or only a limited, description of the relevant costs item, she also made use of (as a guide and no more), the approach taken by Ofcom in its "Fixed Access Market Reviews Approach to the VULA Margin - Confidential Statement" of 19 March 2015 ("the VULA Margin Statement"). VULA stands for "Virtual Unbundled Local Access" which is a wholesale product sold by Openreach (then a wholly-owned BT subsidiary forming its "access division"). The VULA product is necessary for those communication providers who wished to provide superfast broadband. Ofcom's concern was that BT (through Openreach) could set a price for VULA provision which meant that there was an insufficient margin between that price and the

retail superfast broadband price; this would give rise to the risk of a “margin squeeze” on BT’s competitors seeking to enter and operate in the superfast broadband market. The object was to impose a condition requiring BT to set the VULA charge so as to maintain a minimum VULA margin, with a requirement on BT to provide the data necessary to monitor compliance every six months. This would be consistent with Ofcom’s regulatory aim to ensure that BT could not use its SMP in the wholesale market to set the VULA margin, such that it would cause retail competition in superfast broadband to be distorted. See paragraph 7.1 of the VULA Margin Statement.

531. The VULA margin exercise conducted by Ofcom was relevant here, according to Dr Jenkins, because part of it involved Ofcom seeking to allocate a proportion of BT Consumer’s SG&A costs. Ofcom gave its view as to which particular SG&A costs could be considered “short-run variable” (“SRV”) or “long-run variable” (“LRV”), which Dr Jenkins said approximated to incremental and common costs, in the sense that an item labelled SRV would have a lower proportion of common costs than one labelled LRV. Dr Jenkins set out Ofcom’s categorisation of the relevant costs at paragraph A7.7 in Annex 7. But she emphasised that she used the VULA Margin Statement as a guide only.
532. The next stage in Dr Jenkins’ analysis was to allocate a proportion of the incremental costs (as opposed to common costs) of BT Consumer which she had identified, to SFV Services. Unlike the RFS, which used the principle of costs causality to allocate incremental costs, Dr Jenkins used the so-called EPMU (Equi-proportional mark-up) approach. This allocated incremental costs in proportion to direct costs. She did this because she said she did not have a means of allocating those costs on the basis of costs causality, as she had no costs causation drivers. She added that, had she allocated the incremental costs on the basis of number of lines or number of customers, the outcome would not be materially different.

#### *SAC Combi*

533. That then left the task of deciding how BT Consumer’s total common costs (as now ascertained by Dr Jenkins) should be borne by its various constituent services and in particular, by the SFV Services.
534. For this assessment, Dr Jenkins uses a SAC Combinatorial (“SAC Combi”) approach. SAC stands for “Stand-Alone Costs”. These are the costs that would have been hypothetically incurred in producing a given service or increment if it was offered on a standalone basis, i.e. by a firm producing only the relevant service or increment. Accordingly, if BT Consumer’s only service was provision of the SFV Services, all of its common costs would have to be recovered from SFV Services. What that would look like, according to Dr Jenkins, is shown, on a monthly basis for

2015/2016, at Figure 6.7 of HJ1. On that footing, common costs would represent by far and away the most significant element of the competitive benchmark.

535. However, as Dr Jenkins explained at paragraph 6.134, this would not be an appropriate way to recover common costs from SFV Services because, of course, there were in fact other services within BT Consumer that make, and would be expected to make, a contribution to the recovery of common costs overall. The question then is how to distribute those contributions across all of BT Consumer's services, and in particular, ascertaining what contribution should be made by SFV Services. This is where the SAC Combi approach comes in.
536. At this point we should say something more about the conceptual basis for the SAC Combi approach. The idea behind it is to replicate what would happen in contestable markets – i.e. a market where effective competitive constraints were exerted by a credible threat of easy entry into each and every activity. The question that drives the SAC Combi approach is: how much flexibility would a multi-product firm have to recover its common costs, if it was subject to a credible threat of entry from rival suppliers who produced each and every possible combination of those products? This assessment is conducted within the overall competitive constraint that the sum of all the profit contributions across the products that share common costs should not over-recover those common costs.
537. To take an example, suppose a firm supplies 4 products A, B, C, D that share common costs and the issue is the reasonable common cost recovery achieved on product A. If an entrant tried to compete on the basis of product A only, it would need to recover the whole of its common cost from sales of A, so this would correspond to the SAC of product A. That would therefore represent a comparatively high reasonable price benchmark for product A. But if the entrant instead chose to compete on the basis of A+B, or A+C, or A+B+C, etc., the entrant would be able to recover the same common costs across a broader base of sales and this could well lead to a lower reasonable price benchmark for product A. By exploring these different entry options (or combinations) the SAC Combi test yields a benchmark that imposes a stronger standard on the incumbent firm when setting the price of A.
538. The aim of Dr Jenkins' use of this approach is thus said to be to assess the contribution to common costs which products other than SFV Services (but which share the same common costs as SFV Services) actually make towards the recovery of common costs. To the extent that such common costs are not recovered from the sale of these other products, they are then attributed to SFV Services.

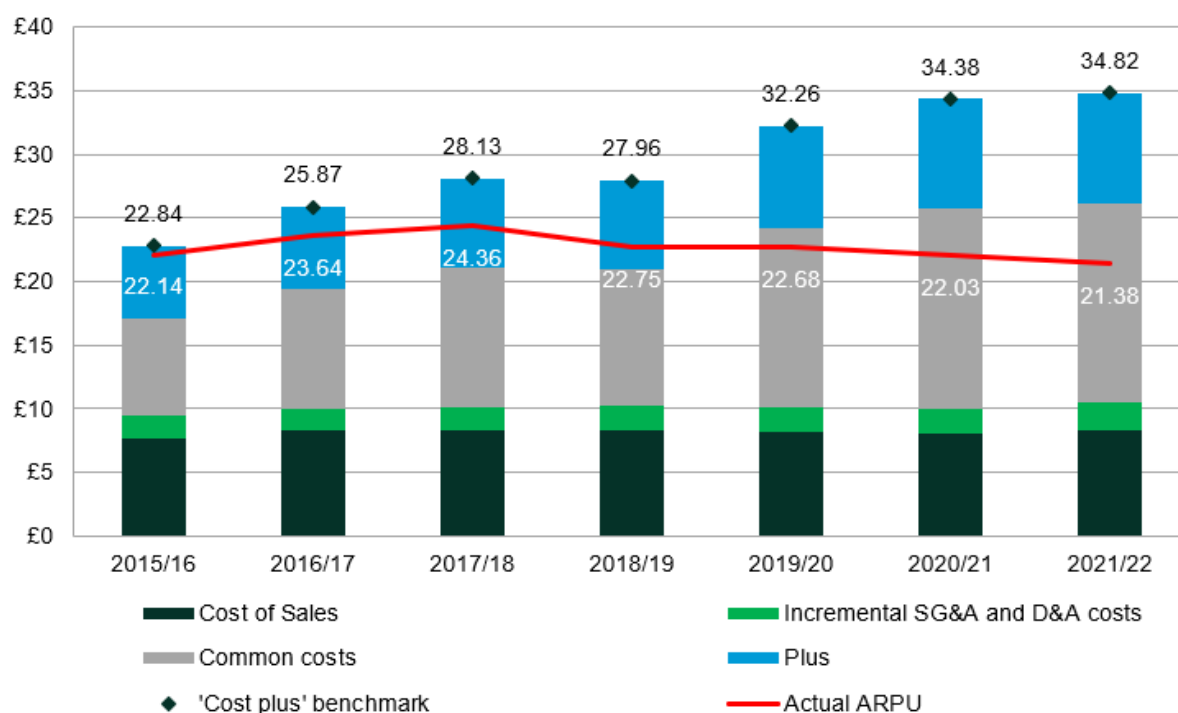
539. As there are a variety of products within BT Consumer, the SAC Combi exercise required that different combinations of the individual services be tested together, so that the range of differing contributions to common costs could be fully ascertained.
540. Dr Jenkins therefore decided to use a total of 25 combinations of services for the period up to April 2018, and 24 combinations for the period thereafter. The reason for the difference in numbers is that after April 2018, the Voice Only element of SFV Services became irrelevant due to the Commitments. The different combinations are defined and set out at paragraphs 6.141-6.145 and Table 6.9 of HJ1.
541. For each combination of services, there was actual data in terms of (a) combined revenue, and (b) direct costs (dealt with in detail in Annex 6 to HJ1). There was also data as to the relevant amount of incremental costs as a result of Dr Jenkins' allocation exercise set out above. There was also, of course, the total common costs of BT Consumer as also ascertained by Dr Jenkins.
542. The next steps are set out at paragraphs 6.146-150 of HJ1 and described in more detail at Annex 8.
543. In summary, for each combination, Dr Jenkins first calculated a putative ARPU (as a proxy for price) which consisted of the entire BT Consumer common costs, the direct costs, the allocated incremental costs (all of which Dr Jenkins here refers to *en bloc* as SAC) together with a margin which would represent 25% of the putative revenue. 25% was chosen because that is the reasonable profit margin which Dr Jenkins separately considers should be allowed to SFV Services. Mathematically, this means that the putative ARPU can be calculated by multiplying the SAC (as here defined by Dr Jenkins) by 4/3. She refers to this as the "Benchmark Combination Revenue" ("BCR").
544. The next step is to calculate the actual revenue for all the elements in a particular combination (including SFV Services) for the year in question, which Dr Jenkins calls "the Observed Revenue" ("OR"). This is done on an annual basis. The differential between BCR and OR is then calculated. If the OR is less than the BCR, it means that the OR could in theory be increased to the point at which all of the SAC are recovered plus the margin i.e. the BCR. If, on the other hand, the OR was higher than the BCR, then it would have to be decreased so as to avoid the making of excessive profits which are here defined as profits over and above the revenue required to discharge all the SAC plus the margin.
545. As it happens, on the basis set out by Dr Jenkins and taking 2015/2016 as an example, the OR was always below the BCR, which meant that there was "headroom" in theory for the revenue (i.e. the price) of the total combination to increase.

546. The annualised differential figure is then divided by the number of lines to reach a per line annual differential. Here, it is important to note that Dr Jenkins uses the total number of BT's voice lines, whether within SFV Services or within any bundled product. She says that she does this in order to reflect the commercial strategy on the part of BT to have a single price for voice, whether provided on a stand-alone basis or with other products.
547. Dr Jenkins then divides the per line annual differential into a monthly differential so as to reach an increment which should be added to the actual SFV price so as to enable that particular combination to achieve its BCR. This exercise is shown at Table A8.2 in Annex 8. The final uplifted figures for SFV Services are shown for 2015/2016, by way of example, at Figure 6.8 of HJ1. The putative benchmark price will vary across each Combination because the revenue, incremental and direct costs for each Combination will be different, even if the total common costs figure is the same.
548. For Combination 1, which is SFV Services only, a putative ARPU of £28.47 is generated by taking 4/3 of the SAC which was £21.35. Then £7.12 is added, being 25% of £28.47 which is the margin for that case. See Figure 6.7 of HJ1. In other words, in order to recover all of the SAC (which includes all of BT Consumer common costs) together with a reasonable margin, the price would have to be £28.47. The figures here are easy to calculate because this is in truth not a combination at all, but simply SFV Services. It follows that the competitive benchmark yielded for that "combination" will be the highest of any combination, because there is no prospect of a contribution to common costs coming from any other product.
549. The final part of the SAC Combi exercise for any given year is then to select the lowest competitive benchmark for SFV Services entailed by the different Combinations. Dr Jenkins explains the basis for this in HJ1 as follows:
- "6.150 In order to ensure that my SAC Combinatorial "cost plus" benchmark does not allow SFV Services to over-recover common costs (i.e. does not include common costs which are not reasonably attributable to SFV Services), I identify the lowest "cost plus" benchmark for SFV Services from the range of combinations, which I call the "binding constraint".
- 6.151 The "binding constraint" is the lowest level "cost plus" benchmark for SFV Services that ensures that no relevant combination earns returns above its SAC plus a 25% EBIT margin. The "binding constraint" for each financial year is therefore my "cost plus" benchmark for SFV Services for that financial year."
550. Figure 6.8 shows that the lowest monthly putative ARPU for 2015/2016 is £22.84, being the figure generated for Combination 23.
551. Figure 6.10, shown below, then compares the benchmarks resulting from the SAC Combi exercise for each relevant year with the actual known ARPUs for SFV Services for each year. It can be seen that in no case, does the actual ARPU exceed or even reach the competitive benchmark. On that basis, according to Dr Jenkins, there is no excess pricing for the purposes of Limb 1, since the actual price never exceeds the competitive benchmark at all. These figures are updated and changed



slightly in the Results tab of the BT Spreadsheet for the reasons given above, but the difference in result is not material.

**Figure 6.10 Comparison between SFV Services ARPU and the SAC Combinatorial “cost plus” benchmark (baseline common costs scenario)**



552. It will be seen from the results for 2015/2016, that the monthly contribution to common costs is about £8 per line. The total monthly common costs for all of BT Consumer’s services, as shown in Figure 6.7, is £11.92 per line. In other words, the competitive benchmark figure for 2015/2016 includes about two thirds of BT Consumer’s total common costs (as identified by Dr Jenkins).
553. The annual figures for all of this are shown in Table 5.1 of HJ2 set out at paragraph 511 above.
554. According to Dr Jenkins, the use of a SAC Combi exercise is appropriate, because it recognises both that it cannot be correct to load all of BT Consumer’s common costs on to SFV Services, given the other services that exist and contribute, but also that considerable flexibility should be permitted to the operator in terms of how common costs are recovered. This is especially because, by definition, there is no principle of causality which can attribute such costs across the different services.

#### *DSAC Cross-Check*

555. In addition, and as a cross-check, Dr Jenkins also undertook an analysis on a Distributed Stand-Alone Costs (“DSAC”) basis. This involves, again, an allocation of common costs to the different individual services. Her starting point is the same as for the SAC Combi exercise, namely her ascertainment of what part of BT Consumer’s SG&A and D&A costs are common, as opposed to incremental, and then her allocation of incremental costs to different services. The difference with

the DSAC approach is that instead of allocating common costs as a result of the SAC Combi exercise, they are allocated to individual services within a “broad increment” of services on a simple EPMU basis. On this alternative footing, according to Dr Jenkins, there is still no excessive pricing. See paragraphs 6.156-6.158 and Figure 6.11 of HJ1 (itself set out under paragraph 860 below).

#### *Dr Jenkins’ Sensitivities*

556. Finally, Dr Jenkins then applies two conservative sensitivities to her conclusions from the SAC Combi exercise. First, she has her “low” common costs scenario as set out in Annex 7, and second she has an alternative reasonable margin of 20% instead of 25%. The effect of using these sensitivities is shown at Table 6.10. This shows that price was still below the costs benchmark where the margin is 25% but with a low common costs scenario. For baseline costs and 20% margin, price exceeded the benchmark only in 2015/16 and 2016/17 and then only very slightly. For low common costs and a 20% margin, price exceeded the benchmark only in 2015/16 and 2016/17 and then only by 9.3% and 2.9% respectively. A further comparative table with all the different alternatives is at the Results tab of the BT Spreadsheet.

#### *Comparative Tables*

557. A useful comparison between the very significant difference in outcomes from Mr Duckworth’s and Dr Jenkins’ respective analyses is shown at Table 6.11 and Figure 6.12 of HJ1, reproduced below (Table 6.11 has been updated in Table 5.1 of HJ2, set out at paragraph 511 above):

**Table 6.11 Comparison between the CR’s and HJ my “cost plus” benchmark for SFV Services (£ per year, per line, excluding VAT) [Confidential: Information for Financial Years 2020/2021 and 2021/2022]**

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
<b>(A) Cost of sales per line</b>							
CR	96.68	104.86	99.95	100.49	98.44	96.76	100.51
Dr Jenkins	92.05	99.22	100.16	100.52	98.36	96.70	100.50
<b>(B) Non-network costs per line</b>							
CR	34.80	35.74	36.61	37.37	37.69	38.24	41.68
Dr Jenkins	113.51	133.60	153.02	151.08	191.94	212.68	212.88
Of which:							
Incremental SG&A and D&A	21.17	20.30	21.21	22.23	22.69	23.31	24.96
Contribution to common costs	92.34	113.30	131.80	128.85	169.25	189.38	187.92
<b>(C) Total costs per line (A + B)</b>							
CR	131.48	140.60	136.56	137.86	136.13	135.00	142.19
Dr Jenkins	205.56	232.82	253.17	251.60	290.30	309.39	313.38

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
<b>(D) EBIT margin per line</b>							
CR (8.76%)	12.62	13.50	13.11	13.23	13.07	12.96	13.65
Dr Jenkins (25%)	68.52	77.61	84.39	83.87	96.77	103.13	104.46
<b>(E) “Cost plus” benchmark (C + D)</b>							
CR	144.11	154.10	149.67	151.09	149.20	147.96	155.84
Dr Jenkins	274.08	310.43	337.56	335.47	387.07	412.52	417.84

558. On an annualised basis Dr Jenkins’ analysis (see Annex 3 to BT’s Closing and Table A6.3 of Annex 6 to HJ1) is as follows:

	Unit	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
Number of SFV Services Lines	#m	2.67	2.09	1.67	0.59	0.46	0.37	0.28
Number of Voice lines across BT Consumer	#m	9.56	9.29	8.93	8.41	7.07	7.65	6.93
Proportion of SFV Services to total voice lines	%	28%	23%	19%	7%	6%	5%	4%
SAC Combi Baseline Scenario								
Total BT Consumer Revenue		4,373	4,676	4,709	4,682	4,486	4,114	4,253
Total BT Consumer Costs		3,564	3,887	3,988	3,982	4,114	3,988	3,815
Total BT Consumer Cost of Sales		2,580	2,912	2,963	2,911	2,885	2,748	2,837
Total indirect costs (SG&A and D&A)	£m	983	975	1025	1071	1229	1240	1261
Common costs across BT Consumer	£m	390	379	398	427	548	562	541
Amount allocated to SFV Services (under 25% margin scenario)	£m	243	241	225	79	80	73	55
% of BT Consumer common costs	%	62%	64%	57%	19%	15%	13%	10%
% of BT Consumer total Costs	%	11%	10%	10%	11%	13%	14%	13%

	Unit	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
Amount allocated to SFV Services (under 20% margin scenario)	£m	217	218	205	69	72	67	49
% of BT Consumer common costs	%	56%	58%	52%	16%	13%	12%	9%
Total SFV Services Revenue	£m	784	681	592	464	408	365	283
SFV Services Revenue as a percentage of BT Consumer Revenue	%	18%	15%	13%	10%	9%	9%	7%
Total Revenue from voice in bundles	£m	1,684	1,801	1,850	1,769	1,663	1,579	1,571
Total voice in bundles Revenue as percentage of BT Consumer Revenue	%	68%	73%	76%	80%	80%	81%	85%

559. For the sake of completeness, we should add that both sides (but principally BT) have produced other analyses, taking into account points made by the other. These will be referred to below.

## **REASONABLE MARGIN**

### **Introduction**

560. Although the assessment of the reasonable rate of return in the costs-plus analysis is, in one sense, at the end of that analysis - because it is added to the costs to arrive at the competitive benchmark - it is necessary to consider it at the outset here.
561. This is principally because Dr Jenkins' SAC Combi exercise itself involves the application of the margin - see paragraph 543 above.
562. In addition, however, Dr Jenkins introduces an "upper-bound" element to the eventual margin she adopts.
563. In very broad terms, the extent of the dispute between the parties is this: Mr Duckworth postulates an 8.9% margin, but in the hot tub discussion, he was prepared to move somewhat to say that the maximum could be 10%. For the sake of clarity this 10% margin would imply an 11.1% margin if calculated as a mark-up over costs excluding the margin itself. The discussion below employs the margins discussed by the experts on the former rather than the latter basis, although the difference

of calculation is purely mathematical. The former basis is referred to as the EBIT margin which is operating profit divided by total revenue.

564. For her part, Dr Jenkins' primary EBIT margin is 25%. That is itself the 90<sup>th</sup> percentile of a range of margins which she produces. But as an alternative, she would accept 20%, which is the midpoint of her 75<sup>th</sup> and 80<sup>th</sup> percentiles. For the sake of completeness, we would add here that her aggregated median percentile is about 14%. See Table A5.8 in Annex 5 to HJ1, shown in paragraph 615 below.
565. Unlike the calculation of the underlying costs (see below), in the context of a reasonable margin, it is not the case that the experts have each chosen entirely different models. Instead, they have considered, in the main, (a) a number of different but allegedly comparable firms and industries, (b) what EBIT margins have been reported by BT at various stages, and (c) what Ofcom has said on the subject. We concentrate on these three different aspects, along with Dr Jenkins' upper bounds model.

### **The Law on Reasonable Margin**

566. The case-law recognises that a company may legitimately want to cover its cost of capital which corresponds to the profit which enables it to remunerate its investors at the appropriate level. It must therefore in general reflect the minimum sustainable return that investors would expect to earn in the relevant business in order to make it worthwhile for them to commit funds to it. In economic terms, this minimum sustainable (or "normal") return is part of the cost of providing the good in question, since investor funds are a resource that is required for the good to be supplied, and investors will provide that resource only if they receive adequate compensation for doing so, just as would be the case for any other necessary input to the supply of the product.
567. The cases do not, however, prescribe any particular approach to the determination of a reasonable margin other than the fact that it should be a "reasonable", as opposed to the highest possible such margin. One approach may be to look at return on capital employed ("ROCE"). Another is return on sales ("ROS"). Both sides here have adopted some form of ROS approach on the basis that an ROCE approach does not work here, given the nature of the SFV business.

### **Mr Duckworth's Approach**

#### *BT's Reported Margins 2004-2006*

568. Mr Duckworth obtained his 8.9% figure from BT's reported net EBIT margins for its retail residential fixed voice services for 2004-2006 being 9.9% (the CR's Closing says 10.1% but Figure 5 of MD1 shows it as slightly lower, though the difference is immaterial here), 8.8%, and 8.9%, respectively. He chose 8.9% as the latest reported margin within those years. Mr Duckworth then sought to corroborate that figure, as it were, by a number of other data points.

569. First, we consider the correctness or otherwise of taking BT's reported margin from 2006. Mr Duckworth fixed on this year because it was the last year in which BT's voice charges were regulated by Ofcom. This therefore suggested that margins at that level were considered not excessive, and moreover, that it was not now necessary to constrain them. An important point made by Mr Duckworth here was that at this stage, Ofcom's own perception of the market was that there had been considerable change, with substantial growth in competition which would develop further. Ofcom also noted the decline of BT's market share. The markets were becoming dynamic, competition was growing and with competitive pressure on BT increasing, this looked set to continue. Technical developments continued apace. All of this led to the need to consider whether price regulation was still necessary, and Ofcom found that it was not. See paragraphs 4.37-4.41 of its 2006 Statement.
570. Mr Duckworth's view was that this growth in competition suggested that BT's prices - and hence its margins - were at or above a competitive level by 2006. It would therefore be wrong to discount the reported 2006 margin as irrelevant simply because it reflected a regulated price. We agree with that.
571. There was much discussion between the experts in the hot tub (Day 14/146-Day 15/22) as to what exactly Ofcom was doing in 2006, and the extent to which it expected BT's margin to go up because this would lead to entrants coming in, and whether, in doing so, Ofcom was looking at this as a short-term measure because ultimately, such market entry would drive BT's margins down.
572. In the end, we were not much assisted by the exercise of trying to divine Ofcom's true thinking in 2006, especially as Ofcom was in any event entitled to look at things differently, as indeed it did in 2009 and 2017. And of course, we are not ultimately bound by Ofcom's views and decisions.
573. Of course, in the event, BT's voice services' reported margin did increase after 2006 to reach just under 21% by 2009 (see the RFS). It had been 16% in 2008. Yet, as is pointed out by BT, Ofcom did not intervene. Indeed, at that point, it removed regulation from BT's residential voice services altogether on the basis that it no longer had SMP. See Ofcom's 2009 Statement. It is to be noted that in the summary, Ofcom stated that price regulation had been removed in 2006 "Given the improvement in competition in the market". It also said that as at 2009, "The market was effectively competitive" with competition likely to increase.
574. BT therefore suggests that the 21% margin earned by it in 2009 is a better starting point than 2006 for a reasonable margin analysis if one is looking at BT's previous reported voice margins. We can see the force of this point, although it is possible that this higher margin might be consistent with the outcomes that arise from workable competition, and yet still be higher than the minimum profit level that would be necessary sustain competition.

575. Ofcom also noted in 2009 that BT's costs had decreased faster than revenues. It said that the evidence suggested that BT had maintained profitability by reducing costs, but strong conclusions were difficult to make from gross margin data. However, Ofcom clearly felt that the increased margins (in some cases, accompanied by increased prices) could not simply be put down to BT's market power, and obviously Ofcom concluded that it did not at that stage have SMP.
576. Mr Duckworth, for his part, concluded that there was an element of market power at this point, because the significant cost savings made by BT were not being passed on to the customers, which it is argued is what would necessarily happen in conditions of workable competition. We understand this argument, but it largely reflects the general position of the CR and its experts, which sought to equate the zero excess profits of perfect competition with the more nuanced concept of workable competition.
577. A further point made by Dr Jenkins was that BT Consumer's margins had fluctuated considerably between 2012 and 2021. They were 14% in 2012/13, rising to about 20% in 2014/15 and then declined to 3% in 2020/21. While there was a degree of circularity in using BT Consumer's own margins to assess the reasonable level of return here, she said that the range of returns here supported the idea of using an "upper bounds" approach.
578. In fact, and as Mr Duckworth notes at Figure 3 at p59 of MD2, between 2015/2016 and 2020/2021, BT Consumer's actual margins were lower than its margins, shorn of the alleged excessive margin in SFV Services, and significantly so between 2015/2016 and 2017/2018. For that latter period, the adjusted margin for BT Consumer was between around 11% and 14%, with much lower margins for the following 2 years. Of course, there is some circularity here as well because Mr Duckworth has used the CR's full case on the excess pricing; as he says at paragraph 5.118 he subtracted Mr Parker's estimate of the quantum of overcharge in each year of the claim.
579. In the light of what we have said above, we do think there are some problems with Mr Duckworth's use of 2006 as a starting point, although BT's alternative starting point of 2009 is not free from difficulty either. However, we do need now to consider what Mr Duckworth describes as cross-checks for his 10% figure, which consist of a number of comparators, together with what Ofcom said about BT's margin in its Conclusions in 2017.

#### *Mr Duckworth's Comparators*

580. Mr Duckworth's comparators consist of other UK telecoms companies, namely the Post Office, Virgin Media, TalkTalk, Utilities Warehouse and Phone Co-op.
581. The Post Office margin data relied upon by Mr Duckworth are notable for relating specifically to the Post Office's SFV activities. Mr Duckworth points out that the Post Office's SFV margins were

always less than 10% for the period when it operated in the voice-only market, i.e. 2014-2017, the actual percentages being -15%, 10%, 5% and 10% respectively. See Table 22 at MD1 p84.

582. The other comparator margins relied upon by Mr Duckworth related to broader sets of services than specifically SFV. Over the period 2010 to 2019, the average margins for Sky, Virgin Media, TalkTalk, Utilities Warehouse and Phone-Co-op were 16.9%, 7.4%, 6.9%, 5.3% and 2% respectively (see Figure 7 in MD1 which relates to their overall EBIT margins). He said that these companies were engaged in similar activities with a similar business model to BT Consumer. Also, his approach was conservative, because all the comparators had a higher capital intensity than SFV Services which would tend to increase the margins required (we deal further with the question of capital intensity in paragraphs 630 - 632 below).
583. Sky, with its 16.9% margin, is the obvious outlier here if one compares it to Mr Duckworth's 10% figure. Mr Duckworth says that it is a less reliable comparator because a high proportion of Sky's revenue comes from Pay-TV, which has a different and higher capital intensity element than SFV Services. He further notes that Sky took significant risks in entering this market and was likely to have significant intangible assets, such as content rights and brand and subscriber relationships, which potentially justify higher returns.
584. In the hot tub discussion on Day 15, Dr Jenkins said that this is not a reason to exclude Sky from consideration altogether, and it should form part of the range. She added that merely because a comparator had a differentiated offering, that was not a reason to discount it on the basis of a particular product mix, since that is just how the market is. Mr Duckworth agreed that differentiation is important in this market, but said that from an investor point of view, differentiation is just a means to an end, and that investors will not require different returns just because there are differentiated strategies within different suppliers. We see this, but overall, we would not rule out Sky as a comparator, broadly for the reasons given by Dr Jenkins, although we note its particular position, and of course, it does not support a margin as high as Dr Jenkins' 20-25% figure.
585. On Virgin Media (7.4%), Dr Jenkins said that it had to be remembered that Virgin was a vertically integrated company. Her point was that Mr Duckworth had criticised her choice of comparators for including vertically integrated companies which would tend to have higher capital intensities, and yet here, he was including one such company. However, that point does not go anywhere because, as Mr Duckworth observed, if one took the approach that companies with more assets would have higher margins, then this would mean that 7.4% for Virgin should be regarded as the top end of the scale. Mr Duckworth therefore accepted that Virgin Media was not a perfect comparator, but argued that this imperfection made his estimate conservative.



586. As for TalkTalk at 6.9%, Mr Parker thought that this was probably the closest comparator, although, as Dr Jenkins pointed out, it stopped actively marketing voice-only services in 2014, shortly before the claim period. Moreover, it expressed the view to Ofcom that there was not much incentive to stay in the voice-only market, even bearing in mind BT's high margins. See paragraph 462 above. The fact that TalkTalk later decided to cease supplying voice-only services altogether (save for existing customers) suggests that its margin was below the minimum sustainable level. So one needs to apply some caution to TalkTalk's margin in our view.
587. On any view, however, Mr Duckworth's range of margins here are considerably below Dr Jenkins'.
588. We accept that Mr Duckworth uses only 6 comparators and Dr Jenkins criticises this as being too few in number. However, the fact remains that they are all in (or include) a market which supplied voice-only services, and we consider that we should attach weight to them although of course they are hardly conclusive on the point.
589. Mr Duckworth then looks at the margins in postal, energy and water sectors. Here, Ofcom had found that 5-10% was a reasonable margin for Royal Mail. In its energy market investigation, the CMA noted that margins were around 3.5% for 2009-2014 and that 1.5% was consistent with competition for an established supplier. Finally, Ofwat set a margin of 1% for domestic water supply. See paragraphs 5.132-5.133 of MD1.
590. However, Dr Jenkins observed that these were very different business models and in the end, Mr Duckworth accepted that he did not place a huge amount of weight on them as comparators. He said that he recognised that there was potentially more innovation in the telecoms market. On that basis, we do not place any significant weight on these utility sector comparators. We would note, however, that if margin comparisons drawn from industries that differ from SFV and other retail telecom activities are inherently problematic, this problem could apply equally to the broader industry margin comparators on which Dr Jenkins relies for her analysis.

*Ofcom's 2017 Provisional Conclusions and a 10% margin*

591. The CR relies upon various passages in the 2017 Provisional Conclusions to show that in 2017, when Ofcom was considering imposing price regulation on SFV Services, it took the view that a 10% EBIT margin was appropriate for VOCs. To understand this, it is necessary to set out a number of passages from the 2017 Provisional Conclusions and the Annex thereto.
592. First, in the conclusions themselves, Ofcom stated as follows:

“8.2 In developing proposals for the appropriate level of prices for an SFV control, we have considered the following factors:

- Protecting consumers from prices above costs: as set out in Section 6, our analysis suggests that BT's prices of SFV services are above what we would expect to see in a competitive market. Given past price increases

and BT's current level of profitability, customers of SFV services are paying considerably more than they should be.

- Promoting competition in the provision of SFV services: in Section 7 we discuss remedies to support increased consumer engagement and encouraging competitive entry and expansion. These remedies will not be effective in promoting competition if we reduce the price of SFV services below the level at which it is profitable for other CPs to acquire SFV customers. When dealing with SFV customers, these acquisition costs may be quite substantial, although such costs should be reduced if engagement remedies prove to be effective.

8.3 We therefore face a trade-off between controlling prices in a way that protects consumers and ensuring that we do not reduce them by so much that we weaken the scope for growth in competition (taking into account the impact of any engagement remedies discussed in Section 7). We can strike this trade-off in various ways with a range of options on a price control....

8.17 BT currently earns revenue of approximately £["24] per month (ex VAT) from SFV subscribers on average. Our estimates of BT's costs suggest it achieved profitability (ROS) for SFV services in 2015/16 of c.34-42%, which equates to profit of about £8-10 per line per month (ex VAT). Our analysis suggests that a ROS of no more than 10% is consistent with a cost based estimate of profitability for a provider of retail voice services, which equates to profit of between £["1] and £[2.50] per month. We could therefore reduce prices for SFV services by around £[8] per month (ex VAT) in order to reduce BT's profitability on these consumers to a cost based level, which equates to a decrease in prices that consumers experience of between £8-10 per month (inc VAT).

8.18 However, as discussed below, an adjustment of this size would be highly likely to make it uneconomic for other CPs to compete in offering SFV services and acquiring customers. Other CPs incur substantial acquisition costs when acquiring customers, which BT does not incur when serving its existing SFV subscriber base. These costs make other CPs less profitable when compared to BT. Even if the engagement remedies we discuss in Section 7 are effective, some acquisition costs will remain meaning it is unlikely that other CPs would be able to profitably supply SFV customers if prices were set on the basis of BT's costs. We would therefore only use an £8-10 reduction in prices if we were not also imposing engagement remedies. We discuss below the level of price reduction that is still consistent with competition emerging.

#### **A competitive benchmark for SFV retail prices**

8.19 In order to understand how much we could reduce prices by and still expect competition to emerge, we have looked a number of different measures in order to estimate a competitive benchmark. Analysis of these options is set out in more detail in paragraphs A5.70 to A5.86.

#### **BT's historic levels of profitability for SFV voice services:**

8.20 In 2009 we removed retail regulation on the basis that the retail market was competitive. BT's level of retail profitability at this time was at a level at which we believed regulation was no longer necessary, given the market circumstances. At that time BT was struggling to maintain its market share and, despite the removal of retail price controls in 2006 did not appear to have the commercial freedom to raise retail prices. Accordingly, the level of profitability that BT achieved on retail services at that time provides us with a starting point for the level of profitability that we believe is consistent with a market that is sufficiently competitive not to require regulation.

8.21 In 2009, we assessed BT's profitability using ROS and have used the same approach for this assessment. Our assessment of ROS in 2009 suggests a margin for BT of c.20% is consistent with emerging competition. If a similar margin was applied today, BT's monthly line rental would need to be reduced by approximately £["5.80] (ex. VAT)."

593. The CR relies in particular on the statement at paragraph 8.17 which we have underlined for emphasis.
594. However, Figure A5.14 in Annex 5 to the 2017 Provisional Conclusions is also relevant. It provides as follows:

**Figure A5.14: BT's estimated EBIT margins for SFV services [X]**

Line rental (£/month inc. VAT)	Estimated EBIT margins in 2016/17 financial year	Comment
£18.99	BT: ~ 34-42% Other CPs: ~ [REDACTED]%	BT's current price
£13.99 (£5 adjustment)	BT: ~ [X<25]% Other CPs: ~ [REDACTED]%	Lower estimate consistent with promoting competition
£11.99 (£7 adjustment)	BT: ~ [X<20]% Other CPs: ~ [REDACTED]%	Upper estimate consistent with promoting competition
£10.99 (£8 adjustment)	BT: ~[X<15]% Other CPs: ~ [REDACTED]%	Similar to BT's estimated EBIT margin for fixed voice and fixed broadband combined
£8.99 (£10 adjustment)	BT: ~[X<10]% Other CPs: ~ [REDACTED]%	

595. BT contends that the statement in paragraph 8.17 of the conclusions is effectively irrelevant. This is because Table A5.14 shows that if there were to be a £7 price drop (which transpired to be the case in the Commitments), then this would still be permitting BT to make an EBIT margin of 20%, which is Dr Jenkins' alternative margin. So BT positively relies on the 20% figure here.
596. However, we think that the position is not as simple as that. What the Table shows is that a margin for BT of 20% is consistent with promoting competition. This obviously refers back to what Ofcom had said in the passages quoted at paragraph 592 above, namely that Ofcom would want to set a price which nonetheless enabled effective competition to emerge, given that competitors face higher customer acquisition costs than BT. Thus, there needed to be a trade-off between controlling the price to protect consumers, but also ensuring that the scope for growth of competition in the market was not weakened. See in particular paragraphs 8.2 and 8.3. Effectively, as we see it, this is all about providing sufficient incentives for sustaining competition in the market by other suppliers. Ofcom's Figure A5.14 implies that in view of the cost asymmetries between BT and its rivals, allowing BT to earn an SFV margin of 20% would enable rivals to sustain their SFV operations at a margin of between [REDACTED]% and [REDACTED]%, and that this latter range is a truer depiction of Ofcom's view of the competitive margin.
597. We also agree that as a matter of law, the reasonable margin for the purpose of the cost-plus analysis under Limb 1 should not be based on a price designed to incentivise entry into the market. In *Liothyronine*, the Tribunal dealt with an appeal from a decision of the CMA that the various pharmaceutical company appellants had abused their dominant position (they had raised prices by

over 1,100%) and the imposition of a financial penalties which totalled £101m. The appeal against the decision as to abuse was dismissed, although the financial penalties were reduced in some respects.

598. In its judgment, where there were many grounds of appeal, the Tribunal agreed with the approach taken by the CMA in rejecting the use of comparators consisting of entry-incentivising prices as a valid competitive benchmark. While the use of the latter expression in paragraphs 317 and 318 of the judgment might suggest that what was being referred to here was the benchmark for Limb 1 purposes, in fact, both the CMA and the Tribunal said that it was more appropriately to be considered in the context of Limb 2. This does not matter for present purposes. The Tribunal said that it would be incorrect to use entry-incentivising prices in this way because to allow a position whereby a dominant firm's pricing could not be regarded as unfair so long as it was below an entry-incentivising price, instead of protecting consumers, could allow the firm to benefit from high barriers to entry. See generally, paragraphs 137 and 317-320 of the judgment.
599. It is, of course, correct, that the facts in *Liothyronine* (especially as to barriers to entry, the hypothetical nature of the entry-incentivising price levels that were presented, and the excessive prices charged) were very different from this case. It is also true that at least in part, the appellants in *Liothyronine* had advocated that the CMA was obliged to consider comparators such as entry-incentivising prices, whereas here they are being considered simply in the context of analysis of how Ofcom was regarding BT's margin as part of the exercise of determining a reasonable margin under Limb 1. Nonetheless, and as the CR contends, we think that *Liothyronine* has some application here and for that reason, we do not think that BT can simply seize upon Ofcom's reference to a 20% BT margin in the context of proposing a £7 reduction as support for its claimed margin of 25% or 20%.
600. On the other hand, the reference by Ofcom to 10%, as referred to in paragraph 8.17 of the 2017 Provisional Conclusions set out at paragraph 592 above, is not free from difficulty either if it is to be used to justify a reasonable margin of that order in this context. After all, Figure A5.14 above shows that a margin of 15% was similar to BT's estimated margin for fixed voice and fixed broadband combined. That figure would have been the result, according to Ofcom, of an £8 reduction rather than £7 reduction in line rental. This was one of the options which Ofcom considered in paragraph 8.17 save for the point about promoting competition. Indeed, the margin of 15% in the Ofcom Figure makes no reference to promoting competition at all.
601. On that basis, and for the purposes of Limb 1, we do not agree that the CR can rely strongly on what Ofcom said in paragraph 8.17 about a 10% margin, though it is not wholly irrelevant. We think that if weight should be attached to what Ofcom said about the margin here, it is equally valid to refer

to the 15% figure as well. What we also agree is that BT cannot place any real reliance here on the 20% figure for the reasons we have given in paragraphs 598-599 above.

602. Yet further, as matters turned out, while some of BT's competitors had already stopped actively marketing SFV services prior to the introduction of the Commitments (see paragraphs 118-119 above) what the Commitments (including the associated engagement remedies) did not do was lead to a general increase in competitors promoting SFV Services in order to acquire greater market share. [REDACTED] Virgin Media [REDACTED] was no longer strongly promoting SFV Services from August 2021. On that basis it would suggest at least that the margin required by BT's competitors to sustain their SFV operations was towards the top end of the Ofcom [REDACTED] % margin range (if not above it).

### **Dr Jenkins' analysis**

#### *The Upper Bounds Point*

603. First, we deal with Dr Jenkins' "Upper bounds" approach. This denotes Dr Jenkins' approach to the collections of the various margins she has taken from her data-sets to select those margins which constitute the 90<sup>th</sup> percentile of the ranges which amounts to 25%. As an alternative to that, she takes the margin at the 75<sup>th</sup>/80<sup>th</sup> percentile which yields 20%. That is, in contradistinction to, for example, taking the median margin. As it happens, the overall median margin taking the aggregate of all the different comparator datasets is about 14%. See Table A5.8 under paragraph 615 below.
604. Dr Jenkins says that it would be wrong to take the average of all the margins because "this would imply that at least half the firms were earning excessive returns", and that conclusion should not be drawn from the data.
605. The position of Mr Parker and Mr Duckworth is that the average should be used. Mr Parker also points out that any given margin above the average would not necessarily fall to be judged excessive in the Limb 1 sense. There are many reasons why one firm may be able to charge more in a particular market than another. It does not follow that one firm's pricing is necessarily excessive, or that any of them is a precise comparable for SFV services. Further, any excess has to be significant and persistent. For our part, we do not see why the upper bounds approach is required for the particular exercise of ascertaining a reasonable margin. After all, what one is trying to do here is to get a sense from the comparators as to what margin the other companies actually achieve. This is of considerable evidential value, but it does not mean that one has to take the upper bound of the range.
606. In the hot tub discussion and in her report, Dr Jenkins expressed the reason for the upper bound by saying that taking the upper end is reflecting the natural reward for the risks being taken, innovation and investment, and suppliers at this level having judged the challenge well. Mr Duckworth and Mr

Parker disagreed with this. They point out, as is the case, that the question of rewards for innovation and risk-taking are not really relevant here, since SFV Services constitute a mature legacy product.

607. Further, to the extent that it was suggested that the margin should be increased to take account of other factors, such as a general need for caution in the exercise or flexibility, Mr Parker and Mr Duckworth say that these are matters that should more properly be considered in connection with the issue of “significant and persistent” or perhaps under Limb 2. Mr Parker said that if one uses too much discretion at the stage of assessing the reasonable margin, one might reach a margin which makes the costs plus benchmark so high that “anything goes”. We agree with this. It is also consistent with the Commission’s decision in *Aspen*. There, the Commission adopted as the reasonable margin, the median measure of the relevant comparators which yielded a margin of 23%. There was then a separate question as to whether Aspen’s prices were significantly in excess of that benchmark. See paragraphs 132-136 and 139 of *Aspen*.
608. A further justification ventured by Dr Jenkins was that the upper bound was needed to signal to other investors that there were opportunities to earn a return. We recognise that in many workably competitive markets there will be a range of different margin outcomes across different firms, but as noted above, we see the task of defining the reasonable margin benchmark as being to describe the minimum sustainable margin that could justify the continued support from investors in the business concerned. Further, and to the extent that this suggested that there was no previous entry and expansion at all, that is not correct, as there was growing competition from at least 2006, according to Ofcom. See paragraphs 569 and 571 above.
609. In the JES, Dr Jenkins also sought to justify the upper bounds approach on the basis that there were different common costs and demand and supply side relationships within the comparators. However, we do not see the relevance of this, since common costs is separately addressed here and demand-side factors do not really assist on what is a reasonable margin. Dr Jenkins added that the upper bound would “reduce Type 1 errors (over-enforcement),” and assist in the analysis of significance. Of course, one needs to take a careful approach in determining the competitive benchmark to ensure that the approach as to what is a significant excess is not erroneous, and use caution where appropriate. But that does not itself justify an upper bounds model here. Nor do we see how the upper bound approach would assist on the separate question of significant excess anyway.
610. Indeed, the dangers of Dr Jenkins’ approach can be seen by paragraph 599 of BT’s Closing as follows:

“Moreover, in taking an upper bound approach to the rate of return, Dr Jenkins has constructed a Cost Plus benchmark that (as she put it in the hot tub on Quantum) not only “*recognises the dispersion [in prices] by taking the upper end of the distribution of returns*” but “*is capturing some elements of economic value, brand, efficiency, all of those elements*”. Her benchmark thus reflects a price that is *fair*, in the sense that it makes

appropriate allowance for the full range of prices that would be consistent with workable competition and thereby captures the considerations that are relevant to both Limb 1 and Limb 2 of the *United Brands* test.”

611. This is to conflate separate elements of Limbs 1 and 2, and if that is what Dr Jenkins’ approach is doing, then it is not only incorrect as a matter of legal analysis, but it becomes inherently uncertain. The remedy for this is not the dropping of the reasonable margin down to 20% based on the 75<sup>th</sup>/80<sup>th</sup> percentile; it is to remove the upper bounds approach from the Limb 1 assessment altogether.
612. Finally, and as already explained, the upper bounds approach leads to an increase in the common costs assessment within the SAC Combi approach since the relevant costs margin is built into the calculations for each combination. See below.
613. For all of those reasons, we do not accept Dr Jenkins’ upper bounds approach. It seems to us to be sensible to select for consideration an average or a midway point in terms of the outcome of her review of comparators.

#### *Dr Jenkins’ comparators*

614. Dr Jenkins comparators are of two kinds:
- (1) Clusters of companies in industries which can be considered similar to BT Consumer i.e. other telecoms operators (“Similar Industries Cluster”); and
  - (2) Clusters of companies with similar financial metrics to BT Consumer, regardless of the nature of the products (“Similar Metrics Cluster”).
615. Dr Jenkins then compiles tables of results, including all percentiles for each of these sets and then produces an aggregate set of results. This is at Table A5.8 in Annex 5 to HJ1, shown below:

**Table A5.8 Operating Profit (EBIT) Margin for all BT Consumer comparators**

	FY 2013-2022	FY 2013-2017	FY 2018-2022
Min	-98.3%	-94.4%	-98.3%
10th percentile	3.2%	3.1%	3.4%
Median	14.1%	13.7%	14.3%
Mean	13.6%	13.5%	13.7%
75th percentile	19.2%	19.0%	19.3%
80th percentile	21.0%	20.8%	21.4%

	FY 2013-2022	FY 2013-2017	FY 2018-2022
90th percentile	25.0%	24.5%	25.3%
Max	57.1%	53.1%	57.1%
# Companies	133	127	131
# Observations	1215	580	635

616. The Similar Industries Cluster is broken down into four elements. The first two come from the MSCI World Index. MSCI is the investment research company Morgan Stanley Capital International. The

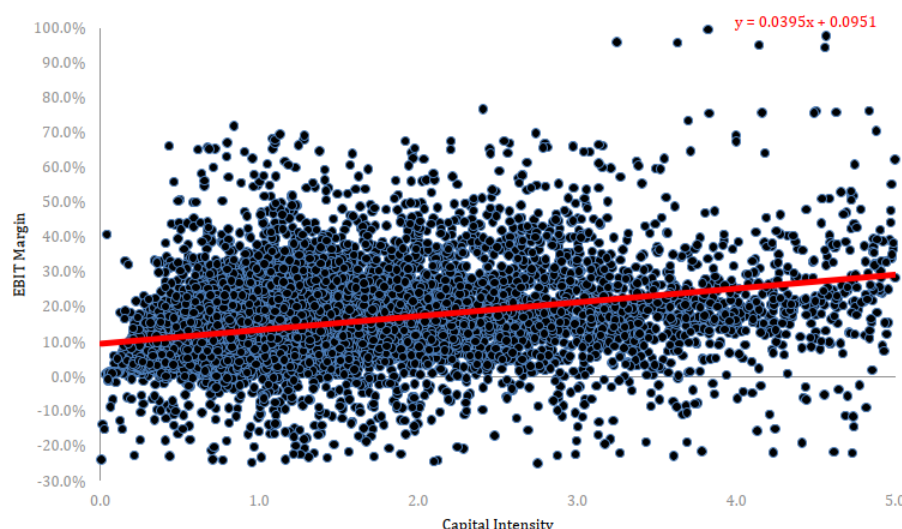
first element is companies within two classifications, being “Diversified Telecommunication Services” and “Wireless Telecommunication Services”. The second element consists of companies within “Diversified Telecommunication Services” only.

617. The third and fourth elements come from the database of Professor Damadoran, who teaches corporate finance and valuation at the Stern School of Business at New York University and provides data on industry averages for US and global companies. The third element consists of companies within his European “Telecom Services” and the fourth element consists of that classification of companies plus “Cable TV”.
618. Dr Jenkins has taken the reported margins of a number of companies that fall within one or more of these elements.
619. For the first element, the reported EBIT margins over the period 2013-2022 or subsets of that period, are drawn from 29 companies. At the 90<sup>th</sup> percentile, the average margins are between 23.2% and 23.9% while on a median basis, they are 16.6-16.7%.
620. The second element relates to 23 companies, themselves a sub-set of the first group of companies. Here the margins at the 90<sup>th</sup> percentile are 23.1% to 24%, with the median being 16.7% to 17.3%.
621. The third element draws margins over the same groups of years from 52 to 55 companies, including major or state-owned telecoms companies in Europe. The 90<sup>th</sup> percentile has a range of 20.9% to 25.7% and the median is 9.3% to 11.3%.
622. The fourth element, which adds in Cable TV companies (on the basis that BT Consumer also supplied TV services) has between 57 and 60 companies, which include those in the third element. On that basis, the margins at the 90<sup>th</sup> percentile were 23.5% to 27.6% and the median was 12.7% to 13.1%.
623. One then turns to Dr Jenkins’ Similar Metrics Cluster. This concerns margins from datasets relating to companies which are said to have similar financial characteristics to BT Consumer, though not in terms of particular products or marketing. This cluster consists of three elements.
624. The first element contains 11 or 12 companies, whose capital intensity is within the range of BT Consumer’s (if one includes EE and Plus net). The 90<sup>th</sup> percentile margin is between 27.6% and 28.9% and the median of 15.6% to 16.9%.
625. The second element contains 17 companies whose ratios of D&A to Opex (operating expenses), lie within BT Consumer’s range of such ratios. Here the 90<sup>th</sup> percentile has margins of 21.9% to 24%, with the median being 10.1% to 11.3%



626. The third element contains 43 or 44 companies whose D&A to Revenue ratios lie within the range of BT Consumer's such ratios. Here the 90<sup>th</sup> percentile yields margins of 24.5% to 26% and a median of 12.3% to 13.6%.
627. As already noted, the results from both clusters are drawn together and aggregated in Table A5.8, shown in paragraph 615 above.
628. As the relevant margins all vary somewhat, depending upon which group of years is being considered, Dr Jenkins has taken the mid-point of the 90<sup>th</sup> percentile, and that gives the 25% margin, which is her starting point.
629. As to all of her comparators, the CR criticises first, the Similar Industries Cluster, on the basis that some of the companies are vertically integrated with high capital intensity, and operate networks as well as retail services. Also, they include capital intensive companies that are not "asset light", as it is agreed that SFV Services in particular, and BT Consumer as a whole, are. Mr Duckworth considers that such companies that own an infrastructure network would need higher margins to compensate their investors for the capital invested in the networks, in addition to the capital employed in the retail part of their businesses. So they would be more likely to resemble returns for BT Group, which includes an asset-heavy infrastructure, such as Openreach. So to that extent, they are not useful comparators because the margins will be skewed upwards.
630. On the point of using comparators with high capital intensity, Dr Jenkins agreed that there is a correlation between capital intensity and margin, but in practice it is not a very strong one. In particular, she said at paragraph 7.2.4 of the JES that firms with low capital intensity can earn a wide range of returns, and while BT Consumer is "asset light", based on the accounting book value of the assets in its accounts, this does not mean that the economic value of its assets on which investors require a return on investment, is low. For example, the book value of an asset may not reflect its current market value and may also omit intangible assets such as brand value, investments in customer acquisition and other economic rights which are not recorded as assets in a company's accounts due to accounting conventions. To support all of this she produced Figure 3, in Section B4f in the Annex to the JES. This "scatter plot", shown below, displays an extremely varied relationship between EBIT margins and capital intensities of a very large number of companies, and a simple regression result that shows the extent to which margins increase with capital intensity. Therefore, overall, she considers that the point about capital intensity has limited force:

**Figure 3 Relationship between EBIT Margin and Capital Intensity for the MSCI World constituents for the period FY2013–FY2022**



Note: Total number of observations: 10,830. Capital intensity is the independent variable, EBIT margin is the dependent variable. The p-value of the slope coefficient is 0 under the null hypothesis that the slope coefficient equals 0. The sample only includes observations for which a value for both the capital intensity and the EBIT margin is available in a given year. I exclude all observations that have a capital intensity which falls outside the range [0,5] and/or have an EBIT margin that falls outside the range [-25%,100%].

631. Mr Duckworth disagreed, on the basis that the scatter plot in Figure 3 could contain asset measurement discrepancies related to book value and discrepancies based on whether brand value was taken into account.
632. Overall, here, we think there is more force in Mr Duckworth’s point about capital intensity than Dr Jenkins would allow, and which is not simply answered by the scatter plot. Indeed the red regression line on the scatter plot shows, on an average basis, a positive relationship between margins and capital intensity, although it is fair to say that no evidence was provided on the statistical significance or robustness of that relationship.
633. So far as the Similar Metrics Cluster of companies is concerned, Mr Duckworth says that the comparators are inappropriate because they are very different businesses and in very different markets (for example, BMW, Nippon Steel and Starbucks). They also include large global businesses which are not asset-light. Also, on the capital intensity comparators, Dr Jenkins has used data from BT Consumer, which includes EE and Plus net. However, EE is vertically integrated as it operates a network, so this would again skew the results.
634. As for the second and third elements within this cluster, which focus on D&A ratios, Mr Duckworth says that D&A does not include any amortisation which is not shown on the balance sheet. Also, there would be a difference in the nature of the assets used and their operational lives, with BT Consumer’s assets tending to be relatively short lived and there could be accounting differences as well. All of that could skew the margins upwards.

635. As to all of that, Dr Jenkins responded that it is usual to take a broad range of comparators which is what competition authorities and regulatory bodies do when trying to work out a benchmark for return on sales. We see that and accept that it is not possible to find perfect comparators. We also think that (as is perhaps inevitable in an exercise of this kind) there are weaknesses in the particular clusters of companies that Dr Jenkins has chosen. This is the corollary of the similar point that we made, and which Mr Duckworth accepted, concerning the dangers of relying on return on sales margins from non-comparable utility companies.
636. As already noted, we also think that comparators drawn from similar telecoms operators in the UK (as Mr Duckworth has selected) are likely to be of more assistance, although they are by no means perfect comparators.
637. In fact, much of the difference between the experts here lies in Dr Jenkins' use of the upper bounds approach, since her median figure is in fact about 14%.
638. One then needs to consider Dr Jenkins' cross-checks. We have already dealt above with BT Consumer's margin in 2009 and the treatment of its margin in the 2017 Provisional Conclusions.
639. However, there are further data-points relied upon by Dr Jenkins. First, she referred to another part of the 2017 Provisional Conclusions where Ofcom stated that rivals' margins for voice customers were similar to BT's - see paragraph 8.21. However, Ofcom also said at paragraphs 8.24 and 8.25 that such figures should be treated with caution, since there was an element of price leadership and issues over data reliability. There could also be an element of price dispersion depending on the quality of the services. Ofcom's own figures were therefore caveated.
640. Dr Jenkins also relied upon Ofcom's estimate of BT's margins for dual play (a competitive market) of 15-20%. However, Mr Duckworth considered Ofcom's approach here was over-simplified. This is because it is assumed that profitability was a combination of profitability per line for voice and broadband, adjusted for BT Sport costs. But that ignored the differences in the mix of services provided to SFV customers and bundle customers, and variations in price. In any event, margins drop significantly after 2017. Again, we see those points but do not consider that such margins were wholly irrelevant. See also the specific reference by Ofcom to 15% in Table A5.14 referred to in paragraphs 600-601 above.
641. Finally, as already noted, one cannot simply rely upon BT Consumer's reported results from 2012 to 2022 (3% to 20%) because this includes the returns on SFVs which are themselves alleged to be excessive. If these returns were adjusted to remove the excessive element (though of course we accept there is something of a circularity here, as noted above), they would be much nearer 10%.

## **Conclusion on reasonable margin**

642. We have taken all of the evidence on margin referred to above into account, giving it such weight as we consider appropriate, recognising that the material before us does not lead to one clear answer.
643. In our judgment, having regard to all the matters discussed above, we consider that the appropriate reasonable margin is 13.5%. In summary, this level of margin lies well below the 25% margin advocated by Dr Jenkins, and her alternative 20% for the reasons described above. It does, however, come close to her median figure of 14%. However, it lies above Mr Duckworth's preferred value of 10%, reflecting the variation that we observe in the margins historically earned by BT's voice business even at times when Ofcom judged it to be operating under conditions of effective competition, along with the fact that the figure of 10% ascribed by Ofcom in 2017 is not really any more reliable than its alternative figure of 15%, and the observation that the [REDACTED] % range of margins projected by Ofcom for competing retailers at the time of the Commitments appears not to have succeeded in encouraging the sustainable development of rival SFV offers. We have, of course, also taken account of the evidence referring to the margins of the comparators used to the extent noted above. The 13.5% is on a percentage of revenue basis, which is how the experts proceeded (the 13.5% margin as a percentage mark-up over costs would be 15.6%).

## **LAW ON COMBINATORIAL AND OTHER TESTING - PPC**

644. In the specific context of combinatorial testing, it is then necessary to refer to the decision of the Tribunal in *BT v Ofcom* [2011] CAT 5 ("PPC"). This was BT's appeal against a determination made by Ofcom in a dispute between BT, on the one hand, and various other communications providers on the other (referred to collectively as Altnets). The dispute centred on allegations that BT was overcharging the Altnets for the provision by it to them of partial private circuits ("PPCs"). It is not necessary to describe PPCs in detail. Suffice to say that PPCs are used to provide access from the site of a particular telecoms customer of an Altnet, often a business, to the BT network. Two particular elements of PPCs (though not both present in all PPCs) are these: first, a terminating segment, which connects a local exchange to which the link from the third party site is connected, to a main BT exchange and second, a trunk element. The latter is required if the Altnet concerned wishes the link from the third party site to go to a particular main exchange other than the default main exchange. The complaints made by the Altnets as to overcharging concerned BT's pricing for these two elements.
645. In its *Review of the retail leased lines, symmetric broadband origination and wholesale trunk segments markets 2004* ("the 2004 LLMR Statement"), Ofcom concluded that BT had SMP in various telecoms markets, including the two PPC elements referred to above. As a result, and pursuant to its statutory powers it imposed a condition obligation upon BT that it must:

“secure and to be able to demonstrate to the satisfaction of OFCOM that each and every charge offered, payable or proposed for Network Access covered by the condition in question was reasonably derived from the costs of provision based on a forward looking long run incremental cost approach and allowing an appropriate mark up for the recovery of common costs and an appropriate return on capital employed.”

(“The Condition”).

646. The 2004 LLMR Statement also decided in principle that financial reporting obligations should be imposed on BT. The nature of these obligations were themselves subject to a consultation process. On 22 July 2004, Ofcom published a final statement and notification entitled “The regulatory financial reporting obligations on BT and Kingston Communications final statement and notification” (“2004 Financial Reporting Notification”). Among other things, this obliged BT to prepare RFSs supported by audit opinions. The broad purpose of the RFS was so that BT could demonstrate (among other things) that its costings complied with whatever cost orientation obligations had been imposed upon it by Ofcom, in relation to the various markets in which it had SMP.
647. The RFSs produced by BT pursuant to the 2004 Financial Reporting Notification included annual Current Cost Financial Statements and Primary Accounting Documents, the latter explaining in detail the accounting principles employed in producing the former. In the context of the RFS used by Mr Duckworth in his methodology to arrive at a competitive benchmark, we shall explore those documents in more detail below. However, in the context of *PPC*, the RFS obligations upon BT included reporting in respect of the two elements of PPC which were the subject of the dispute.
648. The Tribunal in *PPC* distinguished the LRIC of a product from its fully allocated cost (“FAC”). It noted that if a multi-product firm prices one of its products at SAC (thereby recovering all the firm’s common costs) and then charged more than the LRIC for another of its products, there would be an over-recovery of common costs and so the firm would be making excessive profits. The Tribunal then referred at paragraphs 76-78 of the judgment to “contestable market theory”. This states that where there are no barriers to entry, if a firm prices a product at more than its efficient SAC, this will attract other firms to enter the market for that product.
649. The Tribunal then observed as follows:
- “79. Matters become more complex when the fact that firms will often sell many products or services, sharing common costs, is taken into account. For prices to be sustainable in a contestable market, it is then not enough for each individual price to be at or below its SAC, but for each and every combination of services also to be below the efficient SAC for the combination. If this is not the case, while entry to supply only the individual products is not profitable, it may be profitable for firms selling groups or combinations of products with shared common costs.
- (e) The problem of common costs
80. Of course, the theory of contestable markets is just that – a theory – and electronic communications is far from being a contestable market. SAC does, however, give a measure of what a competitive outcome would be in the absence of barriers to entry. As such, it is used as a test for identifying prices that are excessive. In the case of a single product firm, a price significantly and persistently above SAC is to be regarded as excessive and unreasonable.

81. A problem arises in the case of multi-product firms, where it is possible to price an individual product well below SAC, whilst nevertheless over-recovering common costs.

82. Some method of ensuring that common costs are recovered – but not over-recovered – is clearly essential. This was recognised by OFCOM in paragraph A11.6 of Annex 11 of the Determination:

“Because of the existence of significant common costs between BT’s activities, BT will only recover costs overall if at least some of its charges are above LRIC. However, there may be many different ways of attributing these common costs to different services, none of which may be uniquely correct or uniquely reasonable. The maximum proportion of these common costs which it is reasonable for BT to recover from any given service is generally given by SAC, which includes all (relevant) common costs.”

83. In short, whilst it is obvious that if a multi-product firm prices at LRIC it will make a loss (because there will be no recovery of common costs), and if it prices at SAC it will make an unreasonable profit (because there will be multiple recovery of common costs), it is much less obvious how common costs are to be treated.”

650. The Tribunal thus agreed with Ofcom that none of the three approaches for the allocation of common costs, namely, SAC Combi, FAC and DSAC could be regarded as uniquely correct or reasonable. We think that this reinforces the notion that it is necessary to allow flexibility to a firm as to how it recovers its common costs, although that flexibility is not unlimited.

651. The Tribunal then said this about combinatorial tests:

“89. One way of assessing whether a particular charge for a particular product might be regarded as excessive or not, is to consider whether the prices for different combinations of products lie between the LRIC and SAC of those combinations. Where all the different combinations satisfy this test, there is no over-recovery of common costs.

90. A problem with this approach, however, is that depending upon the size of the product portfolio of the firm, and the types of common costs, the number of combinatorial tests could be impracticably high.”

652. In considering the complaint before it, Ofcom used the data contained in BT’s 2009 RFS, as well as data contained in earlier, revised RFSs. As part of its determination, Ofcom considered that BT’s prices for the termination and trunk elements of the PPCs should be considered separately, whereas BT said they should be considered together. The Tribunal agreed with Ofcom on this point.

653. Furthermore, in its determination, Ofcom had used a DSAC approach to see if BT had met its cost orientation obligations. In its 2004 Financial Reporting Notification, Ofcom observed as follows:

“5.67 BT also claimed in its Response that by focussing on DSAC, Ofcom is implying that this is the only appropriate mark-up of common costs when in fact the SMP obligation entitles BT to make “an appropriate” mark-up to recover common costs. However, BT is incorrect to suggest that the DSAC approach only permits one specific pattern of common cost recovery. In fact, it allows for a very wide range of possible sets of mark-ups. The sum of all of the DSACs exceeds BT’s total costs (unlike FAC). Where FAC is used as the cost basis, charges below FAC must be offset by charges of an equal magnitude above FAC in order that incurred costs are fully (but not overly) recovered. This is not true for DSAC, where charges for services can be below DSAC and still allow for full cost recovery. BT could therefore allocate common costs in a myriad of different ways and still price its services in accordance with DSACs...”

5.90 ...[DSAC] allows BT reasonable flexibility to efficiently recover its common costs”

654. Accordingly, Ofcom saw the use of DSAC as giving effect to the need for reasonable flexibility.

655. The DSAC analysis undertaken by Ofcom showed that BT had not met its cost orientation obligations in significant respects, and had indeed charged excessive prices to the Altnets.
656. The Tribunal held that the cost orientation obligations here did not dictate any particular method for the recovery of common costs, provided that it was an appropriate method.
657. For its part (and leaving aside the issue over whether the two relevant PPC elements should be disaggregated or not), BT used 3 different tests to justify its pricing as compliant. These were a combinatorial test, “circuit analysis” and international benchmarks. The latter two tests can be disregarded for present purposes.
658. Although BT’s expert had agreed in cross-examination that his view was probably that combinatorial testing was “a bit of a waste of time”, the Tribunal said this:

“254. As a general proposition, we do not agree with this. As we have described in paragraphs 89 to 90 above, combinatorial tests are one way of assessing whether or not a firm is over-recovering its common costs, and in some cases will be an entirely appropriate approach. The drawback of combinatorial testing, as we have also noted, is the number of permutations or combinations that may have to be undertaken where a firm sells a large number of products/services that share common costs. In some cases – and this is one of them – this purely practical difficulty may render combinatorial testing inappropriate.

255. The problem is simply stated: it may very well be that the price for a single product lies between LRIC and SAC; but that does not mean that the firm is not over-recovering its common costs. As the Determination notes in paragraph 7.118:

“...it would not be sufficient to demonstrate that the charges for an individual service are/were below the (efficient) SAC for that service. The existence of significant common costs requires BT to also demonstrate that those common costs are/were not over-recovered from all the services that share them. Therefore, BT must also undertake a series of combinatorial tests to ensure that each and every combination of services that shares common costs with the service in question (in this case 2Mbit/s trunk) does not lead to an over-recovery of common costs.”

256. Had BT demonstrated an absence of over-recovery of common costs through a series of combinatorial tests, then this would have been an appropriate way of demonstrating an appropriate mark-up for the recovery of common costs. However, at the end of the day, it was common ground that such combinatorial tests as were conducted by BT during the course of the Dispute Resolution Process were insufficient to establish this. The point is very clearly put in the Determination:

“7.120 The exact combinations of services to be considered by the combinatorial tests are determined by the number of other services which share common costs...”

7.121 As we have explained above, the aim of any such combinatorial analysis is to ensure that common costs are not over-recovered. Where all common costs are not shared by the same services, separate combinatorial tests are required for each of the common costs, as well as for combinations of the common costs. Where firms have numerous products and many types of common costs, as is the case with BT, this can lead to a very large number of combinations being required to satisfy the test. For example, with 10 services sharing common costs, there are over 500 combinations. For 11 services this increases to over 1,000 combinations and for 12 services to over 2,000 combinations.

7.122 In its Response, BT reported the results from six different combinatorial tests, based on a range of different combinations of PPC trunk and terminating segment services.

[These were then described.]

7.123 ...all of the combinatorial tests contained in BT’s Response focus exclusively on combinations of services from the three PPC markets regulated in the 2004 LLMR Statement (ie trunk and the two terminating service bandwidths). BT did not provide results for any tests that consider services other than PPCs in its Response.

7.124 If all the common costs that are incurred by 2Mbit/s trunk (as the service of interest) were exclusively shared by the combinations tested by BT, the approach to specifying combinations adopted would be sufficient. However, as BT’s inclusion percentages tables show, the SAC estimates

in all cases include common costs that are shared with non-PPC services...in excess of 75% of BT's SAC estimates in each year consist of trench (effectively duct), optical fibre and transmission equipment common costs, which are shared by numerous other (non-PPC) services."

257. Given the nature of BT's business, inevitably the number of combinatorial tests that would have to be carried out in order to show that BT was only making "an appropriate mark up for the recovery of common costs" would be vast..."

259. It is right to say that, during the course of the Dispute Resolution Process, BT did ask OFCOM what combinatorials it might undertake in order to satisfy OFCOM as to BT's cost orientation. The problem is that – in this context – this was an impossible question to answer, save to say that a very large number of tests would have to be carried out.

260. Ultimately, as we have noted, ... it was BT's responsibility to carry out appropriate combinatorial tests if this could feasibly be done, or (if, as we find, it could not be done) find some other way to demonstrate that 2 Mbit/s trunk charges were cost orientated.

261. The limited combinatorial tests carried out by BT were insufficient to demonstrate that BT had complied with its cost orientation obligation under Condition H3.1. [ie the Condition]"

659. The Tribunal thus rejected BT's combinatorial analysis as inconclusive. However, it approved Ofcom's DSAC approach as follows:

"281. Although there was some suggestion to the contrary in the draft determination, DSAC is not a proxy for combinatorial tests. It operates in a very different way. Whereas combinatorial tests seek to assess cost orientation by what is in effect a properly representative sampling of the prices for multiple products sharing common costs, DSAC distributes the SAC of a broad increment of services pro rata amongst each of the services within that increment. It is very different from combinatorial testing. In particular, it avoids the practical difficulties of combinatorial testing that arise when many products share common costs."

660. It went on to reiterate that combinatorial testing was "simply not practicable here". In passing, the Tribunal noted that had FAC been used, it would have effectively imposed a single price on BT and that was why BT would not have wanted to use it. In the event, the Tribunal dismissed BT's appeal. It also seems to us that, in approving Ofcom's approach here, the Tribunal was endorsing Ofcom's view that there should be reasonable flexibility in the recovery of common costs, as set out in paragraphs 653 - 654 above.

661. In its submissions here, BT drew a distinction between the combinatorial testing undertaken by BT in *PPC* (which involved 6 combinations) and that undertaken by Dr Jenkins which involved 25 combinations for the first period and 24 for the second period. However, this point assumes that if the number of combinations analysed by BT in *PPC* had been somewhat larger, its combinatorial testing would have been satisfactory in the eyes of the Tribunal; but that does not follow, because in *PPC*, the Tribunal endorsed the proposition that if combinatorial testing was to be undertaken in that case, it had to be done across all combinations of all relevant products (i.e. all the products that shared the same set of common costs). With a firm like BT, and in the context of *PPC*, that was simply impracticable. On the other hand, the exercise might not be impracticable in respect of a firm which had only 2 or 3 products.

662. In our view, therefore, and in the context at least of BT in that case, the Tribunal was indeed saying that combinatorial testing can be impracticable where large combinations of products are involved



and it so found in that case. Although the relevant set of products that shared common costs with SFV Services is not the same as those wholesale products sharing the same common costs in *PPC*, which included the terminating and trunking segments, the risk of impracticality remains. We therefore consider that *PPC* is a relevant case when it comes to assessing the appropriateness or otherwise of Dr Jenkins' SAC Combi analysis, as discussed below.

## **ANALYSIS OF THE RFS METHODOLOGY**

### **Introduction**

663. As set out above, and save on the question of direct costs, the methods employed by Mr Duckworth on the one hand and Dr Jenkins on the other, to reach a competitive benchmark are very different. Each model has been formulated and explained in considerable detail.
664. That said, in oral closing arguments, Mr Beard KC somewhat downplayed the significance of Dr Jenkins' SAC Combi test by characterising it as simply a sense-check to show that the RFS method was clearly wrong.
665. While we must consider these competing methods in detail, we do accept the proposition that if the RFS methodology is fundamentally or inherently defective, then the CR's case on Limb 1 is not going to be "saved", as it were, because the SAC Combi methodology is also defective. This observation recognises therefore that the CR has the burden of proof.
666. On the other hand, we also recognise that in relation to a number of arguments deployed by BT as to the inadequacy of the RFS methodology, it is important to ascertain whether such arguments are essentially speculative in circumstances where BT, had it so wished, could have adduced evidence of its own on the point but did not do so. We refer to this in paragraphs 676, 693, 703-704 and 715 below. Indeed, the CR invites us to draw appropriate adverse inferences due to the failure of BT to adduce relevant evidence - see paragraph 371 of its Closing. We do not think it necessary or appropriate to draw adverse inferences as such from the absence of such evidence. The simple point is that BT could have adduced relevant evidence and it did not, so such evidence is simply not there.
667. For the above reasons, it makes sense, first to consider the RFS methodology and the criticisms made of it and then, in the light of that, the SAC Combi methodology.

### **Objection as a matter of principle to the RFS model as an appropriate way of calculating a competitive benchmark as at 2009**

668. BT's criticisms of the RFS methodology fall into two distinct categories. The first contains arguments to the effect that even in the context of 2009, the RFS model is wrong in principle. The second is that even if it is broadly appropriate as at 2009, it cannot sensibly be "uprated" by the CPI index, so as to produce a competitive benchmark for the years of the claim period.

669. At this stage, we deal with the objections in principle to the RFS methodology altogether. There are essentially two:

- (1) the RFS model is expressly based on the concept of FAC which is itself inappropriate here; and
- (2) the purpose for which the RFS was required is (too) different from the purpose of ascertaining a competitive benchmark in the present context, so that it is of no or no sufficient use.

*Use of an FAC model*

670. The RFS's methodology is a form of LRIC+ model, using FAC as a workable proxy for LRIC+. It was designed to achieve such an outcome for each of the relevant services, and it says as much. Thus far, we did not understand BT to be in disagreement. Like the SAC Combi method, FAC was sensitive to the need to have common costs, as well as all genuinely incremental costs, attributed to the relevant service. Both models are designed to ensure that common costs are recovered (but not over-recovered) across all relevant services (see paragraph 6.63 of HJ1).

671. However, BT contends that an FAC model is not appropriate here, because, while it will ensure that common costs are not over-allocated (and therefore over-recovered), it imposes an arbitrary rule as to how those common costs should be recovered across the services that share them. Such an approach is unduly rigid because it does not reflect the more flexible way in which common costs are recovered in workably competitive markets. The level of such contribution depends on that service's revenue - how much of it (after discharging direct and indirect costs and an allowance for a margin) was actually available to discharge part of the common costs; see, for example, paragraph 6.65 of HJ1.

672. As against that, the CR says that first, the level of profit of BT Consumer Services other than SFV Services is not relevant when setting a benchmark to see if SFV Services prices were above the costs of production. Taken by itself, we think that this answer is too prescriptive; we see no reason in principle why there should not be a degree of flexibility in terms of how a business recovers its common costs.

673. In this regard, paragraph 338 (a) of the CR's Closing says this:

“BT and Dr Jenkins criticise Mr Duckworth's use of a FAC approach, based on the BT RFS, on the basis that it “does not allow for an assessment of whether the firm actually recovered (or over-recovered) its common costs across all services”. That criticism is unfounded:

(a) Applying the FAC standard to SFV Services does not explicitly assess the level of common cost recovery across the wide range of products offered by BT. However, the level of profitability of BT Consumer services other than SFV Services is not a relevant factor when assessing whether SFV prices are above the cost of production...”

674. We do not think that the position is as stark as that. It is reasonable to argue that the profitability of unconnected business activities should not be a factor that determines the reasonable profits of SFV

Services, but that criticism does not apply where the different services in question share common costs. In this scenario, the different businesses are inherently connected, and so the profitability of other products can be a relevant factor. For example, to take a variant of the coffee and cake shop example posited by Mr Parker at Day 13/79-82, Mr Parker is right to observe that if the cake supplier failed to deliver cakes to one particular shop in a particular week it would hardly justify increasing the price of coffee in that shop in order to pay the rent for that week. However, if cake wholesale prices go up so that retail margins earned by all shops become very tight on that product, it is quite plausible that a market-wide cost shock such as this could affect the competitive equilibrium and the margins that shops need to charge for coffee in order to sustain the continued existence of the sector. How much the price of coffee could be increased would depend on how consumers reacted to the increase in prices for both cake and coffee, but the fact is that the common cost across the two products make their pricing interdependent.

675. We accept that there should be flexibility in the recovery of common costs from a particular product. On the other hand, this cannot be a licence for what would amount to cross-subsidisation. See paragraphs 111 - 112 above. Indeed, this is precisely what the CR says BT has done here, using the excess profits from SFV Services to fund quite separate products, such as BT Sport. We deal with the question of BT Sport below, but the point to be made here is that in this context, we would restrict the notion of a cross-subsidy to those cases where one product is being subsidised by another where the price of the former is itself below its incremental cost. The fact that there is no cross-subsidy, strictly so called, of course, does not mean that there might not be an unacceptable level of common costs recovery from one particular product.
676. The CR then makes a separate point about the appropriateness of the FAC exercise in this case. It is that this exercise was undertaken by BT itself in the RFS, albeit that it had been required to produce RFSs as a matter of regulation. Incremental costs were attributed on a costs causality basis with the remainder which could not be so attributed, allocated on a “fair” basis. BT does not suggest that the particular approach, taken by itself, in giving effect to the fairness requirement in the RFS was somehow inappropriate, and the CR is entitled to assume that it was not. This is an example of where BT could have adduced evidence on the point had it wished to do so, but it did not. Subject to the separate point about the particular context of the RFS (dealt with in paragraphs 692 - 694 below) it is very hard to see why this particular manifestation of a FAC, carried out by BT itself in considerable detail and accompanied by an auditor’s opinion, should not be considered as at least an appropriate method of allocating common costs. This is of course subject to BT’s more general point about the need for flexibility in how common costs are to be recovered, as already noted. We return to the limits on such flexibility in paragraph 685 below.

677. A further point made by the CR in various contexts is that BT did not incur a significant amount of common costs anyway in order to provide SFV Services, in which case particular concerns about the way in which common costs are recovered becomes much less important. We deal with the factual point made here in paragraphs 761 - 777 below. But in any event, we do not consider that this would entitle the CR to disregard altogether issues of principle concerning the recovery of common costs.
678. However, it does seem to us that Dr Jenkins' criticisms here could only have real weight if it could be demonstrated that there is some workable alternative that does fairly or appropriately take into account the contribution to common costs actually made by the other services. Here she relies on her SAC Combi method. But as we point out in paragraphs 781 - 856 below, there are difficulties with it.
679. Overall, we do not accept that just because the RFS methodology adopts a FAC approach, this renders it inappropriate as a matter of principle for deriving a competitive benchmark.
680. In addition, the CR says that there cannot be unbounded flexibility conferred upon BT. This is because the emphasis is on ascertaining the costs "reasonably attributable" to the product in question, not other products; see *Albion Water II*, referred to in paragraphs 60-61. Further, it points out that the case law referred to in paragraphs 110 - 111 above shows that the emphasis is on the product in whose market the business has a dominant position, because it has a special responsibility to consumers there. Practices which suggest true cross-subsidisation must be carefully examined.
681. In Section 4.2.3 of DM1, Mr Matthew says that Ofcom itself had noted that where there are significant common costs, causing prices to be tied to FAC can be unduly restrictive. He relied on three particular Ofcom documents. In the case of two of the documents, and as pointed out by Mr Duckworth in cross-examination, the context there was quite different, dealing with wholesale prices where there were very large common costs, and where Ofcom had imposed a price-cap. There was also a costs orientation provision which prevented a disproportionate recovery of fixed and common costs. In the case before us, of course, there is no relevant price cap.
682. The third document relied upon by Mr Matthew is the VULA Margin Statement. At paragraph 5.127, Ofcom stated as follows:

"5.127 As we have previously set out, the total fibre portfolio approach provides BT with the flexibility to determine the margins on individual products within the portfolio. We consider that flexibility is particularly desirable given two aspects of the VULA margin assessment. First, fibre services are still developing, with various technologies such as G.FAST likely to increase speeds. Second, since we consider that a LRIC+ standard should be applied (see paragraphs 5.54 to 5.56) flexibility would allow BT to determine what contribution to common costs (i.e. the 'plus' in the LRIC+ calculation) is made by different products. Such flexibility would allow BT to experiment when setting the relative prices of different superfast broadband products and to respond to differences in consumer demand for different superfast broadband packages. By contrast, we considered that the limits on BT's flexibility under the both the fibre product group approach and

the individual product approach would on their own mean that each of these are disproportionate when compared to the total fibre portfolio approach.”

683. We see that, but the flexibility there was limited to products within the superfast portfolio (being the portfolio regulated). BT was not permitted to extend this flexibility into other BT products.
684. Having said the above in respect of those three documents, we are conscious of the *PPC* case where (as noted in paragraphs 654-660 above) Ofcom’s approach to cost-orientated prices, which was ultimately endorsed by the Tribunal, did involve an explicit desire to allow some flexibility in common cost recovery.
685. A further point made by the CR is that in any event, in conditions of workable competition, a multi-product company would not be able to exercise too much flexibility in terms of how it recovers common costs. This is because if, notionally, it set a particularly high price for one product because it wished that product to make a large contribution to common costs, the market would not tolerate it. Competitors would move in with significantly lower prices, precisely because they had chosen not to require their prices to cover a large amount of common costs.
686. During the exchanges between the experts at the hearing, Mr Parker noted that firms operating in competitive markets faced the problem of how to recover common costs across multiple products all the time, citing the example of a supermarket that had to earn margins on various different grocery categories in order to recover the common cost of the land on which the store and its car park were sited. He argued that the competitive process defines how such costs are recovered, and that one does not observe what he described as an ‘anything goes’ approach to common cost recovery, in which any single supermarket would choose to recover all its common costs on the sale of just one product category. He argued that a supermarket that sought to do so would face an adverse reaction from consumers who would, given alternative competitive options, choose to buy the grocery category in question from a rival store.
687. Dr Jenkins did not disagree with this particular example, but claimed that in practice firms in this position would nevertheless exercise considerable flexibility in the margins they charged for different categories, depending on a variety of factors including the different competitive pressures they faced across their product portfolios. She did not accept that there was a rigid price-cost rule that could determine how such common cost recovery should or would occur in workably competitive markets.
688. Mr Parker did not agree with this notion of pricing flexibility, and argued that his preference for a more deterministic outcome was supported by an article written by Christopher Bliss in 1988 entitled “Theory of Retail Pricing”. The reference to this article emerged here, only in the course of the JES discussions. At that stage, the point he was making was that in a competitive market, one

would expect to end up with only a single competitive benchmark, as opposed to a range. This is expressed in the JES at paragraph 7.3.1 and in the references to Professor Bliss' article.

689. There was some discussion in the hot tub discussion between, in particular, Mr Parker and Dr Jenkins, about the article, which showed that common cost recovery under competitive conditions would proceed on the basis of a version of so-called 'Ramsey pricing'. Specifically, this predicts that margins for individual products will vary in inverse proportion to the demand elasticity for each item, subject to the added complication that the inter-relationships between products must also be taken into account (a factor referred to as the need to account for the "super-elasticities" of each product).
690. However, we do not consider that Mr Parker's introduction of the Bliss article at a rather late stage in the debate between the experts provided much clarity. We certainly would not see it as a basis for saying that multi-product firms must charge identical price-cost margins across all the products that share a common cost, or that there cannot be a range of possible competitive benchmarks. As was observed in the experts' discussion of supermarket pricing, competitive market outcomes can exhibit a variety of price-cost margins. However, we do think that there is force in Mr Parker's observation that, in a competitive market, there is likely to be a limit to the ability of a company to price in too much of the common costs. Of course, in a market which is not competitive and where the relevant company is dominant (which is the case in the SFV Services market) there is a danger that the company can do precisely that. If so, this does not necessarily mean that the recovery of common costs with that effect is automatically fair or reasonable for the purposes working out what a competitive benchmark should be for Limb 1 purposes.
691. Overall, and for the reasons given above, we do not consider that the RFS model is inappropriate *per se* on the basis that it is too inflexible so that it should be rejected out of hand.

#### *The Regulatory Purpose of the RFS*

692. The second point, although it was not clear by the end of the trial to what extent it was still pursued, concerns the purpose of the RFS. Of course, it was required by Ofcom in the exercise of its statutory powers and on the basis that BT had SMP. It was also in a context where BT was still prevented from offering bundles, although that was about to change. However, we do not see that this context by itself rules out the RFS methodology. After all, BT chose the particular attribution methodologies used, which in any case could hardly be described as controversial or arbitrary i.e. a FAC model and, in relation to indirect costs, the application of the principle of costs causality with the remainder of the costs allocated on a fair basis.

693. Yet again, if BT had wished to adduce particular evidence to show how the output of the RFS was specifically inappropriate to be used as a template for pricing in this context, it could have done so. It did not.
694. So there is nothing in this further point.
695. For those reasons, there is no basis for ruling out the RFS methodology *ab initio* because of the regulatory context, either.

### **Objections to the use of the RFS methodology in respect of the claim years**

#### *Introduction*

696. We therefore turn to the second broad reason given by BT for rejecting the RFS methodology, namely that it cannot sensibly be uprated in the way chosen by Mr Duckworth, so as to constitute relevant figures for the claim years. We refer to this as the Timing Point.

#### *The use of “actual data”*

697. BT initially submitted that as a matter of law, the RFS methodology could not be used because its data was from 2009 and what was required was “actual data” from the claim years.
698. In this context, Mr Beard KC relied on the reference to “costs of production” and “actual costs incurred” in *United Brands*, referred to at paragraph 43 above. This was not to suggest that there has to be absolute precision in the costs model used to determine the competitive benchmark, but that it should be based on the actual underlying costs of the company at the relevant time. As the RFS model did not do this, its application was contrary to *United Brands* and wrong in law (see Day 26/161).
699. Just pausing there, we do not consider that this can possibly be right. After all, the later cases referred to in paragraphs 46-73 above stressed that there was no single correct method and it was permissible in theory to use comparators instead of the dominant undertaking’s own costs. Indeed, to be fair to Mr Beard KC, he did not labour this as a point of law. His alternative contention was that in any event, there was no sense in which the RFS model captured BT’s actual data for the relevant period on the facts, as it were; nor was there any form of cross-check with the actual data available undertaken by Mr Duckworth. In those circumstances, the RFS model could not succeed here.
700. As to this, the first point concerns what is meant by “actual data”. From BT’s perspective, it is perfectly true that Dr Jenkins used BT’s actual costs data for the relevant period, but at a much more general level, namely the indirect costs of BT Consumer as a whole, of which SFV Services only formed a relatively modest part, something like 18% of the revenue of the business in 2015/16, and decreasing thereafter. See paragraph 558 above. The whole question was then how to extrapolate the relevant costs for SFV Services. On the other hand, from the CR’s perspective, his starting point

was a set of actual costs for BT's voice services in 2009 (i.e. from the relevant market), but they had to be updated. It is very hard to see why the former method is permissible in principle, but the latter is not. Again, Mr Beard KC later accepted that he could not say that there was an absolute bar to using pre-claim data; rather it was a question of how the updating was done.

701. In that context, he did make the point that there should, on any view, have been a cross-check with BT Consumer's actual data for the claim period. Mr Duckworth accepted that he did not do so, but he explained that this was because it would not have been a useful exercise. That is obviously because, again, the BT Consumer costs were not themselves the relevant costs. We refer to some more detailed submissions by BT on the size of the indirect costs in the claim period, in paragraphs 710 - 737 below.
702. This leads on to another general point. The position of Mr Duckworth (and Mr Parker) is that because there was no specific costs data in relation to SFV Services for the claim period, they had to look elsewhere, and that is where the RFS for 2009 came in. BT informed the CR that it did not have specific costs data for the SFV Services. It is perfectly true that there was a very substantial amount of disclosure from BT on the question of costs. However, it was not suggested - nor could it be - that this opened the window, as it were, to indirect costs information that was specific to SFV Services. Had it done so, no doubt Dr Jenkins would have availed herself of it. So, BT's argument that the CR somehow wrongly failed to make use of relevant disclosure does not hold water. There is ample evidence that BT did not maintain appropriately granular records for SFV Services as opposed to BT Consumer.
703. On the other hand, there was nothing actually stopping BT from producing, admittedly after the event, some more focused analyses that did drill down into the indirect costs that could be said to relate to SFV Services. This was by no means an impossible exercise. First, as it emerged when the evidence about "unit costs" from Mr Cackett was explored in detail at the hearing, it turned out that some "rough and ready" P & L accounts for voice services did exist, although not in any formal way. But this suggests that it was at least possible to do work towards that end. In its s135 response to Ofcom in 2017, BT estimated that it would take approximately 2 months' systems development work, at a cost of £120,000, together with an operational headcount for 3 months at £60,000, plus a further financial management cost of £80,000, to create retail reporting on SFV Services using BT's then accounting system. Given the sums at stake here, such an exercise might be regarded as involving only modest costs and not disproportionate. Indeed, it transpires that BT is now working towards a model of that kind but it is forward-looking only.
704. Clearly, the only party which could have produced that information was BT. It did not do so. That is its right, but in those circumstances, it cannot be said that Mr Duckworth's decision to use an



alternative model in the absence of specific information pertaining to SFV Services was unreasonable. The real question is whether that alternative model is helpful, and if so, to what extent.

### *Legal Certainty*

705. BT contends that the use of the RFS model, based as it is on 2009 data as the starting point, violates the principle of legal certainty. This principle was referred to by the Court in *Deutsche Telekom AG v European Commission* ECLI:EU:C:2010:603. Here, the context was the importance of carrying out a price/costs test using the dominant undertaking's own data, rather than that from a different firm. In particular, the Court said at paragraph 202 that using the former data was:

“consistent with the general principle of legal certainty in so far as the account taken of the costs of the dominant undertaking allows that undertaking, in the light of its special responsibility under Article 82 EC, to assess the lawfulness of its own conduct. While a dominant undertaking knows what its own costs and charges are, it does not, as a general rule, know what its competitors' costs and charges are.”

706. However, that point only goes so far in this case for three reasons. First, the data used by Mr Duckworth was indeed BT's own data, albeit from 2009. Second, had BT wished to undertake a “meaningful self-assessment” as Ms Kreisberger KC put it, it could have done so. And after all, BT was on notice and from January 2014 of Ofcom's interest in its rental prices. While the RFS of 2009 did not relate to the years in question, or the putative years ahead, when BT might wish to ascertain whether it was at risk of abusing its dominant position, it had the wherewithal to make adjustments to it going forwards, if it wished to do so.

707. Third, given the complexities and drawbacks of Dr Jenkins' SAC Combi model (discussed below) it is far from clear that its operation is any less uncertain than that of the RFS model.

708. We should add that the principle of certainty invoked by BT here is all in the context of the application of the Limb 1 test to particular facts. It is not about the underlying principles themselves. We fully accept that the principles should be clear and certain. That is why, for example, any upwards deviation by the dominant undertaking from the competitive benchmark must be “significant and persistent”. But we are not dealing with the adequacy or otherwise of the underlying legal principles under Limb 1, here.

709. Accordingly, we do not consider that the EU principle of legal certainty renders the RFS model deficient.

### *Use of the CPI Index and reported indirect costs before and as at 2009*

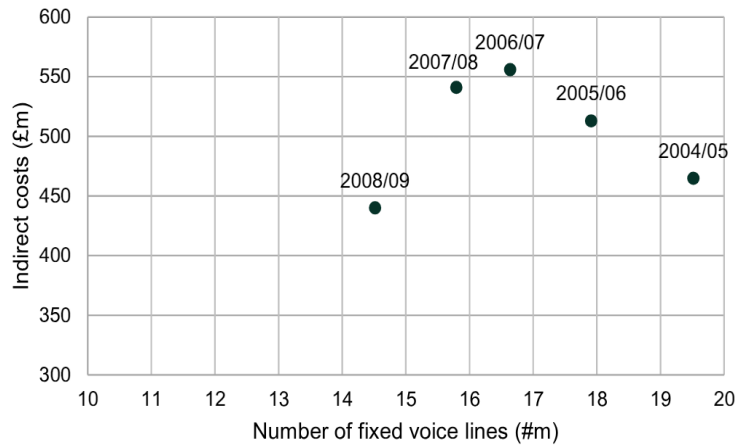
710. The tool used by Mr Duckworth to project the results of the RFS forward to the claim years is the CPI Index. It is hard to see why doing this (as opposed to some other method of uprating) could be wrong in principle. In fact, Dr Jenkins accepted that she did not have a better index to use and would not recommend a different one; rather, it was that any index would not capture what actually happened to indirect costs going forwards (Day 13/125-126). Quite so, but then the question is what

can be drawn from the available data about possible increases (or decreases) in indirect costs for SFV Services. We refer to the pre- and post-2009 costs data below.

711. First, however, it is necessary to deal with why Mr Duckworth says that in fact, his model, based on the use of the CPI Index, is itself conservative. He says it is because of the likelihood of cost efficiencies being made going forwards from 2009, which Mr Duckworth has not taken into account as such. As to this, there is specific evidence that BT conducted a Consumers Cost Transformation Programme with the aim of reducing costs and increasing efficiency. In particular, BT stated that there was a costs saving of £104m in terms of SG&A between 2008 and 2009, related to voice services.
712. There were also costs transformation efficiencies reported by BT between 2010 and 2012 although this was now in relation to BT Retail (of which BT Consumer is a part) as a whole. The cost reductions were reported as £299m, £339m and £262m in the years 2010, 2011 and 2012 respectively. See Table 18 in MD1.
713. In addition, Mr Cackett said in evidence that BT Consumer expected to make efficiency gains each year (Day 8/185). This was reflected at page 17 of BT Retail's Operational Review of September 2009 which said that it was continually striving to improve efficiency and reduce costs.
714. As to the making of costs efficiencies, BT submits that it does not follow that every intended cost efficiency would succeed; and when asked in re-examination whether BT Consumer always made the cost efficiencies which it had forecast, Mr Cackett answered, perhaps unsurprisingly, not always. In addition, Mr Duckworth accepted that he had used BT's 5 year MTP from 2020 which had expected a 5% reduction year-on-year. He did not know if, in fact, that reduction had been achieved and he had not undertaken an explicit forecast of the intended efficiency gains. But he added that he thought the MTP was informative as to expected efficiency gains, and was not merely aspirational. (It was also put to him that Mr Cackett had said that the plans were "often not met"; actually he said that they were not always met - see above.)
715. We follow all of that but there is no specific or detailed evidence from BT on areas where particular planned cost efficiencies had in fact failed. It could surely have been produced easily.
716. So in truth, we see little reason to doubt that in general terms, some form of cost efficiencies were being made by BT over the relevant years which affected SFV Services. As already noted, Mr Duckworth did not take the making of cost efficiencies into account directly, but what he did was to invoke this point as a rebuttal of certain points against his use of the CPI Index, made by BT. We deal with those matters in context below.

717. At this stage, we should make reference to Figure 5.4 of HJ2. This shows the total indirect costs for BT's residential fixed voice services, as disclosed in the RFSs for the 5 years up to and including 2009.

**Figure 5.4 Relationship between the indirect costs attributed to residential fixed voice services within the RFS and the number of BT fixed voice lines**



718. The fall of over £100m between 2008 and 2009 could be seen as a reflection of the £104m cost saving referred to in paragraph 711 above. On the other hand, and as BT points out, indirect costs were rising significantly in the earlier years shown in Figure 5.4 despite the fact that customer numbers were falling steadily. Dr Jenkins thus questions why Mr Duckworth's starting point should be 2009, since there were RFSs from previous years available, though showing higher costs. She suggests that this is therefore an arbitrary starting point, quite apart from the correctness or otherwise of using the CPI Index as a way of ascertaining costs going forward beyond 2009. We accept that it is problematic to base a forward projection on just one data point where there is considerable year-on-year variation in this data point in the prior years. However, we think that there are two countervailing factors here. First, it remains the case that 2009 is the closest available data set to the claim period. Second, if costs savings were indeed being made as from 2006 (and were expected to continue as a trend), that suggests that 2009 is not an inappropriate starting point. As against this, Mr Beard KC argued that if one assumes that indirect costs were going up by the CPI index each year, then that approach would fall down if one attempted to "back-calculate" the CPI index increase from 2009 to 2008 and 2007. This is because the result of such a back calculation would be that the 2007 and 2008 costs would each be taken to be less than the costs for 2009, yet we know that in fact they were more. See Figure 5.4. Hence, he argued, the exercise of starting from 2009 is necessarily arbitrary. We do not agree because, again, we think that there is sufficient in the materials to show that costs efficiencies were being made in the two years prior to 2009.

719. Overall and for the reasons given above,

- (1) while we accept the need for caution in using the single data point of 2009, we do not agree that it falls to be rejected entirely, and
- (2) as for the use of the CPI index *per se* (i.e. without looking at other matters), the CPI index does seem to us to be conservative, and in any event not arbitrary.

*Indirect Costs Data from 2015/16 going forward*

720. However, it is then necessary to consider the indirect costs data from 2015/16, which of course is shown only in relation to BT Consumer as a whole. The relevant figures, drawn from Tables 4 and 5 of the letter from S & S dated 18 February 2024 (“the February Letter”) are set out below. They also appear in the Table at paragraph 558 above.

£m	2015/6	2016/7	2017/18	2018/19	2019/20	2020/21	2021/22
Total Revenue	4,373	4,676	4,709	4,682	4,486	4,114	4,253
Total Costs	3,564	3,887	3,988	3,982	4,114	3,988	3,815
Costs of Sale	2,580	2,912	2,963	2,911	2,885	2,748	2,837
Actual Indirect Costs total	983	975	1,025	1,071	1,229	1,240	1,261
Of which: SG&A	782	774	819	838	948	957	978
D&A	201	201	206	233	281	283	n.a

721. This shows (among other things) that BT Consumer’s actual indirect costs did increase somewhat from 2017/18, and more significantly as from 2019/20. In addition, Dr Jenkins noted at paragraph 5C.3 of HJ2 that there were significant increases in SG&A costs of BT Consumer between 2012/13 and 2015/16 being from £600m to £782m.
722. BT points out that these increases would have exceeded Mr Duckworth’s CPI Index, and significantly more so, in the later years. It makes the broad point that this shows that costs did indeed increase, notwithstanding the supposed costs efficiencies. We see that, but the difficulty is that it is not possible to say how much of those increases in indirect costs can be attributed to SFV Services.
723. Mr Duckworth’s approach was to say that the indirect costs figures, of course, included incremental costs and common costs. One would not expect common costs to increase suddenly, unless there were changes to the outputs. So cost increases linked to expanding output to deliver, for example, triple play (TV, broadband and voice) would not be concerned with the costs of production of SFV Services; rather they would be incremental to those other services that caused them, not to SFV Services. Mr Parker added that one explanation for the increased SG&A costs overall may have been the provision of more bundles (as was undoubtedly occurring), and marketing aimed at that

product. The same could be said of the creation and promotion of BT Sport. So none of this shows that the indirect costs which could properly be allocated to SFV Services were themselves going up.

724. As a counter to this, Dr Jenkins said that in fact there were substantial changes to the design of call packages (as set out in paragraphs 11-50 of JB3) and all of these would require central office support, product design and development which would affect common costs across the board. In the course of the hot tub discussion on these points (see Day 14/107-120) Dr Jenkins said that money was being spent on, for example improved billing services, the “onshoring” of customer care and improving the BT brand generally. All of these were elements of SG&A that would be relevant across the board i.e. SFV Services, along with other elements of BT Consumer. She thought there were too many examples of things that were changing, and that meant that BT was very likely spending as much on their fixed voice customers as on the bundle customers. She said that more work on the actual costs that were incurred would have to be done to be able to say that none of them were relevant to the SFV Services Group. We see that, but then it is BT which would have the information to undertake such further work.
725. We also think that there is force in Mr Duckworth’s point that essentially, SFV Services were the same “legacy” product year-on-year. There was not the same kind of technological shift as for bundles (for example the move to superfast broadband) or investment in television. And after all, this is where BT was facing its most direct competition.
726. Overall, on this point, we thought there was more force in Mr Duckworth’s view than that of Dr Jenkins which we found to be somewhat speculative. Of course, BT could have provided examples of increases in SG&A that related to SFV Services as much as other elements of BT Consumer, but it did not.
727. Dr Jenkins added that the costs of providing BT Sport were not indirect costs anyway - see Day 14/114-115. As to that, we do not think that this can be correct across the board, because there must have been some indirect costs in relation to BT Sport as opposed to the direct costs of delivering it.
728. At this point we should deal with the fact that according to BT, the way in which it classified its SG&A costs changed as from 2019/20, but with alternative figures being given for 2018/19 as well. As already noted, and as can be seen from the table at paragraph 720 above, such costs increased significantly as between 2018/19 and 2019/20. The common costs which Dr Jenkins derived from such SG&A costs similarly increased, from £427m in 2018/19 to £548m in 2019/20.
729. In its letter dated 30 November 2022, S&S explained the matter thus:

“...The SG&A calculations represent the total of all of BT Consumer’s direct SG&A costs plus an allocation of fixed overhead costs, or recharges, from other BT cost centres, such as the Technology Service Office (now subdivided into Networks and Digital) and Corporate Units.

In FY 2019/20, BT amended the methodology it used to recharge fixed overhead costs to its Customer Facing Units (“CFUs”), including BT Consumer. As set out further in the enclosed 2019 paper from BT’s Audit and Risk Committee outlining the proposed changes to BT’s methodology for recharging fixed overhead costs to its Customer Facing Units, the amendments reflected the fact that changes to BT’s trading dynamics and organisational structure (e.g. the merger with EE, the creation of the Consumer and Enterprise Units, the formation of Openreach Limited, and further transfers of accounts between Global Services and Enterprise) had significantly changed the structure of the business and therefore changed the relative size and scope of the CFUs and their use of Technology Unit (“TU”) and Corporate Unit (“CU”) assets and resources. In addition, it was found that some Technology assets were no longer used by, and should not be allocated to, Openreach. Overall, BT considers that the changes more closely aligned the percentage of BT recharges received by each CFU with their percentage share of BT earnings (as measured by EBITDA).

As a result of the above, there is a variance in the SG&A figure for FY 2018/19 in the BT P&L Tables tab (I57) and the SG&A figure in the SG&A Breakdown tab (K23). Following the change in recharges methodology, BT issued restated FY 2018/19 annual accounts in accordance with the new methodology. The figure in I57 of the BT P&L Tables tab is based on data in the original annual accounts for FY 2018/19.”

730. Some further detail is then given in the attachment to that letter, which is a paper from BT Group Finance dated April 2019 (“the 2019 Paper”). It states, among other things, as follows:

“1. The purpose of this paper is to update the Committee on a proposal to amend the methodologies used to recharge fixed overhead costs reported within EBITDA. These changes would impact the Group’s external segmental reporting.  
 2. We have undertaken this review of internal recharging at this time because:  
 i. Recent changes to the Group’s trading dynamics and organisation structure (e.g. Creation of Consumer and Enterprise Units, formation of Openreach Limited, further transfers of accounts between Global Services and Enterprise) have changed the relative size/scope of Units and their use of Technology and Corporate Unit assets and resources. With the exception of a limited refresh for the addition of EE in 2016/17, the Technology and Corporate Unit asset and cost allocations had not been revised for at least 5 years.  
 ii. Based on a detailed review of operational assets early in 2018/19, we identified some Technology assets (MSAN & TDM) that are no longer used by, and should not be allocated to, Openreach in either the RFS or financial accounts.  
 Subject to BARC approval, we would implement the proposed changes to internal recharges in the financial accounts and external segmental reporting starting in the 2019/20 financial year.  
 3. The proposed changes would more closely align the percentage of Group recharges received by each CFU and their percentage share of Group EBITDA generated.  
 4. The proposed changes would also more closely align the Openreach internal recharges in the Annual Report and Accounts (ARA) and the Regulatory Financial Statements (RFS). The current EBITDA difference between these two reports is £575m (based on proforma 2017/18); these proposals would reduce this to £236m.  
 5. A detailed review of all recharge elements has highlighted a need to (i) update a number of calculation input values and (ii) revise calculation methodologies to better align to the current trading dynamics and organisational operational structure of BT, in particular with the consolidation of CFUs...”

“• Openreach currently accounts for 49% of the Group’s recharges and 33% of Group EBITDA. The proposed allocation reduces recharges to 36%, increasing the share of Group EBITDA to 37%.  
 • Consumer currently accounts for 30% of the Group’s recharges and 34% of Group EBITDA. The proposed allocation increases recharges to 36%, reducing the share of Group EBITDA to 32%...”

The higher Consumer percentage of recharges (36%) to EBITDA (32%) vs the other CFUs is primarily due to the inclusion of mobile network costs in the Technology recharges.”...

“9. The proposed changes would more closely align the Openreach internal recharges in the Annual Report and Accounts (ARA) and the Regulatory Financial Statements (RFS). The current difference in internal recharges in EBITDA between the ARA and RFS is £575m (based on pro-forma 2017/18 accounts); the proposals would reduce this difference to £236m. The residual £236m is largely due to different approaches to the allocation of property and technology costs...”

731. There is no further evidence, or detail, about this underlying change to the accounting for internal charges. At paragraph A7.5 of Annex 7 to HJ1, Dr Jenkins simply refers to the F28 data and the

S&S letter of 30 November 2022. She also states that she takes the lower SG&A charge for 2018/19 of £838m rather than the restated amount of £959m.

732. As for Mr Duckworth, at paragraphs 5.34 and 5.35 of MD2, he noted the changed accounting for the recharges, and said that a robust approach to estimating common costs should not be affected by a “reclassification of costs”. Otherwise, the point was not debated in the JES, nor was it the subject of detailed debate in the evidence.
733. What we consider we can safely take from the 2019 Paper is that the change in approach to internal recharges was due to recent changes in how BT Group was operating in terms of its trading dynamics and structure. There were also some operational assets that were not now being used by Openreach and should therefore not be allocated to it. The changes were more closely aligned with internal recharges in its annual reports and its RFS. However, it is also clear that (following the acquisition of EE in 2016/17), the higher percentage of recharges to BT Consumer, as opposed to other CFUs in BT Group, was due to mobile network costs.
734. Any indirect costs deriving from mobile network internal recharges cannot possibly be regarded as common to SFV Services. Further, while we accept that changes in the operation of BT Consumer could have genuinely led to some higher overheads, it is difficult to see why the entire increase in overheads, said to derive from a reallocation of internal charges, can be justified from the point of view of BT’s common costs and there is at least some force in Mr Duckworth’s point about reclassification.
735. We note that Dr Jenkins has not used the higher restated overhead figure for 2018/19 (and in fact the new policy on recharges was stated in the 2019 Paper to apply only to 2019/20 onwards). We agree with her approach, not least because it is clear that a significant reason for the change in policy at that stage was the implication of recent changes at BT Group on the recharges. In any event, BT has not sought to use the higher 2018/19 figure.
736. However, and returning to the more general debate about common costs here, Dr Jenkins made a broader point, which was that if there were common costs directed to promoting bundles, BT Sport etc, they were still relevant to SFV Services since the object of the exercise was to attract customers to bundles and many of them would have been taking SFV Services previously. Therefore, the common costs (and any increases in them) should be attributable at least to some extent to SFV Services. We disagree. We prefer Mr Duckworth’s approach which is to say that a cost of enlisting someone who had previously taken SFV Services to taking bundles should be seen as a cost of the bundle and not a cost of the SFV Services. That is particularly because, of course, a significant number of VOCs and SPCs did not switch at any particular moment in time, and the CR’s allegations of excessive pricing relate specifically to those who remained SFV customers.

737. Overall, we do not think that the material before us suggests that there would have been such significant increases in common costs as far as SFV Services are concerned. We therefore reject the idea that Mr Duckworth's CPI Index cannot be used at all.

*Particular cost events that might affect common costs*

738. BT makes the point that Mr Duckworth had not specifically considered the question of whether the significant cost of "onshoring" its call centres might be a relevant and substantial common cost which would not be captured simply by the application of the CPI Index. Mr Duckworth said that his approach was more high level. He said in the hot tub discussion that an exercise could be done to look at onshoring costs over time, but this would also need to take into account any resulting cost efficiencies and other quality changes. In the absence of discrete information going to these particular matters it is difficult to see what more Mr Duckworth could have done.

739. Similar points were also made about the provision of BT's "Gives" for voice services, but in fact, Mr Duckworth did deal with those in the context of direct costs.

740. We do not think that this point adds much, save to form part of any exercise to make some general adjustments to Mr Duckworth's model or its outcome which we refer to below.

*Changes in call pricing and competition*

741. BT also contends that the RFS model did not take account of ongoing pricing practices for VOC and (after 2009) bundle customers. Nor did it take into account the ratio of fixed calls to those made within a particular call plan, or indeed the general decrease in the volume of calls made. However, BT did not really explain why such matters were relevant to the question of common costs and again, we do not think that this point really adds anything.

*Economies of scope and size of common costs*

742. A further point made by BT is that there would have been economies of scope for SFV Services after 2009 and into the claim years. This is because voice and broadband were supplied down the same physical line; by way of example, BT would not pay WLR to Openreach twice where it was supplying a bundle, although there was a separate further charge from Openreach for the supply of broadband, so that BT actually took two products from Openreach. Its competitors, when supplying bundles, tended to take one blended product from Openreach to cover voice and broadband, although there were some further costs as well. If competitors were supplying voice only, they tended to take them from Openreach by WLR. On any view, there were economies of scope which is relevant, because it is common costs that cause such economies.

743. In the course of closing argument (Day 25/34-41) we questioned whether the relevant costs synergies might be pertinent to the setting of the competitive benchmark. This related to four



particular questions asked by Mr Ridyard. Ms Kreisberger KC said that they would not be, at least not in any way detrimental to the CR's case. If, for some reason, the costs synergies went to indirect costs and led to economies of scope, that would only lower costs and not increase them. However, that was not a satisfactory answer because we are here dealing with common, not incremental costs.

744. At paragraph 517 of its Closing, BT accepted that efficiencies in wholesale costs only went to direct costs. However it was said still to be relevant here because it reinforced the importance of the competitive benchmark being set at a level which allowed BT flexibility as to how it recovered its indirect costs across its services. We are not sure that, as expressed, this captures the real point about the significance of economies of scope.

745. However, that does not matter because we think that the real economies of scope between SFV Services and bundles do give some support to the notion of the existence of significant common costs. The more common costs there are, the more such costs might be capable of being borne by one particular product by reason of the principle of flexibility.

#### *Economies of Scale*

746. The total number of BT stand-alone voice lines in 2009 was 14.4m. By 2015/16, there were only 9.5m voice lines in total, and most of these (6.89m) were in bundles. Therefore, according to Dr Jenkins (see paragraph 5.71 of HJ2), the "per line" unit costs (which Mr Duckworth's model uses) would change upwards, as there were many fewer customers to share fixed costs (i.e. costs of providing voice services that do not vary with the number of voice lines). She says that Mr Duckworth's model based on 2009, and simply uprated by the CPI Index, does not take account of this.

747. As to that, the CR says, first, that in any event, the fixed common costs of the SFV Services are likely to be low; again we deal with this at paragraphs 761 - 777 below. Second, Ms Kreisberger KC points to the fact that, according to BT, costs had reduced as a result of the decrease in the number of lines. Section 9.3 of the CCFS section of the RFS at p82 states that:

"Retail operating costs have also decreased as a result of the fall in numbers of connections and rentals. A strong focus on cost control has driven down the SG&A costs for these markets."

748. Here, she adds that the second sentence of this quotation also supports the notice of BT making costs efficiencies.

749. Another way of putting this might be to say that the cost efficiencies being made at the time counteracted any increase in unit costs due to the decreased number of lines.

750. But in any event, in her submissions on Day 25/24-28, Ms Kreisberger KC also pointed to the absence of any evidence to suggest that there were particular blocks of large fixed costs that were

common to voice services and not to other services within BT Consumer, and which therefore should be spread across voice lines only.

751. In this context, we then have to deal with the example of this economies of scale point made here by BT. This is set out in its Closing as follows:

“511. To illustrate why Mr Duckworth is wrong to assert an unchanged LRIC+:

- a. Suppose that in 2009, all of the incremental costs of residential fixed voice services were fixed (£100 million), and that there were no additional common costs between voice and other products. With 14.4m lines, the LRIC of voice would be £6.94 ( $100 \div 14.4$ ) and the LRIC+ measure (which Mr Duckworth says is relevant) would be exactly the same, there being no common costs in this simplified example.
- b. Suppose that by 2015, there were 9.5m fixed voice lines in total and – in line with Mr Duckworth’s (unsubstantiated) assumption – suppose for the purposes of this example that those lines would still have the same £100m of fixed costs (ignoring for present purposes the question of CPI). Now, however, this sum would be considered to be common across SFV and voice sold in bundles. The LRIC of SFV Services would be zero (there being zero incremental SFV costs), whereas the ‘+’ would be £10.53 ( $100 \div 9$ ), so the LRIC+ measure would be £10.53.

512. It can be seen from the above that (i) the mix between incremental and common costs has shifted significantly from all incremental in 2009 to all common in 2015; and (ii) the LRIC+ of SFV Services would be c.50% higher in 2015 compared to 2009. Mr Duckworth’s approach cannot identify (i) and fails to adjust for (ii). And that is before one even attempts to vary his other assumptions.”

752. However, we consider that this is highly artificial. It assumes £100m of wholly incremental costs (i.e. they vary across the number of lines supplied) with no common costs at all. This is in fact different from Dr Jenkins’ own analysis which proceeds on the basis of common costs which are common across the whole of BT Consumer. We do not consider that there is any real force in the example given and of course, it was not supported by any factual or indeed expert evidence.

753. In fact, in oral argument, Mr Beard KC accepted (Day 27/81) that there was nothing more to the economies of scale point than the suggestion that if there was a fixed cost from one year to the next which literally could not change, and it had to be distributed over fewer lines, there would be a higher unit cost. But as an abstract point, we do not think this takes the matter much further. Nor does Mr Beard KC’s suggestion that in fact, the example at paragraph 511 was concerned both with economies of scale and scope. In this regard, we have noted Mr Duckworth’s evidence in the hot tub session at Day 22/80, but do not consider it adds anything here. In conclusion on this point, we do not think that it is fatal to Mr Duckworth’s use of the CPI Index. Once again, if BT felt that there were significant economies of scale that led to higher unit costs as voice lines declined, or the existence of important common costs between SFV Services and bundles, it was open to BT to provide evidence on either or both of these factors. It did not do so.

#### *Different Cost allocations in the claim years*

754. BT says that an important defect of the RFS in this context is that the methodologies used in the 2009 RFS were not fixed in stone and they could be changed. That is correct, although it was not suggested by BT that the allocation principles of cost causality for incremental costs and fairness for common costs had actually changed in the course of the RFSs or would have done so had they

continued. It was also said here that the allocation of costs according to such principles involved an exercise of judgment. That, of course, is true but if it is exercised appropriately and in accordance with settled principles and by BT itself and its auditors, we do not think that this is a reason to deprive the RFS model of force going forwards.

755. Mr Duckworth was cross-examined about this at some length (see Day 15/124-164). He drew a distinction between attribution methodologies in the RFS which would be reviewed regularly, as opposed to apportionment bases which were updated at least annually - see Section 2.1 of the PAD referred to at paragraph 517 above. He accepted that for those indirect costs which could not be allocated on a costs causality basis and would then have to be apportioned on a fairness basis, there were potentially different ways of doing that. So if there was a BT brand-driven campaign, that would be an example of a cost common to all the services provided by BT and there would have to be an apportionment. He further accepted that in relation to advertising, for example, there could be differences in the overall spend from year-to-year but also differences in the nature or focus of particular advertising campaigns. He agreed that in a later year from 2009, there could be a shift, probably an increase in overall advertising expenditure, to cater for a new product line like BT Sport. But whether that meant that the unit costs which would be attributable to SFV Services would go up or down was a different question. We interpose to say that if there was that kind of increase in advertising expenditure focussing on BT Sport, it is very hard to see how it would be a common cost across all services rather than an incremental cost for BT Sport alone.
756. It was then suggested to Mr Duckworth that, hypothetically, BT might wish to publicise, by advertising, the virtues of its telephony services both on a stand-alone basis and within bundles. He accepted that in such an event, the question of apportionment of such costs would be completely different from a situation where the advertising campaign was directed solely to bundles. He later said that the new situation would involve apportionment of some common costs but that others might be incremental and therefore attributed on a cost causality basis. He also agreed that from a costs causality point of view, there would be a shift in the proportions as customer numbers changed.
757. Mr Duckworth also accepted that “onshoring” customer service was an additional cost and would therefore increase incremental costs. He also agreed that if there was a “fundamental dislocation” in the way that customer care services were delivered, the attribution outcome, even with the same numbers of staff, could be completely different. He then agreed that if the office accommodation estate of BT changed, there could be differences, not only in the unit costs of staff due to different rental prices but also apportionment would change as well.
758. Finally, in this context, Mr Beard KC put to Mr Duckworth the example of a new IT billing system introduced after 2009 and which would enable single billing of multiple services for customers and

which was a very large investment. The question then was whether an RFS for that year would have radically different cost allocations from the previous year, the implication being that at least some of the additional costs of introducing the new billing system would fall on SFV Services. Mr Duckworth's first response was to say that with such a new system, the real beneficiaries would be the bundle customers because they were the ones with multiple services. For SFV Services customers, the position was as before. So even with a new IT billing system, it is hard to see how this should be attributed to SFV customers or treated as a common cost. He also said that the attribution methodologies might change. He finally agreed that if the 2009 attribution method was applied in 2010 to a brand-new IT System, the level of costs and their outturn could be radically different as far as changes in costs and distribution were concerned.

759. In relation to that last example, it was posited as a hypothesis. The only document put to Mr Duckworth was the BT Operational Review of September 2009 which stated at page 14 that in respect of bundles, new IT systems would enable single billing to customers of multiple services. The problem with that example, and generally here, is that a number of hypotheticals were put to Mr Duckworth. Unsurprisingly, if there was a radical or fundamental change to the operation of BT Consumer based on some very large investment, that could make a change to the level of costs and how they were distributed. However, again, there is no real evidence of any of that adduced by BT.
760. Overall, we do not consider that this part of the cross-examination of Mr Duckworth itself cast any serious doubt on his use of the CPI Index.

*Likely Size of Common Costs BT Consumer*

761. It can be seen from what we have said above in relation to some points made against the RFS model by BT, that the CR has submitted that in any event, the common costs of BT Consumer were inherently likely to have been small or insignificant. If that point is correct, it would obviously significantly affect adversely the level of common costs ultimately attributed by Dr Jenkins to SFV Services. It is convenient to deal with this topic at this point in the judgment.
762. Both the common costs of BT Consumer as a whole, as attributed by Dr Jenkins, and the proportion of such common costs recovered by revenues from SFV Services using the SAC Combi, are set out in paragraph 558 above. So, to take the year 2015/16 as an example, the common costs of BT Consumer in Dr Jenkins baseline scenario were said to be £390m, while revenues from SFV Services contributed £243m to such common costs.
763. As to this, the starting point is that it is agreed between the experts that both BT Consumer in general and SFV Services in particular were asset-light, as opposed to, for example, BT's wholesale product (see e.g. paragraph 6.94 of HJ1). Mr Parker's view, albeit expressed in general terms, was that

common costs in retail telecoms businesses were not, in reality, significant or should not be so, and Mr Duckworth agreed.

764. Obviously, Dr Jenkins disagrees, in the sense that her figures suggest very significant common costs, both in relation to BT Consumer as a whole and as allocated to SFV Services by her. There is her reliance on Ofcom's VULA Margin Statement and the TSO charges (considered at paragraphs 801-815 below) and there is then her analysis of the descriptors (considered at paragraphs 784-794 below). That analysis is not, however, as persuasive in the present context, as direct and detailed evidence from BT on the size of BT Consumer's common costs which was not adduced, would have been.
765. Dr Jenkins did suggest that relevant common costs could include software licences and support systems, but that would not explain the size of the common costs figures. The evidence of Mr Cackett did not assist materially here. When addressing the MTP for voice services in RC1, he explained that indirect costs such as staffing were recorded at BT Consumer level and were not attributed to any particular product or service, as they were common to all. No formal attribution to individual services was made although the informal "unit economics" analysis (referred to above) made some estimate of how such costs were spread across different divisions. Although we asked Mr Cackett some questions about this exercise, and raised its significance (or otherwise) with the parties, the position was that these were treated as no more than informal estimates and neither side sought to rely upon them. Mr Cackett did, however, make clear in cross-examination that some central costs like those of networking and digital teams would include those who dealt with particular services like BT Sport, in which case such costs would, of course, be incremental and not common.
766. A further argument made by the CR which assumed some significance in the course of the trial is that if the common costs figures were anything like those suggested by Dr Jenkins, then other similar telecoms operators could not have afforded to enter the market, and yet they did. Strictly, the relevant common costs are those of BT Consumer as a whole, in other words £390m for 2015/16, because they would have to be incurred if there was simply an SFV Services stand-alone product. In the hot tub discussion, Mr Parker made the point that common costs of that order would have to have been incurred by other operators precisely because they were common. Where the cost of entry might be incremental, that would be irrelevant because, by definition, the relevant costs to be considered here are common costs (see Day 13/160). Later in the discussion, Dr Jenkins and Mr Matthew sought to diminish the notion that if there were general common costs in relation to BT providing its SFV Services, then they were *prima facie* relevant to any other operator seeking to

provide an equivalent service (see Day 13/161-165). We deal below with the particular points made by BT in this regard.

767. Tables 1-3 of MD2 make a comparison between Dr Jenkins' suggested common costs figures and those pertaining to 3 other operators, namely the Post Office, SSE and PlusNet. The latter is part of BT Group, but it functions as a separate company. For the year 2015/16, the Post Office's total costs for all of its telephony services were £142m, with £78m allocated to its SFV Services. SSE's total costs across voice and broadband were £[REDACTED] and PlusNet's total costs were £281million. All of these were markedly less than £390m.
768. As for the Post Office and SSE, BT made the point that these were companies which otherwise operated very large businesses, so they were not stand-alone telephony companies. Rather, the provision of telephone services was added to their existing range of products, and the costs reported for their telecoms businesses might well be the incremental costs of providing this service, given the common costs already incurred in creating their primary businesses. The new service could therefore be expected to rely upon existing infrastructure with its own set of common costs, and so the costs cited by Mr Duckworth were uninformative as to the size of any costs that are common between the telecoms and other operations of these firms. We think there is force in this point.
769. However, the CR also relied upon the example of Phone Co-op, a much smaller operator. This company was referred to in MD1, although in the context of his reasonable margin analysis. In oral closing, Ms Kreisberger KC referred to the Phone Co-op's s135 response to Ofcom in 2017 which showed its costs and revenue for a three-year period. It had around 20,000 customers while it was in the market [REDACTED]. The point made by Ms Kreisberger KC is that the Phone Co-op could not have operated in the voice market at all if it had to bear common costs of the order of magnitude suggested by Dr Jenkins. In criticising the use of this exemplar, Mr Beard KC described Phone Co-op as a "minnow". Ms Kreisberger KC agreed, but said that this was the point: it was still able to operate in this market [REDACTED], from 2013-2017. And if it did, then this suggests that some of these costs were scalable, depending on the size of the customer base, and that in turn rather suggested that they were not common costs at all, but incremental. We see that, but in this context, Mr Matthew observed that the focus should be on an operator seeking to have "real weight" in the market (like BT) as opposed to other, small standalone operators like Phone Co-op. Thus the common costs necessarily to be attributed to other suppliers might be different for good reason. We think there is force in this point, too.
770. Finally, the CR also relied upon references in MD1 in the reasonable margin section to TalkTalk and Utility Warehouse. As with the Phone Co-op, Mr Duckworth was not there dealing with such companies from the perspective of the common costs as such. Nonetheless, the general point was

made that these two operators could not have entered the voice market if common costs were anything like as high as suggested by Dr Jenkins.

771. We see that, but we think there is a further point here. The likely existence (or not) of important common costs can be inferred from the observed pricing patterns in the market. It is evident that there are large discounts available to UK telecoms consumers who buy bundles, compared to the prices charged for standalone voice and broadband. In the 2017 Provisional Conclusions, for example, Ofcom noted as follows at para 3.41.1 p23:

“Our analysis (see Annex 8, Figure A8.43) shows that on average a split purchaser paying a combined price for standalone voice from BT and standalone broadband from BT, Sky or TalkTalk could save £8 per month (more than 20%) by switching to an equivalent dual-play service from their broadband provider at standard prices, and just over £14.50 per month (more than 35%) at promotional dual-play prices...”

772. These price patterns are broadly similar to the price differentials that Mr Parker relied on in his market definition analysis, in which he argued that if the gap between the price of buying a dual play bundle and the sum of the prices of standalone voice and broadband contracts was greater than 5-10%, this price differential would indicate that dual play and SPC purchases must lie in separate product markets.

773. Dr Jenkins also referred to the extent of bundle discounts in her evidence on Day 13/83, as follows:

“if you actually look at the pricing of Standalone Fixed Voice now and standalone broadband products now they are very similar at between £26-£28 and of both of them offer the alternative product for £5 extra. So if you take a standalone broadband you can add Voice for £5 if you take Standalone Fixed Voice you can take broadband for £5.”

774. Dual Play and other bundle deals were first offered by BT’s competitors. They provided consumers with advantageous price terms that were typically advertised by focusing solely or mainly on the add-on to the line rental price (which in turn in many cases mirrored BT’s SLR). In 2016, however, as already noted, the ASA Ruling required all firms offering bundles to advertise the full price of the bundle, preventing retailers from focusing solely on the incremental price of broadband over line rental. This was due to concerns that such price advertising might be misleading. Bundling of various other services (TV, mobile etc.) along with voice and broadband was also highly prevalent in the industry.

775. Taken at face value, the existence and prevalence of deep discounts for bundles over the stand-alone equivalents does indicate the existence of supply-side synergies, which in turn are likely to come from common costs. If the cost of supplying a bundle of A+B is less than the sum of the costs of supplying A and B separately, this provides a competitive explanation for the bundle discounts. It is the low marginal cost of supplying the second or third product that makes it commercially attractive to offer such price structures. This will be true whether the synergies and common costs arise from direct costs (for example if the costs incurred by telecoms retailers when buying in wholesale services from Openreach create incentives to bundle) or indirect costs (such as the ability

to profit from a common brand name or head office infrastructure when selling related services). The common cost synergies claimed by Dr Jenkins fall into this latter category of indirect cost synergies.

776. The parties did not, however, provide any detailed evidence on the existence or otherwise of such common cost synergies, beyond the claims made by Dr Jenkins regarding the scale of the indirect common costs. The CR contended that observed price discounts might exaggerate the underlying common cost synergies between voice and other services, since BT's pricing in particular contained a deliberate policy of charging higher gross margins on voice than on bundles. Nevertheless, the prevalence of bundle discounts across all operators in the market does seem to us to indicate that there are some important synergies arising from joint provision, and this albeit indirect evidence tends to discount the CR's claims that common costs are immaterial.
777. Overall, we do not feel that the evidence adduced by the CR clearly establishes that the common costs of BT Consumer are so insignificant or immaterial that any discussion of them becomes irrelevant. To that extent, we reject the CR's reliance on such a proposition. Nonetheless, we do attach some weight to the notion that it would be surprising if the common costs were as high as Dr Jenkins has suggested. So this is a matter which we take into account when assessing the competitive benchmark overall.

### **Conclusions on the RFS Methodology**

778. For all the reasons given above, we find it quite impossible to reject the RFS model altogether as being "not fit for purpose" as BT contends.
779. We do, however, consider that on any view, the reliance which can be placed on its outcomes should be tempered by the observations we have made above and in particular with (a) the fact that such outcomes are built upon only one data-point which begins and ends with 2009, (b) the fact that the uprating by use of the CPI Index may underestimate any costs increases and (c) the fact that the RFS has no flexibility so far as the recovery of common costs is concerned.
780. Precisely how these concerns are taken into account in our ultimate findings will be considered after we have undertaken our analysis of Dr Jenkins' SAC Combi methodology, which follows.

## **ANALYSIS OF DR JENKINS' METHODOLOGY**

### **Introduction**

781. Dr Jenkins' overall approach was described at paragraphs 525 - 558 above. As with Mr Duckworth's methodology to arrive at a competitive benchmark, we now analyse in detail each part of Dr Jenkins' approach.



782. Before doing so, however, we would add the following. Dr Jenkins' approach is to identify a competitive benchmark based on BT's own costs (which include common costs). She does, of course, refer to comparators (as did the CR) but only on the question of reasonable margin. However, Mr Matthew's evidence was that in many workably competitive markets there will be a range of cost levels among rival firms. See paragraph 139B of his DM1 and Figure 1 beneath it. At some points, BT deployed this evidence in support of the argument that it was appropriate to fix a higher competitive benchmark than might be the case if one looked at a costs plus calculation for BT alone, or that a range of costs levels would affect whether any excess over the competitive benchmark could be considered significant and persistent. Implicit in this argument is that BT would be permitted a higher level of profitability before its prices would be considered excessive. We do not accept such arguments, because we consider that for the purposes of Limb 1 (and consistent with what we said at paragraphs 53 and 607-611 above) at this stage, the focus should indeed be on the costs of the firm in question. However, arguments of this kind would be relevant under Limb 2

### **Dr Jenkins' Derivation of the Common Costs of BT Consumer**

#### *The Relevant Figures*

783. It will be recalled that Dr Jenkins' baseline approach, taking 2015/2016 as an example, was that out of a total of £983m of BT Consumer's indirect costs, which represented 28% of its total costs, £390m were taken to be common costs and the balance, £593m, were incremental costs. That meant that common costs were 11% of the total costs of BT Consumer. See the Table at paragraph 558 above.
784. Dr Jenkins' low scenario version of her model is based on making a 15 percentage points reduction in the likelihood of any particular indirect cost being common. In other words, where, for example, a cost was assessed in Annex 7 to HJ1 as having a 35% chance of being a common cost, it would now be assessed as having a 20% chance. See Table A7.1 On that basis, £262m were common costs, representing a reduction from Dr Jenkins' base case of around one third, with the balance of £721m, being incremental cost and this meant that common costs now represented 7% of the total costs.
785. The relevant aggregate percentages here are shown in Table A7.7 of Annex 7 to HJ1:

**Table A7.7 Proportion of Total SG&A and D&A (combined) costs deemed common costs**

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
"Baseline" scenario	40%	39%	39%	42%	45%	46%	43%
"Low" scenario	27%	26%	26%	29%	31%	31%	30%
"High" scenario	53%	52%	52%	56%	60%	61%	57%

Note: No D&A data for 2021/22 was available from BT. I therefore assume that the D&A charges for 2020/21 are equal to the D&A charges in 2020/21. I further assume that the proportion of D&A charges that are deemed common in 2021/22 is equivalent to the proportion in 2020/21.

786. In addition to her primary exercise of deciding the probability that a particular cost item was a common cost, as referred to at paragraphs 526 - 531 above, and discussed in detail below, Dr Jenkins performed what she describes as a cross-check using internal charges from BT's Technology, Services and Operations ("TSO") ("the TSO Cross-Check"). According to this, common costs were £269m with incremental costs being £714m, so that common costs represented 8% of total costs. It will be seen that these results are very similar to Dr Jenkins' low scenario figures.
787. The 4 comparisons across the claim years are summarised at Annex 3 to BT's Closing.
788. To complete the picture, and again taking 2015/2016 as an example, on Dr Jenkins' baseline scenario, 33% of BT Consumer's SG&A costs were deemed to be common and 64% of its D&A, costs were so deemed. The respective percentages on her low scenario basis were 21% and 49%. See Tables A7.5 – A7.7 in Annex 7 to HJ1. Taking the deemed common costs as a percentage of BT Consumer's total indirect costs (i.e. the sum of D&A and SG&A), common costs are between 39% and 46% of indirect costs across the claim years on the baseline scenario, and 26-31% on the low scenario.

#### *Dr Jenkins' Primary Approach*

789. The key criticism made by the CR of Dr Jenkins' estimates of common costs relates to the process of analysis which she used so as to derive the common costs figures. That process is summarised at paragraphs 526 - 529 above and is described in detail in Annex 7 to HJ1. Table A7.2 sets out the results of the exercise. The various columns in that table can be explained as follows, by reference to their headings:

- (1) "Label in financial disclosure" is the description given to a set of costs in BT's disclosure for these proceedings; it is not therefore contemporaneous;
- (2) "BT description of cost line" is how BT described the costs line in the SG&A and D&A sections of its P&L accounts for BT Consumer; it is, in other words, BT's own descriptor;

- (3) “my mapping of cost item to Ofcom category (Ofcom cost type)”; this column sets out how (if at all) Ofcom described the costs line for the purpose of its VULA Margin Statement;
- (4) “size of cost item (average over 2015/16 to 2019/20)”; this is the monetary amount involved;
- (5) “my categorisation (proportion of this cost item which is common costs)” sets out Dr Jenkins’ assessment of the probability that the item is a common cost; and
- (6) “Reasoning for my categorisation” sets out her reasons.

790. As Table A7.1 of Annex 7 shows, Dr Jenkins, uses 7 different probability measures. On the baseline case, an item which is not a common cost at all is shown by 0% and certainty that it is a common cost is shown by 100%, as one would expect.
791. Once Dr Jenkins’ probability percentages have been applied to each cost item, it is then possible to arrive at a total common costs figure. It follows that the balance must be incremental costs. Because Dr Jenkins’ analysis started with deriving a figure for common costs, there was no separate or independent attribution of incremental costs. They are arrived at simply by a process of deduction.
792. The first point made by the CR is that Dr Jenkins’ assessment of the probability of any particular cost line being a common cost is arbitrary because it is simply an exercise of judgment. And if one looks at any particular descriptor, there is not enough information to indicate with any real degree of assurance that it tends to show a common rather than an incremental cost.
793. As to that, obviously, it is an exercise of judgment, which Dr Jenkins has tempered, to some extent, by providing a set of low scenario figures as an alternative to the baseline results. But the use of judgment is not *per se* an obstacle, in our view. And in fact, some of the descriptors, assisted by further details, as shown in Table A7.2 do seem informative, especially in the context of D&A costs. Further, the CR did not cross-examine Dr Jenkins at all on her individual allocation of percentage probabilities.
794. More telling, however, is the CR’s related point which is that, however useful her own exercise of judgment may have been, Dr Jenkins could - and should - have been assisted by BT itself in performing this exercise. There is no reason to think that BT could not have provided input as to the status of the costs line (as common or incremental) by reference to much more detailed descriptions of what these costs were actually for, which Mr Duckworth describes as the missing “quantitative evidence”.
795. This is then contrasted with the position under the RFS where the costs were allocated by BT on a costs causality basis as far as possible, with the remainder - the common costs - dealt with on a fair basis and by reference to an extensive and sophisticated set of data. It is of course the case that the RFS did not state which of the indirect costs were incremental and which were common. But at least

it started by seeing which costs must have been incremental by using costs causality. Accordingly, we do think that there is force in this part of the CR's criticism.

796. At paragraph 6.131 of HJ1, Dr Jenkins says that:

"I estimate the SAC of SFV Services in every financial year for which I have financial data from BT Consumer as the sum of the following elements:

- (a) the incremental costs of SFV Services (comprising the Cost of Sales and the incremental SG&A and D&A costs);
- (b) all BT Consumer common costs; and
- (c) a reasonable rate of return of 25% EBIT margin."

797. At paragraph 5.15 of MD2, Mr Duckworth says that implicit in that statement is an assumption that the costs she identifies as fixed (i.e. not incremental) are common to all products, so she does not consider the existence of fixed costs within BT Consumer which are not common to SFV Services. Such costs would include: product development costs relating to the provision of broadband, television and mobile services, or bundles, product management costs relating to such services, advertising and marketing costs for non-SFV products, and other fixed costs relating to television, or bundles, including television, such as the cost of the acquisition of content rights which would be independent of the number of customers or the cost of TV production. In other words, costs which have no apparent connection to the SFV product and would not have to be incurred by a standalone SFV provider. From this, Mr Duckworth suggests at paragraph 5.16 that:

"Dr Jenkins' simplified approach does not allow for fixed costs which are not required for the provision of BT SFV Services to be correctly classified and implicitly assumes that these costs would be incurred in the provision of SFV Services on a standalone basis. As a result of this, Dr Jenkins over-estimates the level of fixed and common costs associated with the provision of SFV Services."

798. Dr Jenkins' response to this in the JES is essentially to rely on the TSO Cross-check. We deal with this response at paragraphs 808 - 815 below, in the context of the TSO Cross-check generally, but should say here that we do not find it a complete answer to the point made by the CR.

799. Overall, while we would not by any means simply disregard the primary approach taken by Dr Jenkins in saying what should be regarded as the common costs of BT Consumer, there are clearly some difficulties with it such that her ultimate figures cannot simply be adopted without more.

800. However, we then need to consider the support which Dr Jenkins says she has obtained from (a) Ofcom's treatment of some of these costs in the VULA Margin Statement and (b) her use of the TSO Cross-check.

#### *VULA Margin*

801. As for the VULA Margin Statement, it will be recalled that VULA is the mode of access to superfast fibre broadband. One can see that in the VULA Margin Statement, for most of the SG&A cost lines (but none of the D&A cost lines), there were descriptors applied by Ofcom being either "short-run variable" ("SRV") or "long-run variable/fixed" ("LRVF"). The former are taken by Dr Jenkins to describe incremental costs and the latter to identify common costs. They may not in fact be a

complete proxy because long run fixed costs can in fact be incremental to a particular product or group of products, only as opposed to being common to all. That would be the case if a building was taken on a lease in order to service the administrative requirements of some but not all products. This would be a long run “fixed” cost but ultimately it would be incremental to the products concerned, rather than common to all.

802. At this point, it is necessary to say something more about the exercise being undertaken by Ofcom in the VULA Margin Statement. The purpose was to regulate the margin between BT’s wholesale and retail superfast fibre broadband prices, so as to avoid a margin squeeze by BT on its competitors in the retail market. Ofcom’s requirements here were limited to a minimum margin. They did not extend to imposing particular price caps, thereby continuing its approach since 2014, that BT should retain broad flexibility over its VULA prices in what was a review period.
803. The margin condition imposed was arrived at by Ofcom by, among other things, its assessment of BT’s costs in respect of superfast broadband on a LRIC+ basis, i.e., including an allocation of common costs. This in turn led Ofcom to assess which elements of BT’s SG&A costs should be regarded as SRV or LRVF, apparently on the basis that short run variable costs were more likely to be incremental to whichever service they were associated with, whereas costs that remained fixed had a higher probability of being invariant to changes in output levels, and therefore had properties closer to the notion of a common cost that did not belong definitively to any individual output or service.
804. All that is relevant in the present context is the application of one or other of these labels to particular costs lines within BT’s SG&A costs. These are set out at Guidance Table 1 of the Margin Statement. The source of the information in the table (presumably the description as opposed to Ofcom’s designation) is said to be BT’s responses to various statutory requests for information made by Ofcom in August and October 2013. Ofcom did not analyse D&A costs, and that is why Dr Jenkins’ analysis in that regard makes no reference to any Ofcom designation.
805. We understand why Dr Jenkins has sought to make use of the Ofcom designation, at least as a guide, even if the concepts of SRV and LRVF costs are imperfect as proxies for incremental and common costs. However, there must be a caveat, in that Ofcom’s exercise involved a different focal product, indeed at the opposite end of the technological spectrum, to a simple voice line and so it does not follow that all of the costs labelled LRVF would be common to SFV and other services within BT Consumer as well.
806. In addition, Ofcom employed an FAC methodology in the Margin Statement and so actually determining whether costs here were common or incremental would not affect the results of Ofcom’s costing exercise.

807. Nonetheless, we do not consider that it was unreasonable of Dr Jenkins to seek some assistance from the simple way in which Ofcom chose to designate particular SG&A costs lines. Accordingly, we give some weight to it as a guide, which is how she describes it. However, we do not consider that it provides an answer to the problems we have identified in Dr Jenkins' primary approach.

*The TSO Cross-check*

808. That then leaves Dr Jenkins' TSO Cross-check. The outcome of this cross-check is described in paragraph 786 above. Again, one starts with the VULA Margin Statement. For Ofcom's purposes, BT had referred to a list of TSO activities and said that these costs were recharged internally. At paragraph 6.198 of the Margin Statement, Ofcom said that TSO could be thought of as the "back office" of BT which provided support and services to all the market-facing units ("MFUs"). At paragraph 6.200 Ofcom said that there were three broad categories of TSO costs, namely, direct, indirect and fixed costs. Here, Ofcom was using fixed costs as another word for common costs because it stated that fixed costs were costs that could not be directly or indirectly attributed to an MFU and were mainly related to BT-wide activities or in support of TSO activities. They included accommodation, energy and TSO overheads. Ofcom then included a proportion of all three categories of TSO costs in its margin assessment. It allocated all of the TSO costs on a Revenue basis.

809. We now turn to Dr Jenkins' reliance on the TSO costs. She refers to a BT compliance model for the limited purpose of the VULA margin requirement, which was submitted by BT to Ofcom in October 2016 ("the Compliance Model"). In it, the TSO costs for 2015/2016, were described by BT as being "direct", "indirect," or "fixed". The designation of particular TSO costs by BT as "fixed", as opposed to "direct" or "indirect" was itself drawn from an Ofcom Decision dated 21 October 2014, which responded to a complaint made by TalkTalk that BT was guilty of a margin squeeze in relation to superfast broadband. In the course of reaching its decision that there were no grounds for action against BT, Ofcom undertook a LRIC exercise in respect of BT's costs. In respect of 7 categories of TSO costs, it concluded that two categories were fixed, namely Accommodation and Energy and TSO Functions (Overheads). In its Compliance Model, using those categories, BT said that a total of £127m of costs fell into those two categories and were therefore fixed. This is out of a total amount of TSO costs of £170m. It therefore followed that in the Compliance Model, BT had designated 75% of its total TSO costs as fixed.

810. Dr Jenkins then applied that percentage to the cost lines within BT Consumer's P & L accounts which made express reference to TSO (for example, Fixed Recharges). In other words, she attributed a 75% probability that they were common. For the purpose of this exercise, she did not regard any

other of the costs lines as involving common costs at all. The results of this exercise correspond closely to Dr Jenkins' low scenario, as stated in paragraph 784 above.

811. The CR's response to this is twofold. First, it again made the point that it was not clear that the TSO fixed cost recharges were limited to costs which were common across all the MFUs, in other words the same point as was made generally, noted at paragraph 796 above.
812. As to that, Dr Jenkins said that at least in relation to the TSO costs, there could be no issue that the common cost element thereof would apply to SFV Services, given the definition of "fixed costs" referred to in paragraph 808 above. Moreover, this cross-check exercise was itself conservative, because it excluded other common costs which would arise if one looks simply at her primary analysis. Further, in the hot tub discussion (Day 14/54-56), Dr Jenkins made the point that Ofcom in the VULA Margin Statement was seeking to characterise as much of the indirect costs as possible as being incremental, leaving relatively little for common costs. So if one was relying on TSO costs only, they would be unlikely to over-state common costs by including costs that were not common to SFV Services. We see that, although of course it only goes so far, since if one was relying just on the TSO Cross-check, the results would be significantly below her baseline scenario.
813. The CR also makes a second point here by reference to a set of slides produced by BT on 19 December 2016 called "Ofcom's Proposed Retail Narrowband Market Review". Paragraphs 7 and 8 of that document are headed "our financials demonstrate that increasing value provided is driving down profitability for Solus Customers." In the hot tub discussion, Mr Duckworth pointed to the fact that, against the cost lines referring to TSO Direct, Indirect and Fixed, there was a rubric "significant downweight - proportion of number of products c3-4%".
814. Mr Duckworth said that this showed that BT reduced the proportion of such costs being allocated to SFV Services (i.e. "line-only") to reflect the fact that such costs were not all fixed and common to SFV Services, or should not be treated as such. Mr Duckworth then referred to an underlying spreadsheet showing that, actually, only 20% of the TSO costs were allocated to accessing the SFV Services. He made the same point in relation to the same rubric applied to "Total Marketing and Sales Costs". As to that, Dr Jenkins pointed out that the BT slides were allocating all the indirect costs, as opposed to separating out common and incremental costs. It is also fair to say that Mr Cackett was not cross-examined on these matters. Mr Beard KC said that it was not clear what was going on in the BT slides document. In our view, although we understood what Mr Duckworth was saying about the slides, we did not feel we could draw anything useful from them; there was simply not enough information about what was going on here.
815. Overall, while we think that the TSO Cross-check has some value, it does not provide a complete answer to the difficulties we already identified with Dr Jenkins' primary approach.

### *Conclusion on BT Consumer Common Costs*

816. In our judgment, looking at the evidence overall, we consider that the common costs of BT Consumer, as stated by Dr Jenkins in her baseline scenario cannot be taken as reliably established and there is a significant risk that they have been overstated. We also come back to the observation that reliance on Dr Jenkins' judgment and a series of imperfect cross-checks is inferior to an approach that would have been based on BT's own detailed knowledge of cost causation, and which BT chose not to undertake for the current case. We set out below the extent and impact of this.

### **The SAC Combi Exercise**

#### *Insufficient number of combinations*

817. It is common ground that Dr Jenkins has not undertaken her SAC Combi exercise on every possible combination of the relevant BT products. In particular, her SAC Combi analysis did not explore combinations that broke down the different elements within BT's bundles. Instead one component, which features in 13 of the first 25 combinations was called "Bundles". In relation to this, Dr Jenkins stated as follows in HJ1:

"6.143 The Bundles service is a broad category that includes the provision of TV services and BT Sport, in addition to fixed voice services and broadband services sold in bundles. BT TV services always require the purchase of a broadband line, and are therefore always sold in bundles, whereas BT Sport was a service launched by BT to support its broadband business and, in particular, to increase customer acquisition and retention on superfast broadband packages. I therefore consider it reasonable to consider Bundles as a broad category of services including TV and BT Sport (however sold).

6.144 Furthermore, I have not disaggregated Bundles into dual-play, triple-play and quad-play as separate services from which to derive relevant combinations. In my view, doing so would not materially assist in determining whether SFV Services were priced excessively. Any potential differences in the final "cost plus" benchmark identified in Step 3 that might arise from testing these further granular bundle types in combination with SFV Services would be capturing BT's relative pricing decisions within its portfolio of bundles. In my view, the appropriate allocation of common costs for SFV Services should be judged against the contribution to common costs of Bundles as a whole. In addition, the number of combinatorial tests to run would grow exponentially and potentially render my preferred SAC Combinatorial approach impractical to implement."

818. The CR's first criticism of this approach is that Dr Jenkins has not employed a sufficient number of combinations, which would be very much more, if, for example, her "Bundle" was disaggregated into its various constituent products, and the CR argued that products such as television and BT Sport needed to be treated separately.

819. In effect, the CR contends that (a) there is a general defect with Dr Jenkins' SAC Combi because it does not test for all possible combinations, and (b) there is a particular problem with the failure to separate out BT Sport and which, in effect, means that BT's profits on SFV Services are subsidising the losses incurred on BT Sport. Obviously, both points are related, but we deal with each in turn.

### The General Defect

820. As to this, Mr Duckworth disagreed with the approach taken by Dr Jenkins and, as set out in the paragraphs of HJ1 referred to in paragraph 817 above, his view was that combinatorial testing was



meant to be a theoretical model, designed to see if the focal product's price would entail an over-recovery of common costs or not. In this context, Mr Duckworth noted that for 2015/16, Dr Jenkins' "Bundle" accounted for 78% of BT Consumer's revenue. The point is that Dr Jenkins did not differentiate between different types of bundle and all the elements within it that had different characteristics, costs, prices, and therefore margins. If the bundle included loss-making products (or ones whose costs were inefficiently incurred) that would reduce the profitability of the bundle and would therefore increase the share of common costs that the model would permit to be contributed by SFV Services. He explained this persuasively, in our view, in the hot tub discussion at Day 14/5.

821. Mr Duckworth also considered that Dr Jenkins' approach was inconsistent with what the Tribunal said in *PPC* (see paragraphs 658-659 above).
822. As for Mr Parker, he demonstrated how a failure to consider all different combinations did indeed lead to a greater share of common costs being attributed to the focal product. In the hot tub discussion at Day 14/8-10, he showed this by reference to Dr Jenkins' initial model which explained combinatorial testing at Box 6.1 of HJ1. If Dr Jenkins' very broad "Bundle" category happened to contain two elements, one of which was profitable and the other loss-making, it is intuitive that running an alternative combination which included only the profitable bundle category would generate a higher bundle contribution to common costs, and therefore allow lower headroom for SFV to make a common cost contribution within the overall constraint of no over-recovery of such costs. The broader the set of products within Dr Jenkins' "Bundle", the greater is the scope for some such sub-bundle to exist which would yield a less favourable SAC Combi result for SFV Services.
823. In response, Dr Jenkins, in the hot tub discussion at Day 14/14, and at a general level, again justified her choice of combinations by emphasising that the relevant "competitive arena" was bundles, so there was no need to disaggregate the various bundles involved. Mr Duckworth thought that this was wrong in principle and that if one shows combinations according to one's view of BT's underlying strategy (which may change over time), that introduced a degree of subjectivity, whereas the test should be applied almost mechanistically. Dr Jenkins' response was that to test every single combination would make the SAC Combi exercise "infeasible and someone had to be pragmatic and it made sense in that context to take into account the behaviour of BT and its rivals in the market".
824. However, the problem about that is that, in the context of BT, and as the Tribunal in *PPC* observed, it may be the case that combinatorial testing is simply not practical because of the number of combinations needed. If that is correct here (and it seems to us that it is), it does seem to us that Dr Jenkins' approach is inconsistent in that respect with *PPC*.

825. In any event, it may not even have been necessary for Dr Jenkins to have tested every single combination. She could at least have employed a number of combinations which disaggregated the bundles. But she was not prepared to do this.

826. There is therefore a problem at a general level with Dr Jenkins' selection of the combinations.

#### BT Sport

827. We now turn to the question of BT Sport. First, it is necessary to set out some background facts. BT Sport was introduced in 2013 and was supplied free of charge with BT Broadband. This stopped in 2015. For the period thereafter, the revenues and LRIC costs generated by BT Sport are set out by Mr Parker at Table 2 to DP4. This shows that, taken by itself, BT Sport has been significantly loss-making in each of the relevant years. The losses range between £443m in 2015/16 and £612m in 2019/20 with an average loss across the claim years of £566m. In 2015/16, BT Sports' negative gross margin was 74.5% compared to, for example, positive broadband gross margins of 50%, and voice at 64%.

828. If one compared this with the revenues and LRIC costs of Dr Jenkins' "Bundles", there are here profits ranging from £601m to £968m, with average profits of £828m. And if one looks at Bundles without BT Sport as a constituent, profits are between £1,180m and £1,580m, with an average of £1,394m.

829. Mr Parker goes on to say (Table 4 of DP4), that if BT Sport was removed from the Bundle, the exercise would then produce a competitive benchmark which was significantly lower than the relevant ARPU for all of the claim years, except for 2020/2021, where the ARPU was less than the benchmark by 57p, and where, for the first 4 years of the claim, the monthly ARPU was about £6 more than the benchmark. This comes about because removing the losses of BT Sport from BT's bundles significantly increases the profits of bundles, and this in turn means that under SAC Combi there is significantly less common cost that is unrecovered when the calculations come to assess the headroom that is available to SFV Services.

830. The arithmetic here is clear enough, but the substantive question is whether removing BT Sport from the BT bundle is consistent with the contestable market theory that underlies the SAC Combi approach. Dr Jenkins' contention is that it would not be valid to do so, since the appeal of (and hence the revenues attracted by) BT bundles was inherently dependent on the fact that such bundles were predominantly supplied alongside the attractive BT Sport product. If a hypothetical standalone supplier of BT bundles absent BT Sport would fail to attract the revenues that were associated with BT's actual bundle sales, then the high profits ascribed to this hypothetical "Sport-less" BT bundle would be illusory, and it would not therefore be consistent with the SAC Combi rationale to include a bundle that excluded Sport.

831. Dr Jenkins said that one should regard BT's strategy as not involving it being a retailer of BT Sport alone, but rather that it offered BT Sport to promote the sale of its bundles. Here, she relies, first, on what Ofcom said in the VULA Margin Statement paragraph 5.90:
- “BT's investment in sports content was to support its broadband business and, in particular, including increasing customer acquisition and retention on superfast broadband packages.”
832. This was in fact in the context of Ofcom rejecting arguments made by BT that the revenues and costs of BT Sport should be excluded from the assessment of its VULA margin.
833. Dr Jenkins also relied upon the Financial Factbook produced by BT on 5 July 2016, which, at page 26, recited that BT Sport was established in 2013 and that it “has helped to drive customer acquisition and retention in Voice, Broadband and TV” and that “the benefits of improved customer acquisition and churn across our core products sit within Voice, Broadband and TV P&Ls”.
834. We see all of that, and of course it would be naïve to think that BT's commercial strategy did not at least include using BT Sport to drive sales of bundles, among other things. That said, there was no direct factual evidence from BT on the point.
835. At Table 10 in Section B4b to the JES, Dr Jenkins has provided figures to show the percentage of BT Sport lines sold in a bundle which included voice (and hence BT lines sold on a stand-alone basis by a process of deduction). The proportions forming part of bundles across the claim years were 93%, 85%, 70%, 67%, 63%, 60%, and finally 57%. In addition, Figure 2 of Section B4c shows that, of those BT customers switching from SFV Services to a BT bundle, 47% switched into a bundle which included BT Sport. The proportions doing so in subsequent years of the claim were 38%, 31%, 30%, 23%, 9% and 10%.
836. As to that, Mr Parker said, if, say, 40% of BT Sport lines were sold separately, that is still significant, and the same could be said about Dr Jenkins' reliance on the proportions of BT customers switching into bundles which included BT Sport. The proportion doing so was always less than 50% and very much less so by the end of the claim years.
837. Mr Parker accepted in the hot tub discussion that if there were no stand-alone sales of BT Sport at all, and it could only ever be purchased in the bundle, his objection based on the inclusion of BT Sport in the “Bundle” would be less of an issue. However, he then pointed out that in fact, there was “a whole chunk of stand-alone sport being operated”. In any event, the SAC Combi exercise still had to be done properly and this could involve a service that did include BT Sport and one that did not.
838. Overall, it does not seem to us to be clearly established that, across the entire claim period, the primary purpose of BT Sport was to act as a driver for the purchase of BT Consumer's other products and as we said above, there was no direct factual evidence on the point.

839. However, even if one accepts Dr Jenkins' claim that BT Sport existed primarily as a device to attract consumers to BT bundles, the exchanges between the experts on BT Sport also revealed a further issue that creates problems for including the BT Sport losses in the SAC Combi calculations. As we note above, the losses actually incurred by BT Sport during the claim period were very substantial. Mr Duckworth questioned whether it was appropriate for the large discrete costs incurred by BT Sport in acquiring content to be accounted for on a cash basis, or dealt with as assets that should be depreciated over the years over which the rights were held. Dr Jenkins responded that to take this approach would be to convert the profit assessment to a return on capital ("ROCE") approach that would be inconsistent with the return on sales model on which all of the profit assessment was based.
840. On a separate point, Mr Parker pointed to the possibility that BT might have adopted other approaches to creating content that attracted consumers to bundles, and argued that such alternatives might have very different consequences for the outcome of the SAC Combi calculations.
841. To deal with these concerns fully, it would have been necessary to conduct a detailed review of the rationale for BT's investments in BT Sport and the accounting treatment. However, the brief exchanges between the experts on these questions did not allow us to reach an informed view on these complex factual questions. In circumstances where there is no evidence as to the underlying investment or costing decisions made in connection with BT Sport, for example, there is no way of knowing whether BT Sport's losses were due to inefficiencies or because some other, less unprofitable strategy to promote bundles (if that is what it was) could have been adopted. This last point reflects Mr Duckworth's evidence on Day 14/5, referred to at paragraph 820 above.
842. In our assessment, this fact highlights a more general concern with reliance on Dr Jenkins' SAC Combi results for assessing the competitive benchmark. Whilst, as we have acknowledged above, the sharing of common costs across different activities means that there is an inevitable interdependence between the profitability of those activities, this feature also means that the task of accounting for all such interdependencies is extremely complex. Where, as in the case of BT Sport, the view taken on the profits of any one element has a potentially transformative impact on the SAC Combi result for SFV Services, this seriously compromises the reliance that can be placed on such results. We see this as a further manifestation of the problem – identified in *PPC* – that the theoretical attraction of SAC Combi can be outweighed by the practical problems that arise from its implementation.
843. Having regard to all of the above, in our judgment, there are two problems with the failure to disaggregate BT Sport from the "Bundle". The first is that, notwithstanding any commercial rationale to use BT Sport to drive bundle sales, it is difficult to conclude on the evidence that it

existed purely as a form of advertising, as it were, for bundles. But secondly, even if there were no case at all to disaggregate BT Sport from the “Bundle”, as a result of the foremost commercial function (which was not satisfactorily established), there remains this further problem: on Dr Jenkins’ model, the huge losses made by BT Sport - its extreme lack of profitability - are driving a very high proportion of common costs to be borne by SFV Services even though BT Sport is an entirely different product from SFV Services. Moreover, this is a conclusion on the particular combinations selected by Dr Jenkins.

Conclusion on the combinations chosen for the SAC Combi exercise

844. Overall, on this issue, we do not find that Dr Jenkins’ SAC Combi approach, or the competitive benchmark that flows from it, can be said to provide a reliable basis for the Limb 1 assessment. If the SAC Combi is to be invoked, it needs to be done in a way that addresses the concerns that have been identified with taking this approach. Ideally, that would involve addressing all combinations. If it is impracticable to do this, there must at a minimum be a proper appreciation of the problem and a credible method must be found for dealing with this deficiency. For reasons we have outlined above, we do not think Dr Jenkins has met this test. Attempting to select particular combinations (and not others) by reference to perceptions of BT’s commercial strategy is not an answer to this point. Further, in the context of the particular SAC Combi exercise undertaken by Dr Jenkins for the purpose of ascertaining a competitive benchmark, this deficiency has real consequences, as is demonstrated by the issue of BT Sport. The view we take here is in keeping with the observations of the Tribunal in *PPC*. While we accept that a firm such as BT is entitled to some flexibility in the way in which it seeks to recover common costs, we do not find that the results of Dr Jenkins’ SAC Combi provide a credible basis for defining the reasonable limits of that flexibility.

*The “Number of Lines Error”*

845. It will be recalled that a critical part of Dr Jenkins’ calculation of the competitive benchmark for SFV Services generated by each combination for any given year is ascertaining the “permitted” price increase. This was done by taking the annual amount of the increase, dividing it by the number of lines and then calculating the monthly increase.
846. However, Mr Parker suggested that there was an error in this calculation. Since the relevant increase was to be added to the actual price of SFV Services i.e. the focal product, it should be calculated by dividing the annual sum by only the lines within SFV Services. However, Dr Jenkins divided it by the much larger number of voice lines existing across the board. The effect of this approach was to understate the allowable SFV price per line under the SAC Combi method i.e. it made Dr Jenkins’ estimates of the reasonable cost-related price for SFV significantly *lower* than they would be had she used the number of SFV lines as the denominator in the calculation. What Dr Jenkins should

have done, according to Mr Parker, is to divide the annual sum by the number of SFV Services lines only. The increasing difference between the number of SFV lines and all voice lines over the years is shown at Table 5 in DP4.

847. Mr Parker says that Dr Jenkins' error is one of logic. That is because it is inconsistent with a theoretical approach whose purpose is to identify the recovery of the differential from SFV Services and therefore its customers, not those who have taken voice services as part of a bundle as well.
848. Mr Parker noted that Dr Jenkins said that her approach was correct on the basis that the same voice prices were set by BT, whether for stand-alone SFV Services or for the voice element within bundles. However, he pointed out that this did not mean that prices for SFV Services and bundles would reflect those voice prices as they changed. This is because bundles overall (which is the relevant "product" to consider) were priced much more competitively. In other words, Dr Jenkins' argument here is simply another manifestation of the "bundle pricing fallacy". We have referred to this at paragraphs 439-447 above.
849. Mr Parker then sets out the consequences of what he says should have been Dr Jenkins' approach in Tables 6 and 7 of DP4. If one divides the annual differential by the number of SFV Services lines only, the resulting competitive benchmark is much higher than in Dr Jenkins' results. Further, since the number of SFV lines decreases over time, compared with all voice lines, this effect is magnified in later years.
850. If Mr Parker is correct and there is this error which, if corrected, would entail the figures shown in Tables 6 and 7, the results do become implausibly high. On that basis, Mr Parker suggests that it shows that the underlying SAC Combi model is defective.
851. As a further example, he shows in Annex A4 to the JES that if the focal product was stand-alone broadband rather than SFV Services (the former, like SFV Services, having relatively few customers compared to bundles) BT could raise its prices from 2019/2020 by around 6,500% before they could be considered excessive. He said that this was in part a function of the fact that Dr Jenkins SAC Combi approach allows a large proportion of overall common costs to be recovered from a product with relatively few customers.
852. In answer to all of this, Dr Jenkins says that the "implausibly large" benchmarks which Mr Parker pointed to only arose because he had departed from giving effect to the commercial practices of BT. His set of prices would not be observed in practice. That was, indeed, because there would only be a single relevant voice price set by BT across-the-board. Dr Jenkins says that this is not a manifestation of the "bundle pricing fallacy" because whether, upon any price increase for voice services across the board, the overall bundle price increases by as much, is irrelevant to the

calculation of the “upper bound” of the cost benchmark for SFV Services (see JES at paragraph 7.1.27).

853. She explained further that when setting how individual products should make up the “revenue gap” there was an element of judgment and pragmatism, which here means that sharing the cost of the differential across all voice lines was appropriate. She said that this was reasonable, having regard to what Ofcom had identified as one particular problem with SAC Combi tests, in its *PPC* Decision of 14 October 2009 at paragraph 5.71. The problem was how to identify particular services within a combination that had led to excessive pricing, where the combination had therefore “failed” the SAC Combi test. However, we do not see how this observation justifies Dr Jenkins’ approach here which, in any case, is in a context where the relevant combinations were under-pricing rather than over-pricing in terms of the results of the SAC Combi test.
854. In the hot tub discussion (see generally Day 14/44-52) Dr Jenkins also suggested that spreading the cost across all voice lines was appropriate because it was “better matched” to the scale of common costs and avoided the problem of excessive loading of common costs upon a small group of customers. However, it seems to us that this is not really a principled application of the competitive benchmarks yielded by Dr Jenkins’ SAC Combi model. In reality, we think that what Dr Jenkins was doing, understandably enough in one sense, was mitigating the effect of her competitive benchmarks by spreading the common costs more widely which would then avoid some of the extreme outcomes pointed to by Mr Parker. That is all well and good, but it does not really answer the point that if the proper application of the SAC Combi model, strictly applied, would produce implausibly high figures, that must cast doubt on its reliability. We agree with Mr Parker about the fact of such results probably also reflecting Dr Jenkins’ inputs which would include her choice of combinations and the common costs figure within BT Consumer that she arrived at in the first place.
855. For all those reasons, we consider that there was a “Number of Lines Error” on the part of Dr Jenkins, and its correction also suggests that there is a serious problem with her SAC Combi model.

#### *Conclusions on Dr Jenkins’ SAC Combi methodology*

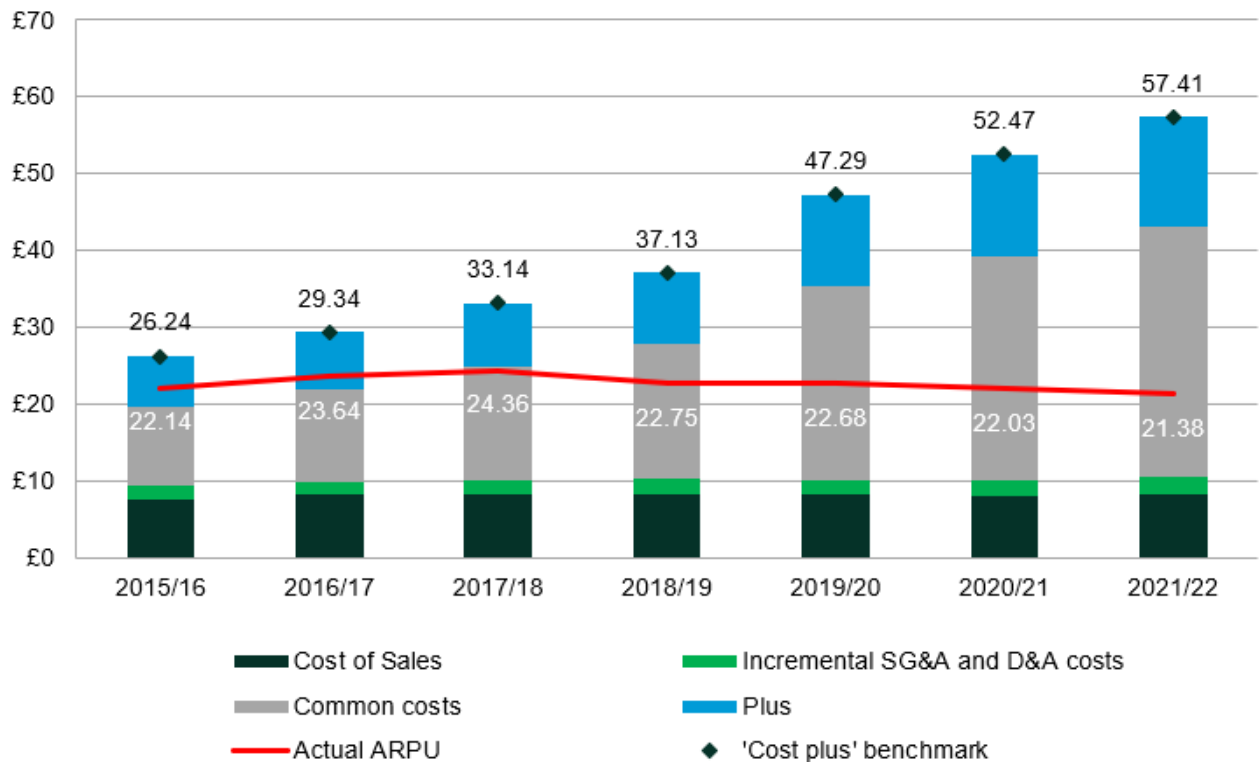
856. Overall, we consider that Dr Jenkins’ approach, insofar as it is based on the SAC Combi exercise, is seriously deficient, and it cannot justify the competitive benchmarks which are said to result from it. However, before dealing with the consequences of that view, we now need to consider Dr Jenkins’ alternative analyses based on DSAC and FAC, albeit these were invoked by her simply as a “cross-check” to her SAC Combi methodology.

## **DR JENKINS' DSAC CROSS-CHECK**

857. Dr Jenkins has undertaken an alternative DSAC analysis as a “cross-check” to her SAC Combi. As is also noted in *PPC*, in contrast to SAC Combi, the DSAC approach does not benefit from being based on the economic theory of contestable markets, but as Dr Jenkins noted (as indeed was the case in *PPC*) DSAC had been recognised as a pragmatic alternative to combinatorial testing, especially where the number of required combinations would be infeasibly large. In fact, as we have pointed out, that problem exists for the combinatorial testing here, as it did in *PPC*.
858. Dr Jenkins calculated the DSAC she considers appropriate here, as follows: she first defined a “broad increment” of services, across which the relevant common costs figures would be applied. This increment contained all the SFV Services (i.e. SLR, Line Rental Saver (“LRS”)) and Line Rental Plus (“LRP”) along with HPS and BT Basic.
859. She then took the common costs figure which she had already derived in her initial exercise (see the table at paragraph 558 above) and allocated it to each individual service within the increment on an EPMU basis, i.e. using the direct costs of each service as the driver. To this figure, she then added the LRIC costs, again, as previously calculated, and the 25% margin. This produced a total annual cost which was then divided by the number of SFV Services lines, and that annual cost was then divided by 12 to reach the monthly competitive benchmark on this basis.
860. The results of that exercise are shown at Figure 6.11 in HJ1:



**Figure 6.11 Comparison between SFV Services ARPU and the DSAC “cost plus” benchmark (baseline common costs scenario)**



861. It will be seen that the competitive benchmark figures start at £26.24 per month for 2015/16 and rise each year, with the benchmark for the final year being £57.41. As can be seen by comparing Figure 6.11 with Figure 6.10, which set out the competitive benchmarks arising from the SAC Combi (as adjusted - see paragraph 500 above), the DSAC benchmarks are significantly higher than the former for every year. In fact, by 2019/20 the ARPU is below the benchmark by around £25 and increasing.
862. The CR makes a number of criticisms of Dr Jenkins’ approach here.
863. First, it is said that, since the DSAC model uses the same derivation of BT Consumer’s common costs as Dr Jenkins had used as a precursor to her SAC Combi, the CRs criticisms there apply equally here. That is correct, and we have already concluded that there are problems with that common costs analysis - see paragraph 816 above.
864. Second, insofar as 25% is not the correct margin, the CR says that this again adversely affects the results of the DSAC model. That is obviously correct, and see our conclusions on margin at paragraph 642 above. Third, and in our view critically, Mr Parker and Mr Duckworth both say that Dr Jenkins’ choice of the elements of the increment are essentially arbitrary in a way which is inappropriate here. In particular, the increment does not include any bundle, including the “Bundle” used as one of the combinations in Dr Jenkins’ SAC Combi. They both consider that her selection of the elements is arbitrarily small.

865. Mr Parker illustrates this by Table 8 in DP4. This shows that if the Bundles were included in the increment, then the level of competitive benchmark is much lower and is then below the relevant ARPU for all of the claim years, and markedly so for the first four of them.
866. In the hot tub discussion, Dr Jenkins defended her choice of increment elements on the basis that this case relates to certain SFV Services which are alleged to have been excessively priced i.e. the focal products. The increment elements should therefore be those services and the other SFV Services which are close to them i.e. HPS and BT Basic, but no other products. It was therefore reasonable to view the increment as being confined in that way. We do not see why this necessarily follows, or why, as a matter of principle, other services (especially those which constitute a large percentage of BT Consumer's services) should not be included as well.
867. On the question of including the bundles, Dr Jenkins said, both in the JES and in the hot tub discussion, that if this was done, then it would yield results almost indistinguishable from the LRIC+/FAC approach. We do not think that this is much of an answer, since if that would be the result, then it might suggest that the sort of LRIC+/FAC approach said to be inherent in the 2009 RFS was itself cross-checked by this iteration of the DSAC model. On any view, it hardly means that such an iteration could not be appropriate.
868. In the hot tub discussion, Dr Jenkins said that if one added bundles to the increment, one was back to asking how common costs should be allocated and then a range of allocators could be used. Otherwise, she just said that she thought that the group she had selected for the increment was the right one. It was therefore another useful piece of information to judge the pricing flexibility that would be observed in the working competitive market. We did not consider that any of these points really address the argument that to use a model which, almost by definition loaded all of the common costs onto just one (decreasing) segment of BT Consumer was arbitrary and inappropriate. As Mr Parker observed (Day 14/64-65):
- “All I have done here is just to illustrate, you could pick another arbitrary combination by also including bundles, and if you do that then you get a much, much lower benchmark. You can see that in Table 8. By the end of the period we are talking about magnitudes of a difference of sort of 250%, if not more. I do not think this really tells you anything, to be honest. I think it just tells you that if you pick an arbitrarily small combination to recover your common costs over at any level of common costs, that will give you a high number relative to picking a broader combination. I think to the extent that all firms in this market seem to be operating on a multi-product basis, I am not sure why you would restrict your attention just to SFV services. So, for me, this does not really add much. This is just a different way of cutting the common cost cake that Dr Jenkins suggests is the right level of common costs.”
869. He added that, in fact, pricing at this level (up to around £50) would simply not arise in workable competition.
870. We consider that the CR's criticism of Dr Jenkins' DSAC model in this respect is well-founded. The criticisms made by Mr Parker seem to us to reflect a number of the concerns we have already

identified with Dr Jenkins' SAC Combi approach, and the difficulties associated with how to account for the BT Sport losses also continue to apply here. We therefore do not consider that the way the DSAC model has been applied by Dr Jenkins in this case provides any greater reliability or certainty.

871. There was a separate debate about the extent to which there was positive endorsement of DSAC models by the Tribunal in cases like *PPC*. The point made by Mr Duckworth was that the DSAC approach approved by the Tribunal there was in the context of the cost orientation obligation exercise (which we described above at paragraphs 646-648) and where some flexibility was indeed allowed to BT by Ofcom, but also in a context (wholesale markets) where there was already an overall regulated price. (In fact, of course, on the DSAC test used by Ofcom, BT was in breach of the cost orientation obligation anyway).
872. Mr Duckworth distinguished that situation from the instant case, where there was no regulated price, and so there was no overall restraint in place to limit excessive pricing and which might therefore imply that any flexibility to recover common costs should be seen in a more limited way. He went on to say that the exercise here was to understand the costs of production and a reasonable attribution of common costs under workable competition.
873. As against this, BT argued that, while there may have been differences in the context of *PPC* and this case, they were essentially irrelevant and in any event, there was an effective price cap here as from 2018 as a result of the Commitments. We are not sure that this latter point goes very far since there is no claim on behalf of VOCs after 2018 and there was no price Commitment as far as the SPCs were concerned. More broadly, however, we would not see Dr Jenkins' use of DSAC as flawed, just because the context here was somewhat different to that in *PPC*. As she said in evidence, it is simply a model to allocate common costs.
874. The real point, as it seems to us, is that for the reasons already given, we considered that her DSAC analysis does not act as a meaningful crosscheck to her SAC Combi.
875. That then leaves Dr Jenkins' further cross-check in terms of her FAC exercise.

### **DR JENKINS' FAC ANALYSIS**

876. This first emerged in HJ2 as a "sensitivity" to Mr Duckworth's RFS approach, which involves a consideration of indirect (i.e., incremental and common) costs as a whole, as derived from the 2009 RFS (uprated by the CPI), which did not distinguish between the two.
877. What Dr Jenkins does is to take the total of BT Consumer's indirect costs, as represented by its SG&A and D&A figures, and allocate them to each service by the use of 3 alternative allocation rules. These are EPMU (direct costs), Revenues and Customers/Lines. Figure 5.2 of HJ2 shows that

on an EPMU-allocated basis, the indirect costs of SFV Services are very similar to those used by Mr Duckworth via the 2009 RFS model - around £40 per year. However, if allocated on a Revenue or Customers basis, the indirect costs yielded by her analysis are significantly higher and the Customer-allocated indirect costs are themselves significantly higher than the Revenue-allocated costs. Further, for the last 3 years of the claim period, the indirect costs allocated on a Customer basis are around the same as Mr Duckworth's competitive benchmark.

878. These differences, as they are worked through to produce competitive benchmarks, are then set out in Tables 6, 7 and 8, at section B4a to the JES, where they are compared to Mr Duckworth's competitive benchmarks. Dr Jenkins points out, as is shown in Table 8, that if Mr Duckworth's 8.9% margin is used instead of 25%, then the ultimate competitive benchmarks as between Dr Jenkins and Mr Duckworth are very similar where the cost driver is EPMU. She uses this fact to suggest that, although Mr Duckworth's position was that, certainly for the allocation of incremental costs, the EPMU costs driver was inappropriate, her analysis suggested that this criticism must also undermine Mr Duckworth's own RFS approach, because the results are so similar. Mr Duckworth's response to this somewhat forensic point is that the similarities were simply a coincidence. Either way, Dr Jenkins' EPMU-based FAC analysis hardly assists her position since it, at least, appears more to corroborate Mr Duckworth's benchmark rather than her own.
879. As to the individual allocation rules, the position of Mr. Duckworth was that none of these were appropriate so far as incremental costs were concerned. That is because the correct allocation method should be costs causality as used in the RFS.
880. Mr Duckworth made some more general criticisms about the individual allocation rules as well. As for Revenue, he said this was an inappropriate driver because there is no reason to think that the level of Revenue correlated to indirect costs, and that was especially so where there might be excessive pricing (of the SFV Services) in the first place because the very fact of excessively high prices would tend to boost the cost measure stated by this approach, thus hiding the very phenomenon one is seeking to measure. As for Customers, Mr Duckworth said that there would be some incremental costs which were not applicable to SFV Services at all (for example, broadband or TV), but this method would attribute some of such costs to SFV Services. Also, he said that this method took no account of the difference in the cost incurred by BT between supplying a customer who has a voice-only product, and another who takes a bundle. The effect of this would be to under-attribute full incremental costs of the bundle services. In the case of both Revenue and Customer allocation rules, there was the point already made that these were not costs causality principles which are the relevant ones so far as incremental costs are concerned.

881. As to this, Dr Jenkins stated that both Revenue and Customers drivers could be appropriate. As for Revenue, she pointed to two particular instances in the Detailed Attribution Methods (“DAM”), document underlying the 2009 RFS where there were references to revenue as an allocator of incremental costs. She referred to the following two statements within this very long document:
- “Product-specific marketing and sales campaign costs are identified and attributed directly to the relevant Products or Line of Business (LoB) revenue streams, with further apportionment's generally derived on a revenue-basis.” ...and “Residential bad debts are apportioned to Products on the basis of revenue”.
882. The context of the first was Marketing and Sales, and looking at the context, the statement appears to refer to some form of sub-apportionment. The second reference concerns Billing and Finance. We do not consider that these points add very much. They arose in the overall context of an extremely detailed method statement applying the general principle of costs causality to the allocation of incremental costs.
883. Dr Jenkins then refers to Guidance Table 2 in the VULA Margin Statement, where the costs allocator for certain items within BT’s SG&A costs were on a Revenue basis. However, this was all in the context of where BT did not show a reasonable breakdown to individual product lines. Here, Ofcom allocated to superfast broadband on a *pro rata* basis using Customers, Product or Revenue. Revenue was only used where there was “no obvious cost driver”. We do not think that this reference is of any real assistance, either.
884. As to the problem of Revenue allocation where there is alleged excessive pricing, Dr Jenkins suggested that this was not a real problem overall, because there would be greater revenue shown for bundles. However, Mr Parker said that this is not an answer since the question concerns the allegedly excessive revenue for the focal product. We agree. Further, BT itself accepted in paragraph 570 of its Closing that Dr Jenkins acknowledged the potential circularity of using this driver in an excessive pricing case.
885. Overall, we think there is significant force in the CR’s criticism of the use of the Revenue driver for the allocation of indirect costs as a whole. That criticism is heightened in relation to the incremental element of indirect costs where costs causality should be the overriding principle. Once again, we are drawn to comment that Dr Jenkins’ reliance on a mechanistic rule here, in the absence of detailed information about what does drive costs, is attributable to BT’s decision not to provide the detail that would be required to provide the evidence that would best inform this issue.
886. As for Customers, the CR accepts that for some incremental costs which are proportionate to the number of customers, this costs driver may be appropriate; in effect, it would be a manifestation of the costs causality principle. But many indirect costs may only apply to certain products. And this costs allocation rule does not distinguish between customers of voice lines only, and those who take

bundles, as noted above. See, for example, how Mr Parker put it on Day 16/67-68 and at paragraph 7.1.4 of the JES.

887. Dr Jenkins' response is to note the use of a Customer driver in the 2009 RFS and in the VULA Margin Statement. We do not consider that the examples provided are of any more use than those in the context of the Revenue driver. Dr Jenkins also says in effect that the failure to distinguish between voice only and bundle customers does not matter, given the extent of the effort expended by BT in seeking to maintain the volume of its customers. See paragraph 7.1.4 of the JES. However, we do not see how this observation of Dr Jenkins really answers the problem. Nor do we see how the fact that BT is a customer-driven business answers the problem.
888. BT also suggests that the problem goes away because of the relatively modest size of the SFV Services customer base as compared to that for BT Consumer as a whole. But we do not see how this affects the fact that there is no differentiation between the different customers.
889. So there are similar problems with the Customer allocation rule to those with the Revenue allocation, and again, this is especially so where it would displace the operation of the costs causality principle.
890. As for EPMU, the CR's overall point is that while there may be justification for the allocation of common costs on this basis, again it is not appropriate for incremental costs because there is no necessary connection between such costs and direct costs. Indeed, Dr Jenkins accepted that "EPMU is not always a correct assumption" and needs to be considered along with other allocators. In the context of her use of EPMU as the cost allocator for BT Consumer's incremental costs (see above), she justifies this on the basis that using her figure, the allocation of incremental costs would not change very much if she used Revenue or Customer drivers instead (see Table 11 and Annex B4d to the JES). We see that, but this is largely a function of the fact that on her analysis, incremental costs form a very small proportion of total indirect costs, because of her view on the scale of common costs. In any event, BT did not in the end rely much upon the FAC analysis based on EPMU. One can see why, since its results generally produce competitive benchmarks similar to those of Mr Duckworth.
891. A further point made by Mr Duckworth concerns the fact that the number of customers does not exactly match the number of lines. In the event, this was true only for those customers who took BT Sport as a stand-alone product, and Dr Jenkins stated that these were not counted (see her Note to Table A4.1 in HJ2).
892. As to this, it is certainly correct to say that at the beginning of the claim period, that discrepancy was not likely to make much difference (and see our reference to the BT Sport figures at paragraphs 827- 836 above). Later on, however, there is some difference in the resulting benchmarks, as is set

out in the new tables shown at paragraph 577 of and also Annex 4 to the BT Closing. Following the exchange of closing submissions, the CR took exception to this material, as there was no backup evidence for the new tables, and yet Dr Jenkins must have been involved in creating them. It is also correct that there is no detail as to how the addition of the relevant BT Sport customers was translated into the underlying calculations.

893. Nonetheless, we take account of paragraph 577 of the BT Closing. In reality, it is a matter of common sense that in a period where nearly all BT Sport customers were not stand-alone anyway, to add those who were was unlikely to make any real difference, whereas later on, it did.
894. As it happens, we do not think that the separate point about a discrepancy between the total number of customers and number of lines, while it is correct in respect of BT Sport, is a major point against Dr Jenkins' FAC Customer analysis. But there are other points which, as already noted, showed real problems with it.
895. In general, on her FAC analyses as a whole and their role as a form of cross-check, Dr Jenkins suggested that all of these exercises show that one needs to use a range of allocators. This criticism might have some validity in a situation where there was no information available at all regarding cost drivers, but in the current case we do have such information (in the form of the RFS, albeit that this exercise related to a prior time period) and, more significantly, the absence of contemporaneous information about cost drivers and common costs is entirely due to the decisions BT has taken not to do the work to provide it, even though it was feasible to do so.
896. Nor do we accept BT's submission that Dr Jenkins' cross-checks show that a range of possible competitive benchmarks are consistent with workable competition. This is because there are real difficulties with each of her cross-checks. Just because there is a number of different analyses, and permutations thereof, it does not follow that all of them are correct, or that the right approach is to be found in a simple average from the various individual flawed approaches.

## **OVERALL CONCLUSION ON THE COMPETITIVE BENCHMARK**

### **Introduction**

897. It will be seen from the above that we do not reject either expert's methodology entirely, and thus we do not accept in either case that no reliance can be placed on the other's expert methodology at all, although each party invited us to do just that.
898. Instead, and perhaps unsurprisingly, we considered that, because each side's methodology contained a number of problems, it is necessary to strike a balance in terms of the outcome that reflects the weight which we consider should be given to each methodology in respect of:

- (1) the starting point for common costs, being the proportion of BT Consumer's total indirect costs that should be represented by common costs ("the Common Costs Starting Point");
- (2) the proportion of such common costs that should be borne by SFV Services ("the SFV Services Common Costs Contribution"); and
- (3) the application of the 13.5% margin on the total costs of sale ("Application of Margin").

899. This exercise will result in a specific competitive benchmark which can then be compared to the ARPU for the year in question. The percentage excess over the competitive benchmark can also be shown. On the basis of those figures, an assessment will be made as to whether there is an excess of the ARPU over the competitive benchmark that can be regarded as significant.
900. The above exercise will be undertaken, first, in relation to 2015/2016. We will then consider the most appropriate method of dealing with the figures for the following years, and again, ultimately assessing the nature and extent of any excess of the ARPU over the competitive benchmark.
901. The question as to whether any excess over the claim period is also persistent will also be addressed.
902. We should add, equally unsurprisingly, that it is impossible in an exercise like this to be able to reach figures as if undertaking a scientific calculation. Indeed, both sides' experts accept that their approaches involve the exercise of their own, albeit professional, judgment. The same is true of our approach here. We have endeavoured to reach figures on the basis of the totality of the materials (including expert views and the parties' submissions) put before us that seem to represent the most appropriate outcomes. We have done so on the additional basis that if there were to be a minor adjustment here or there to our figures, the overall outcome will not be materially affected.

## **2015/2016**

### *The Common Costs Starting Point*

903. Dr Jenkins' baseline scenario uses a starting point of BT Consumer's common costs being £390m out of a total indirect costs figure of £983m. The former thus represented about 40% of the latter. See the tables at paragraphs 558 and 785 above. On her low scenario, such costs became £262m or 27% of the total indirect costs.
904. We should add that in this context, there is no Common Costs Starting Point figure from Mr Duckworth which can feed into the analysis here. This is because the RFS contains no information on the split between incremental and common costs, and neither Mr Duckworth nor Mr Parker provided any estimation of BT Consumer common costs except to argue that they were very low. For the reasons given above, we do not accept that they were very low.



905. In our judgment, the appropriate Common Costs Starting Point is £250m. This recognises the problems with Dr Jenkins' approach which mean that in our view, even her low scenario common costs figure is too high.

*The SFV Services Common Costs Contribution*

906. Having established the size of the common costs within BT Consumer as a whole, the next task is to assess what proportion of that common cost can reasonably be recovered from SFV Services. Looking at the picture overall, we consider that a reasonable balance is struck where SFV Services are permitted to recover around 40% of the total common costs. Here, we bear in mind that under Dr Jenkins' SAC Combi approach, and applying an assumption of a 25% margin, the SFV Services' contribution to common costs would be 62%. It would fall to 56% if a 20% margin was deployed (because of the way in which the margin is itself part of each SAC Combi calculation), and of course we proceed upon the basis of a 13.5% margin, which would suggest (using Dr Jenkins' approach) a contribution to common costs of a little below 50%.
907. Some context for this is provided by the fact that the SFV Services voice lines constituted only 28% of the total number of voice lines in 2015/16. Equally, so far as revenue is concerned, SFV Services revenue, as a percentage of BT Consumer revenue, was 18% in 2015/16. See the Table at paragraph 558 above. Hence, allowing SFV services to recover as much as 40% of common costs reflects the principle that firms in competitive conditions should enjoy a considerable degree of flexibility in how those costs are recovered, recognising of course that this flexibility is not unbounded.
908. 40% of the starting common costs figure of £250m (see above) is £100m on an annual basis. That figure, on a per line annual basis becomes £37.45 and on a monthly per line basis becomes £3.12.
909. It is possible to make an approximate comparison between the approaches of Dr Jenkins and Mr Duckworth on this aspect, so as to identify where our conclusion falls between the opposing experts' positions. It will be recalled that Mr Duckworth arrived at a total indirect cost per SFV line in 2015/16 of £32.86 per annum, which, with 2.67m SFV lines, implies a total indirect cost for SFV of some £88m. Since we know that the actual SG&A and D&A costs of BT Consumer totalled £983m in 2015/16, the £88m of SFV indirect cost in Mr Duckworth's approach amounts to some 9% of the total.
910. Due to the nature of the incremental cost+ approach adopted in the RFS, there is no way to identify specifically how Mr Duckworth's £88m of SFV indirect cost splits between incremental and the common cost contribution that he believes it is reasonable for SFV services to make. However, it is possible to make a broad inference of this split by comparing the results of Dr Jenkins and Mr Duckworth. In her base case, Dr Jenkins estimates that the incremental indirect cost per SFV line is £1.76 per month, or £21.12 per annum. If we subtract that incremental cost figure from Mr

Duckworth's "incremental + " figure of £32.86, the difference – which is £11.74 – represents a measure of the annual common cost per SFV line that lies within Mr Duckworth's competitive benchmark. Across the 2.67m SFV lines in 2015/16, that would generate an implied common cost contribution of around £31m. This can be compared with the £100m of common cost contribution that we have permitted to be made by SFV services and the £242m that is implied by Dr Jenkins' base case. (The comparison on a monthly common contribution per SFV line is £0.98, £3.12 and £7.75 for Mr Duckworth, our conclusion and Dr Jenkins respectively).

911. We then need to make one further adjustment before proceeding to a calculation of the competitive benchmark. As we have adjusted the estimate of total common costs within BT Consumer's indirect cost downward to below Dr Jenkins' base case, it follows that some of those costs now removed, as it were, would constitute incremental costs that should be allocated to SFV Services. There is no definitively correct way to do this (in the absence of a proper cost causality exercise), but we recognise that some upward adjustment to Dr Jenkins' incremental cost figure of £1.76 is required to compensate for this. We use her figure of £1.76 as a reasonable starting point because there is no alternative incremental costs figure from the CR and it is conservative (in the sense of being relatively low) because of both the high proportion of BT Consumer's overhead costs that Dr Jenkins deemed to be common costs, and because it allocates the remainder of those overheads to the different BT Consumer products on the EPMU basis which is the rule that assigns the smallest share of incremental costs to SFV.
912. Here, it will be recalled that for 2015/16, Dr Jenkins' base case was for £390m of common costs. If the figure we have proposed of £250m is used instead (see above), there is then £140m of indirect costs that must necessarily be deemed to be incremental over BT Consumer as a whole. If one allocates these costs on the basis of the proportion of SFV Services' lines to the total number of lines in 2015/16, in other words, 28%, this would yield an upward adjustment to SFV incremental cost of £1.22 per month. If, alternatively, one allocates these costs in line with the 9% ratio between Mr Duckworth's estimate of SFV indirect cost and actual BT Consumer overheads this would yield a smaller upward adjustment of £0.39 per month.
913. We consider it is reasonable to take a pragmatic approach here, and adopt a position mid-way between these alternative approaches. The midway point between 28% and 9% is 18.5%. Allocating 18.5% of the £140m to SFV incremental cost yields an upward adjustment of £0.81 per line, which in turn yields an adjusted total incremental cost figure for SFV Services of £2.57 per month in 2015/16.

### *Application of Margin*

914. The 13.5% margin, which we consider is the appropriate one, expressed as a percentage of total revenue, including the margin, is then applied. This yields a monthly net profit figure of £2.15 per SFV line.

### *Resulting Figure for 2015/16*

915. The calculation entailed by the above, on a monthly per line basis, is as follows:

- (1) Total costs excluding margin: £13.75;
- (2) Margin: £2.15;
- (3) Therefore Competitive benchmark: £15.90 ( (1) plus (2) above);
- (4) ARPU: £21.86;
- (5) Therefore excess of ARPU over competitive benchmark is £5.96, or, in percentage terms, 37.5%.

916. We consider that, on the facts of this case, an excess of this magnitude is significant.

917. We then have to consider the position going forwards over the entire claim period. We should reiterate here that neither side suggested that we should “slice up” the claim so that there may be particular years where there is a significant excess and others where there is not, and in any event we have to consider whether the excesses that are entailed by our calculations are persistent as well as significant. We therefore turn now to the following years.

### **The following years to 2021/22**

918. Going forward from 2015/16, the approach of the two experts again differed. Mr Duckworth’s CPI index uprates the total incremental costs figure from 2015/16 to the later years. Dr Jenkins, on the other hand, re-does (a) the BT Consumer common costs calculation for each successive year, with the reported overheads (SG&A and D&A) for each year as the starting point and then (b) the SAC Combi exercise for each year, which produces the ultimate competitive benchmark which itself includes a per month per line incremental cost allocation and common costs contribution.

919. Because there are uncertainties surrounding the increases in the reported overheads and whether such increases in truth, represent or include increases in costs that are common to all or some of the BT Consumer services, including SFV Services (which we discussed at paragraphs 720-737 above), we do not consider that it is appropriate simply to use each year’s total reported overheads as a starting point across the whole period. In particular, we have taken the view that a significant element of the increase in overheads in 2019/20 which was said to be due to a reclassification of

internal recharges must in fact have been due to costs which were not common across the different products sold by BT Consumer.

920. A further, and more significant, concern with Dr Jenkins' SAC Combi results is the way in which they generate an increasingly large positive gap between her competitive benchmark and BT's SFV ARPU. Whereas in 2015/16, Dr Jenkins' competitive benchmark permits SFV Services to make a monthly contribution of £7.50 per line to common costs, this figure increases to over £11 in 2017/18 and exceeds £16 by 2021/22. Since we do not accept that the SAC Combi approach provides a reliable basis for the competitive benchmarks chosen by Dr Jenkins in this case, and we also have significant misgivings with the way in which Dr Jenkins has applied the SAC Combi theory to SFV lines, we see no reason why our competitive benchmark should need to reflect the profile that arises from Dr Jenkins' calculations over the claim period.
921. Instead, we consider that a fair and reasonable approach is to create an index, drawn from an adjusted set of BT Consumer reported overheads. That index can then be applied directly to the monthly per line common costs contribution which we considered was appropriate for 2015/16, adjusted as described above for the costs in Dr Jenkins' base case that we have disallowed for the purposes of our assessment, and allocated to incremental cost. The basic incremental costs figure calculated by Dr Jenkins for each year is applied without modification.
922. As for the index itself, until 2019/20, this is based on the percentage increase (or decrease) in the total reported BT Consumer overheads. However, when it comes to the more substantial increase in 2019/20, which was something of a "step change" we consider that the position is different for the reasons given in paragraph 919 above. The precise adjustment to be applied is obviously somewhat broad-based, especially as we have no information about the reclassification, other than the document attached to the 30 November 2022 letter. Nonetheless, and taking a cautious approach, having carefully considered that document, we consider that a reasonable adjustment is to set a figure for 2019/20 which is £1,150m, as opposed to the reported figure of £1,229m. In money terms, this means that the increase we are prepared to allow is £79m, half of the £158m.

923. Going forwards beyond 2019/20, we then use the amount of the increase reported each year, but now applied to the modified figure of £1,150m, rather than £1,229m. The index and its derivation is set out in the table below.

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
Actual BTC overhead (£m)	983	975	1,025	1,071	1,229	1,240	1,261
Adjusted BTC overhead (£m)	983	975	1,025	1,071	1,150	1,161	1,182
Adjusted BTC overhead index	100.0	99.2	104.3	109.0	117.0	118.1	120.2

924. This index is applied to the reasonable common costs contribution per SFV line which we set for 2015/16 and to the adjustment to the incremental cost figure that we described above for 2015/16. We then put this together with the actual annual data for ARPU, direct costs and Dr Jenkins' estimate of incremental cost for each of the claim period years, which allows us to compare SFV revenues with a competitive benchmark across the claim period.
925. The results are summarised in the table below. It is notable that the estimated overcharge increases substantially over the first 3 years of the claim period, and then falls back, especially in the final year 2021/22. There are several factors at play here, but much of this pattern is explained by the trends in two variables: the ARPU, which increases and then falls back; and the index we have calculated from BT Consumer's overall indirect costs (as adjusted in the manner described above) which causes the allowable common cost recovery per line to increase towards the latter part of the claim period. The simple average overcharge across the 7 years of the claim period is 38%.

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
ARPU (£/month)	21.86	23.8	24.59	23.23	23.29	22.67	21.95
Direct costs	8.06	8.73	8.32	8.37	8.2	8.06	8.38
Incremental costs	1.76	1.69	1.77	1.85	1.89	1.94	2.08
Common cost per line plus incremental cost adjustment	3.93	3.90	4.10	4.28	4.60	4.64	4.73
Total cost excl margin	13.75	14.32	14.19	14.50	14.69	14.64	15.19
Margin (at 13.5%)	2.15	2.23	2.21	2.26	2.29	2.29	2.37
Comp benchmark inc margin	15.90	16.55	16.40	16.77	16.98	16.93	17.56
Excess profit as % comp benchmark	37.5%	43.8%	49.9%	38.6%	37.2%	33.9%	25.0%

926. In respect of those figures, we consider that any excess would have been significant if it was 20% or more above the competitive benchmark. Given the figures which we have found, it follows that for each year of the claim period, the percentage excess is clearly established as significant. Even if a significance threshold was as high as 25% (which we do not accept) the relevant excess would be established. Yet further, even if that were not the case for the last year in particular, it remains the case that on an average basis across the claim period, the percentage excess would be significant.
927. In the light of the figures above, we also conclude that the excess was persistent, because it applied across the whole period.

### **Overall Conclusion on Limb 1 Figures**

928. It follows from the above that the Limb 1 threshold is met because the prices charged by BT for the SFV Services over the claim were significantly and persistently in excess of the competitive benchmark we have arrived at.
929. This means that it is necessary, finally so far as liability is concerned, to consider, under Limb 2 of *United Brands*, whether such excess was unfair, so that an abuse of dominant position on the part of BT is made out.
930. Given that we have concluded that there was excessive pricing overall, it is not necessary to consider the CR's alternative case which was that there was such pricing at least in relation to line rental. It will be evident from our earlier discussion, however, that we would see significant problems in drawing any conclusions on the competitiveness of the SFV market from focusing on line rental alone, due to its inherently partial nature.

## **LIMB 2 (1): UNFAIRNESS "IN AND OF ITSELF"**

### **Introduction**

931. It is worth summarising at the outset, the key elements of each party's case on this first category of unfairness (as distinct from unfairness by comparison).

#### *The CR's case*

##### Excessive Price

932. So far as the CR is concerned, its starting point, and a major one at that, is that the extent of the excess here was very substantial. On a weighted average basis, the excess over the period was between 74% and 90% for each of the claim years except 2021-22 when it was 60%. If one took the average excess, according to the CR, it would have been 78%. See the table at paragraph 497 above.
933. In fact, of course, the CR cannot use that starting point, or anything like it, because we have concluded that the excess is between 33.9% and 49.9% for all of the claim years bar the last one,

where it was 25%, yielding an overall average excess of 38%. This figure is just under half of the CR's average of 78%.

934. This is a dramatic difference in the starting point, in our view, and it reduces the ability of the CR to say (as it has here) that the extent of the excess here is so substantial that it either entailed unfairness in and of itself, or, in any balancing exercise, it would be a strong factor against BT.

No distinctive value provided by BT

935. The CR also contends that there was no real economic value to put into the equation by reason either of BT's Gives, or BT's brand value. Furthermore, on the question of brand value, there was, in truth, no real evidence of positive or strong customer satisfaction.

Ability of SFV customers to switch

936. A primary point of principle taken by the CR is that the ability of customers to switch did not, and could not, demonstrate economic value in BT's SFV Services. On that footing, the ability to switch and the fact of switching were irrelevant to a consideration of unfairness. In any event, even if they were relevant, they did not actually assist BT here.

Market Dynamics

937. Insofar as BT would rely upon any migration intent or rebalancing, these do not stand up to scrutiny and in any event, are not relevant to unfairness.

BT's conduct was exploitative

938. Next, the CR submits that there was a significant element of customer exploitation here - BT knew that it had real market power, and it knowingly sought to get what it could out of the VOCs and SPCs in a declining market. In this regard, it was also acting in a non-transparent fashion. Further, it so acted in the knowledge of Ofcom's increasing concern over its pricing.

The views of Ofcom

939. The CR also relies upon the views of Ofcom to support its position because the CR maintains that Ofcom's views were, in reality, to the effect that BT's pricing was unfair.

*BT's case*

Excessive Price

940. For BT, necessarily, if the Limb 2 stage has been reached, as it has been, it means that BT has lost on Limb 1, and there was indeed a significant and persistent excess. Having contended otherwise, it did not adopt an alternative position for Limb 2 which assumed a particular level of excess. Nonetheless, it is obviously implicit in BT's position that the lower the excess which has actually been found by us, the more there is to play for in relation to other factors which are relevant to unfairness. Subject to that point, the key aspects of BT's position are set out below.

#### Provision of Distinctive Value

941. Contrary to the CR's position, BT submits that there was indeed real economic value in the SFV Services provided, which included the value of the Givès and BT's brand value. Moreover, there was in fact sound evidence of positive customer satisfaction.

#### Ability of SFV customers to switch

942. In contrast to the CR, BT contends that as a matter of principle, the availability of the alternatives, and the ability of the SFV customers to switch, as demonstrated by the fact of their switching, is indeed relevant and, on the facts, highly so, as a counterweight to the excessive pricing. It indicates that those who stayed with BT (while they stayed with BT) were ascribing positive subjective value to the landline product and/or the brand.

#### No exploitation

943. Next, BT denies that there was, on the facts, any exploitative conduct on its part towards the relevant customers.

#### Market Dynamics

944. Contrary to the CR's submission, BT contends that wider market dynamics, such as migration intent, declining call volumes and rebalancing can and should be taken into account in its favour.

#### Flat ARPUs

945. BT also points to the fact that whatever may be said about its gross margin for SFV Services or the existence of the excessive pricing, ARPU itself remained broadly flat.

#### Price Dispersion and Workable Competition

946. BT argues that it is important to adopt a workable competition standard when assessing Limb 2, and not one of perfect competition. A workable competition approach should in turn be informed by the kind of variability in prices and margins that is observed under real world competition, and in BT's Closing in particular it drew attention to the dispersion that is present in the bundles market, which the CR and its experts agree to be workably competitive, as a guide to this task.

#### The position of Ofcom

947. BT rejects the position taken by Ofcom in the 2017 review as lending significant support to the CR's case. In particular, it points out first, that Ofcom took no remedial action in terms of price regulation as against the SPCs. Second, it found that BT's call pricing (which formed an essential part of its pricing overall) was competitive. Third, Ofcom was acting within a regulatory framework which therefore limits what support can be derived from it; indeed, the Tribunal should be careful not itself to engage in "regulatory overreach" when considering whether there was an abuse of dominant position here. Fourth, Ofcom had a particular motivation in relation to seeking a price reduction for



VOCs because of their perceived vulnerable characteristics which may be seen as a policy goal distinct from the Chapter II criteria and market power exploitation *per se*.

*The Tribunal's analysis*

948. The above set of key points ascribed to the parties is not an exhaustive list of their submissions on unfairness, but it gives an overall picture and illustrates the main areas of dispute between them.

949. Against that background, we propose to deal with the following matters, in this order:

- (1) Extent of the excess;
- (2) Provision of economic value:
  - (a) Generally;
  - (b) Gives;
  - (c) Brand value;
  - (d) Ability of customers to switch;
  - (e) Conclusions;
- (3) Workable Competition Factors;
- (4) Existence or otherwise of exploitation by BT of its price insensitive customers;
- (5) Price Rise revenue used to fund non-SFV investments;
- (6) Disproportionate impact of price increases on SFV customers;
- (7) Lack of transparency;
- (8) Price Rises during period when Ofcom expressing concern;
- (9) Market Dynamics;
- (10) Ofcom's own findings;
- (11) Regulatory Framework considerations;
- (12) Conclusions.

950. Finally, we should add that we take VOCs and SPCs together, in the sense that they both form elements of the Class, even if some factors going to unfairness apply to them in different ways, or to different extents. Indeed, as already noted, the CR's case does not include an alternative claim for VOCs only. It stands or falls on establishing abuse in relation to both elements of the Class.

**Extent of the Excess**

951. We have already noted in paragraphs 932 - 934 above the dramatic difference between the excess we have found and the excess contended for by the CR. In our view this means that the significantly lower applicable excess which we have found carries much less weight in the overall balancing exercise entailed by this part of Limb 2, than would have been the case with the higher Limb 1 excess contended for by the CR.

## **Provision of Economic Value: (a) Generally**

### *Introduction*

952. It will be apparent from our analysis below that although neither side confined itself to examining whether BT's excessive prices (as now found) bore a reasonable relation to the economic value of SFV Services, the answer to this question formed a major part of their submissions.
953. In particular, and as will be seen in detail below, and as noted above, BT contended that the provision of the Gives by BT and its brand value as perceived by its SFV customers showed that its prices did bear a reasonable relation to their economic value. That conclusion was supported in a significant way, contends BT, by the fact that in this case, the SFV customers were not "captive", in contrast to the purchasers in the pharmaceutical cases. On the contrary, there were no barriers to SFV customers switching to alternative voice-only suppliers or to bundles. Moreover, such switching did indeed occur to a very substantial extent each year.
954. For its part, the CR did not agree with any of the core propositions advanced here by BT; there was no, or no sufficient, additional value provided by the Gives, nor did the SFV customers in fact ascribe a positive value to BT's brand, and finally, any question of ability to switch was simply irrelevant.
955. The dispute between the parties here revealed two issues of principle which we should resolve at the outset:
- (1) The extent or level of economic value that needs to be shown; and
  - (2) The relevance or otherwise of the ability of customers to switch.

### *The Extent or Level of Economic Value Required*

956. In evidence, Mr Parker adopted what we consider was too high a threshold for the existence of any relevant economic value, by using the expression "unique". In the event, the CR, in his closing submissions, did not go so far. Rather, he contended that there needed to be some "distinctive" value provided. The expression "distinctive" derives not from *United Brands* or *Phenytoin*, which simply referred to whether the price bears a "reasonable relation" to economic value. As already noted at paragraphs 76-81 above, the expression was deployed in *Hydrocortisone* and we are content to adopt it in the way set out in paragraphs 82-83 above.

### *The Relevance of the ability to switch (or not)*

957. We have already noted the undoubted fact of extensive switching on the part of SFV customers either to other voice-only providers or (in more cases) to bundles, in paragraphs 163-177 above. We have also concluded that the principal reason for such switching was not as a reaction to the

particular prices charged by BT but because of the secular trend away from voice-only services or separate voice and broadband contracts, towards bundles instead – see paragraphs 211-303 above.

958. BT relies upon the ability of SFV customers to switch, and the fact of their switching, as a significant factor in the determination of unfairness or otherwise. This is not because it is some free-standing further economic value point in and of itself (see Day 28/35). Rather, BT contends that it suggests that since customers could (and did) switch, for those who stayed (while they stayed) they should be assumed to have ascribed positive economic value to their BT landline. See also paragraph 689-701 of BT's Closing. This contention is then said to be supported by Dr Hunt's evidence.
959. On the other hand, Ms Kreisberger KC argued that the ability to switch is irrelevant at the Limb 2 because it has nothing to do with the economic value of the SFV Services.
960. For our part, and as a matter of principle, we would accept that in theory, the ability to switch and the fact of switching (or not switching) can be relevant to economic value. For one thing, the fact that a product may have some additional economic value cannot itself be a defence to a claim based on unfair pricing if the customers are in a truly captive market in all respects and have nowhere else to go. This is the essence of the Willingness to Pay fallacy. In such a case the excessive price will not bear a reasonable relation to its economic value. On the other hand, if the customers are not captive, then it would be easier to ascribe a reasonable relation to the underlying economic value. This reflects what Dr Jenkins said at paragraph 6.104 of HJ2, referred to at paragraph 690 of BT's Closing.
961. Put another way, it may be possible to infer that those who stay with the product have actively chosen to stay (since it was open to them to switch but they have not) because they subjectively attach a positive value to the product or the brand. Of course, all of this depends on the facts and the whole question of the existence or otherwise of customer inertia here (dealt with below); but in principle, we consider that the phenomenon of switching can be legitimately relevant in this way.
962. Beyond stating those principles, it seems to us that the existence of a reasonable relation to economic value (or not) is highly fact-sensitive, as well as being a matter for the exercise of judgment. The resolution of this question also depends, of course, on the extent of the excess of the price over the competitive benchmark because the particular price is the "thing" which must bear a reasonable relation to the economic value.

#### **Provision of Economic Value: (b) Gives**

963. We consider the specific features and points made about each of the Gives below. We then consider some other points relevant to the Gives.

964. Before doing so, we should mention one important point of context. It is that there was evidence from Dr Hunt (which was not seriously challenged) that a number of surveys showed that the SFV customers, and in particular VOCs, tended to use their landlines more to make outgoing calls than BT customers generally or indeed UK landline customers generally. In particular, in 2016, the SFV customers made on average 246 minutes of outgoing calls per month which fell somewhat to 213 minutes by 2022. The equivalent figures for BT customers overall and all UK landline customers were 155/140 and 90/66 respectively. Further, although landline usage had declined generally between 2016 and 2022 this decline was far less pronounced for BT's SFV customers. See paragraphs 389 and 397 of SH1. Dr Hunt's evidence was that this preference for use of landline services existed despite 72% of VOCs and 92% of SPCs having access to a mobile phone, according to Ofcom's 2017 Narrowband Market Review residential survey. Dr Hunt, by way of explanation, pointed us to evidence that VOCs valued traditional telephony for better sound quality and reliability, and also because it tended to give them easier access to their social networks. Increased usage of landlines would therefore arguably make some of the Gives, like Onshoring, Call Protect, and Care Level 2/Fault Fix Guarantee more valuable to SFV customers than others.

#### *Onshoring of Customer Call Centres*

965. This was the process of having all of BT's call centres for BT Consumer customers (including those with and without voice services) located in the UK. It started in 2016 and by 8 January 2020, BT had brought 100% all of its call centres onshore. According to slides produced by BT dated 30 November 2016 ahead of a meeting with Ofcom in respect of its proposed Retail Narrowband Market Review, the cost of onshoring for 2017/18 was £42.2m.
966. Although this was available to all BT Consumer customers, as Ms Blight made clear in evidence, almost all of such customers had voice services; the exception were those who subscribed only to BT Sport, which was a small proportion.
967. At paragraph 51 of MB1, Ms Blight said that onshoring was a specific response to customer feedback in 2016, and was against the trend of the industry at the time. In fact, it seems that by 2015, Sky had two contact centres in Scotland and three in England, although it is not suggested that Sky had no offshore call centres at that time. On this point, Dr Hunt's evidence was that by 2016, about 60% of BT's call centres were in the UK, and BT was the first company to achieve 100% onshoring in 2020.
968. Ms Blight also said at paragraph 51 that having onshore call centres was important to the perception of good value for money and improved customer service. She added this:

“For a subsection of the customers that frequently called contact centres, connecting them to an advisor with a local accent was important. We learned that some of BT's customers found it difficult to understand foreign accents, especially certain older customers or those with hearing difficulties. Now we route calls locally as it

is easier for customers to understand people that are local to them, and they perceive this as better customer service.”

969. In cross-examination, Ms Blight said that, while the only benefit she had identified was an adviser with a “local accent”, others at BT would say that the service was better with onshore contact advisers, and her customer services colleagues would feel that they got better results and outcomes, leaving aside the question of local accents, although she herself could not speak to this. Later on, she said that someone from customer services who was more *au fait* with the onshored contact centres would say that there were fewer repeat calls, less aggression and things like that. Calls to the contact centres took place not just when something went wrong, but also when a customer wanted to change their contract or plan, or when they were moving home. She also said that she was cynical about the level of latent racism that might be involved in the perception of the benefit of a local rather than a foreign accent.
970. Notwithstanding Ms Blight’s cynicism in that respect, we think that the thrust of her written and oral evidence was that consumers ascribed real benefits to having all contact centres onshored. This impression is supported by the BT Consumer Business Unit Review for Q1 2017/2018, dated 20 July 2017 at page 32 where it stated that BT was answering 86% of service calls onshore, with improvements in the average answer time down from 1 minute 43 seconds in Q4 to 1 minute 11 seconds in Q1 and the overall environment was more stable and predictable. BT’s Consumer Brand NPS Heartbeat report for August 2017 also stated that one of the things which customers were talking about that month was that “service was getting better since bringing the contact centre back into the UK”. (NPS stands for Net Promoter Scores. It is explained in paragraphs 1034 and 1035 below.)
971. It is quite true that the onshoring of the call centres was for the benefit of all BT customers. However, we do not consider that this detracts from its value to SFV Services customers, as a sub-group of BT Consumer.
972. Further, it cannot be said that there was only “limited uptake” of this Give since it operated whenever a customer wished to call a BT call centre.
973. We accept that this Give was not technically innovative as such, but this does not prevent it from having some real positive value for customers, which was achieved ahead of the competition, and we consider that it did.

#### *Call Protect*

974. This was introduced in November 2016 as a free service to all voice customers (i.e. including those who had bundles) and it followed the 2015/16 price change, which took effect on 3 July 2016.

975. According to a BT document dated 15 October 2015, it was estimated that it would cost £3.2m to provide. However, slides produced by BT dated 30 November 2016 ahead of the meeting with Ofcom referred to above, gave it a total 2017/18 cost of £11.8m.

976. Ms Blight said as follows about this in MB1:

“47. BT Call Protect is a service which helps prevent customers from receiving scam or nuisance calls. This product allowed customers to report the numbers associated with scam or nuisance calls, which were then blocked for them and the rest of the BT Consumer customer base. The more customers that used the product and reported scam numbers, the better it was for all our customers, and particularly our vulnerable customers. That’s why providing it for free as a customer give made it a much improved and more effective product (as this resulted in more people using it, meaning we were able to block more scam numbers) than if we had charged for it.

48. I felt very passionately about BT Call Protect and we talked about it a lot with Ofcom. The feedback we were getting from customers (which I believe started in 2014/2015) was that customers who used landlines frequently were annoyed by scam and nuisance calls. However, customers that didn’t really use their landlines to make calls only tended to interact with their landlines when receiving these scam calls and so found them even more troubling. We wanted to give customers more control and protection from scammers. We had previously developed a landline handset with protective calling features, but we wanted to create a product that would help all customers without requiring them to buy a new phone. I recall that the Citizens Advice Bureau and Ofcom published their concerns on this issue. There was also an industry wide consultation with the Department for Culture, Media and Sport in early 2016. I remember attending cross industry discussion forums in Parliament to discuss the issue of nuisance calls and what we, as an industry, should be doing about it. I believe BT was the first service provider to launch a product of this nature and, in my opinion, it was the best on the market. BT Call Protect didn’t receive much media attention on its initial launch in 2015/2016 so we promoted it during the following price change in 2016/2017 to encourage customer uptake and further improve the service.”

977. That evidence, as such, was not challenged. We infer from Ms Blight’s evidence, that there was clearly some public concern about the issue of scam or nuisance calls in 2015/16, requiring a public consultation and discussions in various industry forums which all suggests it was a significant issue at the time. As is implied by Ms Blight there and confirmed in oral evidence, customers did have to make a positive choice to use the service and to report numbers associated with scam or nuisance calls they received, but then the numbers were blocked for them and indeed for all BT Consumer customers.

978. There was no suggestion that the product was ineffective. Indeed it was reported (BT’s Q1 Consumer Unit Business Review, 20 July 2017) that BT’s Call Protect was diverting about 2m calls per week from numbers associated with scam and nuisance callers; this also supports the thrust of Ms Blight’s evidence that this was an important problem for BT and the industry as a whole.

979. As already noted, Call Protect started operating in November 2016 following the price change on 3 July 2016. However, it had been prefigured in advance. BT’s Q1 2016/17 Operational Review dated 29 June 2016 noted at page 37 that 43,000 customers had already signed up in advance; in fact, page 63 of the same document said that 56,000 customers had expressed interest. In cross-examination, Ms Blight said that while the total voice customer base was around 9m, this was a huge “advance uptake” ahead of the actual launch of the product.

980. By 20 July 2017, 2.2m customers had Call Protect (see BT's Q1 Consumer Unit Business Review of that date referred to above). This would have been out of all of BT Consumer customers who had a landline.
981. However, in Annex 2 to its Closing, the CR has pointed to a BT document on drivers for value for money ("VFM") dated 21 December 2017, which suggested that only 8% of BT voice customers were signed up, while 69% of customers were unaware of Call Protect. These figures seem inconsistent with the figures referred to in paragraph 980 above. This document was put to Dr Hunt in cross-examination. It had not been cited by him in his report. He accepted its contents, but questioned what the survey base was and whether it included the online base of voice customers. On this particular point, we agree that there is an uncertainty which may explain the discrepancy with the earlier figures. We should add that the conclusion on this page of the document was that Call Protect had a positive influence on the VFM scores of the BT customers surveyed, but not to the same extent as competitor offers, in terms of its impact or reach. The strength of those conclusions might, of course, have been affected by the same uncertainty as to the base surveyed.
982. Further, a BT document dated 14 March 2021 shows that of the then 800,000 landline-only customers, 45% now had Call Protect.
983. We suspect that the discrepancy in the figures is explained by whether the relevant group is landline-only customers or all customers who had voice. After all, in terms of who was registered, this must be a matter of fact. If so, there is no reason to doubt the actual take-up figures in any of the documents. In addition, since any number blocked from calling a particular customer was also blocked across the BT Consumer customer base, the numbers who benefited would be considerably more than just those registered to use it.
984. Subsequent to the introduction of Call Protect, Sky introduced a similar product called Talk Shield in June 2017, and in January 2018, TalkTalk introduced Call Safe. Further, Phone Co-op provided a "Choose to Refuse service". It is not clear when this was first introduced, but we do note that there was a maximum number of telephone numbers that could be blocked, which was 10. We also note that Ms Blight had said in paragraph 48 of MB1 that the BT product was the best in the market. More significantly, we do not accept the proposition that just because other suppliers had introduced similar products, this meant that the product of the firm in question cannot add significant value, especially where BT appeared to be ahead of its competitors, at least initially.
985. It is true that there was also the Telephone Preference Service offered by Ofcom and referred to in its Consumer Guide to Nuisance Calls and messages produced in 2015. This offered partial protection for customers, as Dr Hunt accepted in cross-examination. But it was clearly not as extensive as Call Protect, and it was not suggested by the CR that it was.

986. Ms Blight was also asked about Call Protect in the context of the price changes. In emails sent on 28 September and 10 October 2016 in relation to the next price change, which was 2017/2018, Laura Van-Daal, Head of Broadband and Voice, expressed the concern that customers might question why Call Protect was being used as a justification for more than one price change, namely 2016/17 (even though it was not implemented until November 2016) and 2017/18. While the action points in this document noted that there should be “very careful positioning” in pre-notification communications and “strong defence statements” for advisers, this document does not say what they were. Ms Blight considered that, nonetheless, the main message about the Give came in 2017/18, as it was already in operation, then, and this email was just a matter of “people’s interpretations”. We do not think that this is really an answer to the obvious points being made in the email. That said, we see no reason in principle why, for the purposes of assessing value, that value is necessarily diminished simply because during its subsistence, there is a price increase.
987. Overall, we consider that there was real and positive value to Call Protect, even though customers had to take the step of reporting the scam and nuisance calls made to them. In our view, the value extends beyond the active users, i.e. those who had reported a nuisance call which was then blocked, and indeed beyond those who had registered for the service. This is because such customers had the reassurance that there was a free service from which all received protection. This must have assisted with the customer concerns that Ms Blight mentioned in MB1 referred to in paragraph 976 above.

#### *Care Level 2/Fault Fix Guarantee*

988. Prior to the 2015/16 price change, all voice customers were entitled (through BT) to Openreach’s Care Level 1 (“CL1”) service, whereby all faults on the line were supposed to be fixed within two working days. With this price change, BT provided all voice customers with Openreach’s Care Level 2 (“CL2”), which came at an additional wholesale charge to BT of 53p per customer. This level of service provided for faults being fixed by the next day. According to Ms Blight, this came at a cost to BT of some £40m. A BT Consumer document recording a meeting on 24 October 2018 put the CL2 cost at around £50m per annum.
989. In fact, CL2 proved not to be much of an improvement on CL1, since the actual fault repair rate under CL1 often fulfilled the service level of CL2. So customers who experienced faults might not have noticed much of a difference. Accordingly, BT decided that there should be a more tangible commitment to a particular level of service, which led to the introduction of the Fault Fix Guarantee (“FFG”), under which BT would pay all voice customers £20 by way of compensation if the engineer took longer than 2 days to attend, or his attendance was cancelled on less than 24 hours’ notice. Initially, FFG was provided in addition to CL2, as from the April 2017 price change. We should add that, according to Ms Blight, FFG came in earlier, because she was the one who launched



it, which means that it would have to have been introduced prior to her going on long-term leave in the autumn of 2016. We accept this, as she clearly had first-hand knowledge of the launch.

990. Subsequently, the provision of CL2 was terminated for all voice customers, apart from those who had BT Basic, HPS or LRP. A BT document of 24 October 2018 stated that this change would be implemented in April 2019. FFG itself ended in April 2019 when BT joined Openreach's Automatic Compensation Scheme.
991. It is correct that FFG was another "opt-in product", as opposed to some form of automatic compensation being paid as a result of a delay in attending to a problem.
992. However, even so, this seems to us to constitute a positive benefit. Moreover, and as Ms Blight explained, this was more than just compensation for the period when the landline was not available and in this respect it differed from competitors' products. The latter just offered a "pro-rata" compensation depending on the time lost, which would be very much lower than the fixed sum of £20 or £25 being offered by BT. So, for example, if 3 days were lost and the customer was paying £18 per month, then the total compensation received from a competitor would be £1.80.
993. Dr Hunt was taken in cross-examination to Ofcom's Automatic Compensation consultation paper dated 24 March 2017. This made the point at paragraphs 4.6 and 4.7 that the compensation offered by the 4 largest landline and broadband providers (including BT) had to be asked for by the customer, and that most customers do not ask for compensation. Under paragraph 4.28, BT's compensation terms were set out, dealing with loss of service, delayed provisioning and missed appointments. The last one would appear to be the area which FFG was to address. Here, it was said that where an appointment was not kept, a one-off fixed rate payment of £10 could be claimed. If it is correct that FFG was launched in late 2016, then this may have been the missed appointments provision referred to in the Ofcom document. The only question is the payment of £10 since the evidence otherwise points to £20 or £25, but perhaps it was increased from £10 at an early stage. In any event, we do not consider that this document adversely affects the value or otherwise of FFG.
994. It is true that there may have been a period for most customers when CL2 had been removed, but FFG remained in place. It is suggested that this shows that the total amount of benefits had reduced. However, in our view, this is unrealistic, given that Openreach seem to have achieved CL2 timetables even while customers were on CL1, which was the reason BT thought it was uneconomic to keep paying for the CL2 service. The real change was FFG and this was clearly different from the offerings of competitors.

995. Overall, we consider that there was positive value here although, it did require the customer to take action first, and it was not in place for the whole of the claim period.

### *Right Plan*

996. This was introduced with the December 2014 Robin/Window price change. It was a digital tool available for all voice customers and it would advise them as to whether, on the basis of their existing voice usage, they were on the best plan in terms of costs, and if they were not, the plan they should transfer to. Customers could register for it online but it also appears that they could do so by calling BT's Contact Centre. It was discontinued in October 2017.
997. In cross-examination, Ms Blight suggested that the Right Plan tool could also be used by advisers in BT's call centres, although when customers called to discuss their contracts, the advisers should simply go directly to what would be a more beneficial calling plan, for example. This was in the context of Ms Blight being asked to consider an email dated 18 May 2015 from Hazel Morgan to Ms Van-Daal, Mr Bunt and others, following a training call the previous day about the impending Laika price changes for 2015-16. This email read, in part, as follows:
- "Right Plan
- A refresher on what it is and where it sits on useful links on Agent. Advisors should not promote sign-up but should be aware where it sits should a customer ask them to sign them up if they can't be steered online."
998. While Ms Blight agreed that sign-up to Right Plan should not be actively promoted, according to this email, she said it did not really matter because advisers were expected to recommend the best deal for the customer (for example, retention deals) in any event. We see that, but nevertheless, the uptake of Right Plan could obviously have been more, if it was actively promoted.
999. Subject to all of that, however, Ms Blight accepted that it would not be of much use to someone who did not have access to the internet.
1000. A BT document from January 2017, consisting of briefings to various parties, suggested that since the inception of Right Plan, 200,000 (of a total number of voice customers of 9m) had registered for Right Plan and those customers who switched as a result saved over £11.24 per month which is obviously a significant saving. The actual number of customers who did switch and made the saving is not given. A point was made by Mr Armitage to Ms Blight in cross-examination that this was not really conferring any additional value because the customer should have been on the cheaper plan anyway. Ms Blight agreed, assuming that their usage had remained the same as the previous month. However, for our part we do not think that this deprives Right Plan of any value it would otherwise have had. Where there are various options for the customer, and they are not on the cheapest deal, there is a saving to the consumer to be told expressly that there are cheaper options, especially where their usage had changed during the contract.

1001. It is, of course, true that for the majority of customers who did not use Right Plan, some may have missed out on having a better deal. Ms Blight agreed but added that the sort of people who would register for Right Plan would be those who already thought their bills were too high, in other words, the people who did not may have been on the correct plan anyway. We think this is too speculative, not least because those who thought their bills were too high might call the contact centre anyway and if so, Right Plan would probably not figure at all.
1002. At the outset of Right Plan, there was a Project Window 2014/15 update dated 7 March 2014. At page 3, Right Plan was summarised thus:
- “Optimiser - Concept updated to “Right Plan”
  - a service that customers can sign up to on BT.com and through call centres
  - By signing up, customer gives us consent to analyse their usage every month (for 6 months) and to send an e-mail with a recommendation to move to the right calling plan
  - This has the following benefits –
  - Significantly lowers volume risk in call centres as no immediate saving for an agent to offer customers
  - Limits financial exposure due to the need to click through an e-mail/send coupon to redeem offer
  - More relevant recommendation for customer as it is based on latest usage”
1003. The reduced volume risk to call centres is understandable since the more that appropriate price plans were activated via the link on the email advising the customer of the best plan or, it seems, by redeeming a coupon which accompanied a letter sent to the customer, the fewer would need to contact the call centre. The reference to “limits financial exposure” seems to suggest, and Ms Blight in the end agreed, that this was about the lower revenue entailed by putting people on a cheaper plan, because customers still had to jump through some “hoops” to be put on the better plan. In fact, pages 6 and 7 of the same document make this clear. There is there a reference to sending a letter. The service operated for 6 months, with monthly communications and there would only be one offer for the customer in that period. Because of the steps needed to take up the offer, and assuming to begin with that 400,000 users took up Right Plan in 2014/15, the ultimate cost to BT in terms of lost revenue was said to be £0.8m.
1004. Finally, Ms Blight was taken to a BT “16/17 Pricing Portfolio” document, dated 13 January 2016. Here, there was said to be an impact on Financials of £0.1m, and Ms Blight accepted that this looked like the cost to BT, although it could have been just the cost for that year’s iteration of Right Plan, which was there described as Right Plan III.
1005. Overall, we consider that although a useful tool for those customers who used it via the internet or otherwise were referred to it when calling the call centre, it is overall of very limited significance and value. Of course, it terminated in 2017, anyway, part way through the claim period.

#### *Caller Display*

1006. This was introduced in 2005 (or possibly 2008, but in any event prior to the claim period) which allowed all voice customers to see the number of the person calling them.

1007. This was not one of the key Gives relied upon by BT or the subject of Ms Blight's evidence. Indeed, Dr Hunt accepted in cross-examination that he thought everyone offered it and it was not distinctive.
1008. BT had offered it free of charge originally, but then charged for it. From January 2014 it continued to do so until prohibited by Ofcom in September 2018. On the other hand, as at November 2015, both Sky and TalkTalk were offering a similar product free of charge.
1009. In this regard, we thought that paragraphs 449 and 450 of SH1 overstated the value of Caller Display, as became clear when he was cross-examined about them.
1010. In those circumstances, we do not consider that anything of real value was added by Caller Display and it may be disregarded.

*Other Points about the Gives*

Cost and imitation by others of Gives

1011. Mr Parker suggested that a Give should be discounted if inexpensive to provide. In fact, it cannot be said that Onshoring, Call Protect or CL2 were inexpensive to provide. However, in any event, just because a Give may be inexpensive to provide does not mean that from the customer's point of view, it does not confer real value.
1012. Mr Parker also suggested, as part of his "uniqueness" argument which we have already addressed in general above, another reason to discount a Give is if it was later copied by rivals. We do not agree with this, either. It does not alter the fact that, here the SFV customers enjoyed something of value which had not previously been available.

Email exchanges in June 2016

1013. In an email to John Petter dated 14 June 2016, the then CEO, Kevin MacDonald attached a summary of NPS, and said, among other things, that 66% of the customers stated that they were aware of at least one of the "gives" with the price rise, the most common gives being recognised were more Wi-Fi hotspots and increasing broadband speeds. He sent a similar email to Ms Blight on 17 June in which he said:

"In terms of awareness of the 'gives', we have 66% of customers aware of at least one of them. The challenge we have is that there is relatively low awareness of several of the 'gives' – we do need to boost this in order to reinforce our value for money credentials. The big hit we're currently taking on NPS is directly related to a declining performance with VFM."

1014. Ms Blight's response was to say:

"It would be great if we could discuss this as it is quite different from the feedback we've had elsewhere and implies we should be taking quite a different strategy. It could have a big impact on our approach for 1718"

1015. In cross-examination, where it was suggested that the Gives were therefore not feeding through into better NPS, Ms Blight said that at this stage, prior to the implementation of the price change on 3 July 2016, these were relatively early days for assessing the NPS of Gives. We did not fully

understand that response, as there were a number of Gives in operation by that stage. On the other hand, this exchange seemed to be about BT Consumer customers generally (or certainly includes those who had broadband) and in any event, Ms Blight's response at the time was to say that the feedback she had had was quite different. So we do not think this exchange is really a point against BT.

Annex 1 to BT's Closing

1016. This summarises BT's price changes for line rental and call charges for each year of the claim period and the preceding price changes, in addition to (i) other proposed or considered price changes for a given year, (ii) gives and propositions considered and/or offered for that price change, and (iii) references to key witness and documentary evidence, as relevant.
1017. We have considered this document to assist on the detail of the price changes and the 5 Gives, and other offerings.
1018. As for the detailed references to how proposed price changes were considered, debated within BT and ultimately implemented (or not) we do not take issue with the factual narrative set out in Annex 1. In particular we accept that in general, BT would seek to provide (or continue to provide) Gives at around the same time as the price changes.
1019. We also recognise that there were various other promotional offers at different times. For example:
- (1) BT gave, in relation to the 2014/15 price change, 12 months free evening and weekend calls to customers who re-contracted;
  - (2) In 2015/16, free calls to BT mobiles were added to inclusive call periods, and physical handsets which allowed customers to choose the type of call they received were offered at a discount to re-contracting customers;
  - (3) For 2018/19, a personalised calling plan called My Anytime Calls was introduced.
1020. We note matters such as these but do not consider that they materially add to whatever value was in the 5 Gives.
1021. We note from Annex 1 that there were a number of price changes, or other Gives which were not ultimately implemented. We do not see the relevance of this, save that, unsurprisingly, BT gave careful consideration to its landline offerings on a regular basis. But there is no suggestion that its competitors did not do likewise.

### The Aim of the Gives

1022. The CR submits that a principal purpose of providing the Gives was to mitigate bad press and regulatory scrutiny when BT raised prices. In other words, there was a degree of cynicism about providing the Gives. Two particular documents are relied upon.
1023. First, the Project Window 2014/15 Pricing Update dated 24 February 2014. This stated that one of the objectives was to avoid negative criticism of price changes by “Regulator, Public Affairs and the Media”, among others, with the introduction of Right Plan having as one of its objectives, mitigating bad press from price changes by giving a positive message.
1024. Second the Stakeholder plan for pricing dated 4 April 2016. This stated as follows;
- “Problem statement:  
We face increasing regulatory scrutiny of price changes focussed particularly on the treatment of vulnerable customers. We face criticism that our increases in Line Rental disproportionately impact digitally excluded customers, who don’t benefit from competitively priced Broadband and associated discounts from that service.
- “This year’s price change has a number of gives for these customers
- Existing BT Basic and HPS customer don’t see a price change
  - Customers can save money and freeze their price until 2019 by taking Home Phone saver 2019
  - All Standard Line Rental Customers see an improvement in Care Level
  - UAC customers get free calls to BT Mobiles and an extremely competitive SIM offer
  - UK Call Centres news (which could be even bolder for the regulator)
  - BT Nuisance Call Protect”
1025. The above was then said to tackle “regulatory and customer concerns head on”.
1026. Further, Ofcom’s 2017 Provisional Conclusions at paragraph 4.61 stated that:
- “...internal documents from BT suggest that adding additional services when introducing price increases is driven by the desire for a positive PR message and regulatory concerns about pricing rather than pre-empting a competitive response.”
1027. Finally, it was pointed out that Mr Bunt had accepted in cross-examination that deflecting regulatory scrutiny and mitigating criticism and bad press were some of the purposes of the Gives.
1028. We do not think that there is anything in this point. We would be surprised if BT (or any other major provider to consumers) was not conscious of its PR image or the attention of the regulator. At the end of the day, the question is still what value to consumers the Gives really provided. If they gave real value, it is hard to see why BT’s motivation in providing them, if simply for PR or to deal with regulatory attention, for example, should matter. Equally, putting the point a different way, if the Gives added no real value, the fact that they were well-intentioned would not alter the position.
- Gives being available to all bundle customers as well
1029. The CR says that the fact that the Gives were also available to all bundle customers, where pricing, on any view, was more competitive, means that they cannot constitute any or any significant economic value in the context of at least the SPCs since they could not justify the differentials

between the prices charged to the SPCs and bundle pricing. We do not agree; it does not mean that Gives cannot constitute economic value from the point of view of the Class Members, which ultimately has to be assessed by reference to the impact on those customers and the excess which we have found.

Gives did not materially enhance Class Members’ perceptions of their SFV Services

1030. The CR here relies upon the NPS documents which we consider below in the context of brand value. In our conclusions here, we take into account what we say at paragraphs 1047-1072 below about NPS, insofar as they are relevant to this point.

Customer indifference towards SFV services

1031. The CR here relies upon the “Solus - Landline only - customers - NPS and customer experience insight” survey document which was referable to VOCs (“the March 2019 Survey”) which, again, we discuss below at paragraphs 1061-1067. Our conclusions here take account of what we say there.

*Conclusions on the Gives*

1032. We consider that Onshoring, Call Protect and CL2/FFG did constitute distinctive value for the reasons given above.

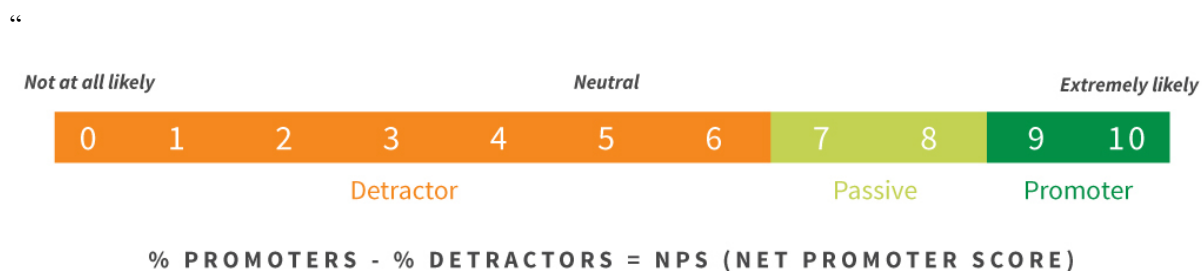
**Provision of Economic Value: (c) Brand Value**

*Introduction*

1033. At this point it is necessary to say something in general about BT’s NPS (Net Promoter Scores) documents, because there is an issue as to the extent to which (if at all) the CR was entitled to rely upon a number of them for the purpose of submitting that they demonstrated that by reason of low levels of customer satisfaction, it could not be shown that SFV customers attributed any or any significant value to the BT brand.

*What are NPS?*

1034. The use of NPS is not, it seems, unique to BT. It is a form of measurement of customer experience (sometimes referred to in the documents as “CX”) used by a number of businesses. Footnote 291 of SH1 refers to the Net Promoter website which explains NPS thus:



The NPS Calculation

Calculate your NPS using the answer to a key question, using a 0-10 scale: How likely is it that you would recommend [brand] to a friend or colleague?

Respondents are grouped as follows:

- **Promoters** (score 9-10) are loyal enthusiasts who will keep buying and refer others, fueling growth.
- **Passives** (score 7-8) are satisfied but unenthusiastic customers who are vulnerable to competitive offerings.
- **Detractors** (score 0-6) are unhappy customers who can damage your brand and impede growth through negative word-of-mouth.

Subtracting the percentage of Detractors from the percentage of Promoters yields the Net Promoter Score, which can range from a low of -100 (if every customer is a Detractor) to a high of 100 (if every customer is a Promoter).”

1035. This is reflected in the body of Dr Hunt’s footnote and we did not understand his explanation to be controversial. It will be noted that the middle band of responses (scores of 7-8/10) are not part of the “netting-off” exercise. It follows that an overall positive score indicates that of those surveyed, a greater proportion were Promoters rather than Detractors and vice versa.

#### *Use of BT’s NPS documents at trial*

1036. A number of these NPS documents, which dealt with customer perceptions of BT’s brand and VFM generally, were put to Dr Hunt in cross-examination and relied upon by the CR in closing submissions. On Day 18, Mr Parker was asked about the NPS documents and the background to their production. He accepted that he had requested sight of them in January 2024 (so after he had produced DP4 and after the JES had been produced), but he did not refer to them for the purposes of the JES. Because they had not been raised earlier, they were not referred to by Professor Loomes in his report and Mr Parker only made a brief comment in DP4 about NPS, which itself was a response to what Dr Jenkins had said in HJ1 in the context of customer inertia. The NPS documents were uploaded to the Opus system during the trial on 15 February, i.e. after BT’s witnesses had finished giving evidence.

1037. BT objected to this reliance by the CR on the NPS documents, on the basis that all such documents could and should have been put to Mr Bunt and Ms Blight, who could plainly have shed light on various aspects of them, as they were both very familiar with them and made general references to them in their WSs. Therefore, BT submitted that we should not place any material weight on them at all, although it did not seek their exclusion as such. We therefore deal first with this objection.

1038. At a broad level, there cannot be any real doubt about the essential nature and purpose of these documents. They were explained by Ms Blight in paragraph 45 MB1 as follows:

“45. In our pricing strategy, and in considering which customer gives to offer, we would monitor our NPS, which included a consideration of value for money perception amongst customers. A company’s NPS is based on a survey asking respondents how likely they are to recommend that company to a friend or colleague on a scale of one to ten. Customers are also able to add comments to their response. We used both transactional



NPS (meaning after a customer had an interaction with one of our contact centres, they would receive a text message asking for feedback) and brand/product NPS (where we would go to a specific section of the customer base and ask how they felt about BT and the products they had with us). My team would go through this data to understand the drivers of our score going up or down. This informed our marketing, pricing and how we communicated with our customers, because it provided valuable insight into customers' perception of value for money and their experience of our service."

1039. In cross-examination, she accepted that she was there saying that NPS was a key metric used to analyse things like the effect of Gives.
1040. It is also fair to say that the NPS-related documents which we have seen show that, whatever lack of clarity there may have been in some instances as to precisely which group of customers was interviewed and how, BT obviously placed considerable importance on the NPS. It is unrealistic to suggest that in those circumstances, if one or more of these documents were put to Mr Bunt and Ms Blight, they would have sought to deny their general significance.
1041. However, with "first-hand" experience of the documents, as it were, they might well have explained particular NPS documents or scores in context, and they were simply not given the opportunity to do so. For example, the June 2016 email exchange referred to at paragraphs 1013-1015 above shows that Ms Blight's immediate reaction to the points made by Mr MacDonald about the NPS was that it did not match the feedback her team had received. We also recognise (and deal with below) some uncertainty as to the extent to which VOCs were involved in the surveys carried out for the purpose of collecting NPS. The documents could easily have been put to them and they clearly had the experience and ability to comment on each of them.
1042. In the event, a number of the NPS documents were put to Dr Hunt in cross-examination (which BT did not object to), in the course of which he indicated the ones that he had seen before, even if not quoted in his report. In re-examination, he said that he had seen many of the documents before and then said that he had seen some of them before he wrote his report, but probably not every single one. He also said that for the purpose of writing his report, he relied mainly on the WSs of the BT witnesses. He would then "drop into" BT's documents, where he felt it necessary to understand more of what was going on. That approach does not seem very satisfactory to us because either not all the relevant BT documents were supplied or made available to him, or his use of them was selective.
1043. However, he appeared to us to be very familiar with the nature and purpose of such documents. Indeed, he relied upon NPS documents in this way at Section 7.4 of SH1:
- "430. Furthermore, internal BT documents suggest that customer service improvements have had a direct impact on uplifting its Net Promoter Score (NPS), which is a measure of how likely customers are to recommend their provider to a friend or family member.
431. In conclusion, notwithstanding the fact that customer service does not appear to be the most important value driver for Class Members, BT has been making investments over time to develop and improve the quality

of its customer service. The market outcomes (as can be seen from the metrics on problem resolution and the NPS index) support the notion that BT is offering good quality customer services.”

1044. In those circumstances, the CR was well-entitled to put the NPS documents to Dr Hunt.
1045. In the light of all the above, we disagree that we should give no weight at all to any of the NPS documents relied on. However, in considering their weight, we very much bear in mind that they were not put to Mr Bunt or Ms Blight.
1046. With that caveat in mind, we will consider each of the NPS documents relied on and give it (and the NPS documents generally) such weight as we think fit. We turn to that assessment now, followed by our assessment of other materials said to go to brand value, as invoked by BT and Dr Hunt.

*Survey Base for NPS documents*

1047. We now turn to the question of the customer survey bases used for the NPS. At a high level, and as pointed out by Ms Blight in paragraph 45 of MB1, the surveys took the form of customer feedback, either following a particular interaction with BT or in response to targeted enquiries of a particular group of customers.
1048. In evidence, the NPS documents were first referred to by Mr Parker (and then Dr Hunt) in the Limb 2 hot tub discussion on Day 17. We deal below with what they drew from the contents of such documents, but the point is that they were discussed at that stage.
1049. In the context of discussing reaction to Gives, Dr Hunt said that the NPS surveys were conducted through ongoing online panels and the only people on those panels were those who regularly used the internet. He went on to say that where Gives consisted of innovations over time, it may be that the main beneficiaries would be those without the internet so their views about Gives would not be captured by NPS. We see that although, since SPCs did have internet access, there would be no reason why they at least could not take part in an NPS survey.
1050. Mr Parker suggested that the references in certain NPS documents to “line only” must have meant line-only BT customers. The difficulty with that is that such customers could have been SPCs as well as VOCs. Indeed, the November 2019 Consumer Brand NPS Report stated at page 8 that due to the nature of online surveys, “line only” customers were mainly BT customers with broadband from another provider i.e. SPCs.
1051. Mr Parker also relied upon a reference to “fieldwork” which he interpreted as connoting face-to-face discussions. However, the March 2019 Survey document which was referable to VOCs only, referred at page 4 to fieldwork using the usual approach for quantitative surveys with self-completion. So “fieldwork” does not mean face-to-face surveys. Both this error, and the previous one noted in paragraph 1050 above illustrate the problems with an expert to some extent having to

speculate on documents on important points where there is no clear underlying factual underpinning (such as detailed explanations given by Mr Bunt and Ms Blight in cross-examination)

1052. As for Dr Hunt, he accepted in cross-examination that NPS surveys would encompass SPCs although he did not know in what proportions. He also accepted that some VOCs could be covered in the surveys. In fact, in SH1 at paragraph 172, he said that on the basis of Ofcom's Residential Consumer Survey, 35% of VOCs accessed the Internet roughly every day and a further 6% did so once a week. That gives a total of 41%. This was all in the context of discussing the true characteristics of Class Members. Of course, and as Dr Hunt fairly said, this does not mean that all of such VOCs would have done an online survey although there was no reason in principle why they could not.

1053. In broad terms, it appears that the NPS surveys were done online by the customer answering questions and giving scores, and such customers could include SPCs who had internet access just like any other customer who had a bundle. It would also in theory be possible for VOCs to participate also, since in practice, a significant proportion accessed the internet in other ways, but the proportion of VOCs that did so here is unknown and probably not large. That said, in cross-examination, Mr Parker also accepted that the NPS documents he relied on did not themselves set out the detail of the method or any concerns about it which might be extremely important.

#### *Particular NPS documents*

##### Introduction

1054. The key purpose for the CR's reliance on the NPS documents is to support the claim that this data in general does not demonstrate any real value or importance given to the BT brand, or its landline products, by the SFV customers. Although a number of these documents are referred to in order to make different points, we think it is most helpful to consider all the relevant aspects of each document in one go, as it were, and to do so chronologically.

##### Consumer Brand NPS Heartbeat report, September 2017 ("the September 2017 Brand NPS report")

1055. This recorded that BT's Brand NPS was -6, one up from the previous month which was -7. This made the BT Brand the second lowest performer, with TalkTalk at -7, Sky at 9 Virgin at 5 and Plusnet (owned by BT but a separate company) at 20. However, this score is of limited assistance since it is referable to all of BT Consumer's customers. The same is true for page 19, where on the VFM scores, BT was the lowest at 22 with Sky at 27, Virgin Media at 29, TalkTalk at 42, Plusnet up 57 and EE (also owned by BT) at 36.

1056. However, page 14 stated that while BT results for other products had improved, its score for "Line Only" was -13, which was a reduction of 1 from its previous score. Dr Hunt accepted that this would

delineate SFV Services but with the caveat that for reasons already given, the customers surveyed here would be principally SPCs. Nonetheless they form part of the Class and so this statement is at least of some significance. This page also stated that improvement was more likely for better products, and Dr Hunt accepted that this document was saying that landline only was not one of the better products.

#### The Drivers of Value for Money - 23 November 2017

1057. This is specifically directed to the metric of VFM, described as a key driver of NPS, Churn and Acquisition and accounting for 25% of Brand NPS.

1058. Page 5 repeats the Brand NPS scores given in the September 2017 Brand NPS report. Page 7 repeats the VFM scores. There were said to be 11 different drivers for VFM across 4 groups namely Price, Brand, Product and Relationship. BT's net score across these drivers was significantly worse than its leading competitors in each case. BT did not "own" any particular driver, in other words have a leading score. On "Trust", BT was 13 points behind the leading competitors. Product was said to be a better performing area for BT which should focus on points of difference to derive "Unique Offer", later said to be Sport, Ultrafast, so not landline. In cross-examination, Dr Hunt accepted that this showed that BT was not viewed as a distinctly trustworthy service provider across all products for the whole online consumer base. That is obviously what the document says but again, this is the whole BT Consumer customer base rather than only SFV customers.

#### Consumer Brand NPS Report, March 2019 ("the March 19 Brand NPS report").

1059. This report set out different NPS sectors within BT Consumer, one of which was "Landline Relationship NPS". At page 5, BT was shown as the worst performing at -5, with Virgin Media at -3, Sky at 5, TalkTalk at 6 and Vodafone at 11. As Dr Hunt accepted, this was a measure of the likelihood of the customer recommending the landline service to a family member or colleague. The CR accepts that here, landline relationship refers to all customers who had a landline i.e. it would include bundle customers. However, page 4 listed Brand NPS by cohort/product holding, and under "Single Landline", BT's score was -25. It was circled in red to indicate that BT was the lowest performing brand although with this cohort, no other provider had a score. Dr Hunt accepted that this cohort was confined to SFV customers, but again with the caveat that they would principally be SPCs. Given BT's very high share of SPCs, it seems hard to envisage a situation in which a panel research study would derive meaningful comparisons between BT and other SPC providers, and this probably explains the absence of any rival operator score on this measure.

1060. All of this data was referable to the period March 2018-March 2019.

#### The March 2019 Survey

1061. This was produced on 13 March 2019. It shows the results of a survey which consisted of telephone interviews with 1,000 VOCs between 29 January and 11 February 2019. By then, of course, such VOCs were paying the discounted line rental price following the introduction of the Commitments the previous year. BT considered that this was a large-scale statistically robust base to analyse. It noted as follows:

This difference in methodology, and the fact that the interviews are interviewer-administered, rather than self-completion, can lead to more positive ratings as respondents seek to please the interviewer.

This means scores cannot be compared with those from the Brand & Relationship NPS survey (which are the published Consumer NPS results each month).

1062. Although the survey had a second purpose, which considered reaction to different letters sent to customers about the Carmen (i.e. Commitments) discount, the first purpose and the only one considered in this document, was NPS and customer experience including value, ease-of-use, recognition and call quality, in other words limited to the landline product. It should be remembered that by this stage, the number of VOCs was no more than around 1m.

1063. The overall NPS was 31, indicating that more than half the base were Promoters (i.e. customers who gave scores of 9 or 10). BT's analysis of the survey data showed that value was the main driver for positive recommendations at 44%, although feeling valued/recognised and that personal needs were being met, drove 40% of the NPS, and reliability drove 15%. BT considered that it was nonetheless underperforming on value, notwithstanding the very high scores being given by many of those surveyed, and that the overwhelming sentiment was that BT was "OK, nothing more". Stronger advocates were few and far between, but on the other hand, many were happy with the *status quo*, even if they had problems. BT felt it could do more, by, for example, giving more customers Call Protect. Overall there was a very high claimed loyalty i.e. customers who did not intend to leave BT even if they gave low scores.

1064. The overall conclusion was this:

**Solus – Landline-only – customers give high scores, and are not looking to go anywhere, but we could still do more to demonstrate that we value this base**

WHAT?	WHY?	WHAT NEXT?
Landline-only base fall into a certain demographic	<ul style="list-style-type: none"> <li>The solus base are old, retired and on lower incomes</li> <li>They appear to be a naturally loyal base – to BT and their landline – with very little interest in switching to another product or provider</li> <li>There is some interest in Broadband, but low levels of ownership of relevant devices</li> </ul>	<ul style="list-style-type: none"> <li>Bear in mind that this base are essentially fine as they are, but seek to pick off relevant upsell opportunities</li> </ul>
Customers are generally positive – albeit passively – about their BT landline	<ul style="list-style-type: none"> <li>They give high scores for NPS and are broadly satisfied with most aspects of their experience. NB – some of this comes from methodology and base (telephone interviews with older customers)</li> <li>However, verbatim comments are relatively passive, rather than effusive (“no complaints”, Likelihood to recommend 9)</li> </ul>	<ul style="list-style-type: none"> <li>Continue to deliver a service that works for this cohort</li> </ul>
But they could feel more ‘looked after’	<ul style="list-style-type: none"> <li>Customers give higher scores for the more functional aspects of their experience, e.g. Line reliability, Call quality</li> <li>Where they’re relatively less positive is around Price and Value, but also Personal, Recognition and treating existing customers well</li> <li>Verbatims suggest BT could do more about nuisance calls</li> </ul>	<ul style="list-style-type: none"> <li>Consider what can be done to make this base feel more ‘loved’ without migrating them onto dual</li> <li>Call Protect could cut through</li> </ul>

1065. The CR says that this document is adverse to BT’s case on brand value, because of the overall “OK” sentiment referred to above. We think that this understates the significance of the document. After all, the CR places great weight on low NPS in relation to a number of other documents, yet here the NPS was very high.

1066. That said, we need to bear in mind, especially on value, that these customers were now in receipt of reduced line rental prices and also, as the document points out, there may be a bias towards giving high scores so as to please the live interviewer. Further, this particular group of VOCs were, by definition, no longer members of the Class. And of course, it says nothing about the SPCs.

1067. Nonetheless, the impression we gain from this document is that there was a significant element of satisfaction and brand loyalty at least for this particular group of VOCs.

Consumer Brand NPS Report, May 2019 (“the May 2019 Brand NPS report”)

1068. Page 3 shows that the “Single Landline” score had fallen to -27.

Consumer Brand NPS Report, November 2019 (“the November 2019 Brand NPS report”)

1069. Page 5 shows that the “Single Landline” score had fallen to -31. Page 8 noted that this score was much lower than that from other cohorts i.e. other groups of customers.

Conclusions on the NPS documents

1070. We would conclude from the above that on the face of the documents and when it comes to the SPC group of Class Members there was a very low propensity to recommend BT. On the other hand, the NPS documents were not measuring brand value as such. Further, the position was that at least for those VOCs surveyed for the purposes of the March 2019 Survey, there was positive brand loyalty.

In addition, we should add that these are not documents which span the entire claim period. There is one from September 2017, the March 2019 Consumer Brand Report, which covered March 2018-March 2019, the (positive) March 2019 Survey and the May and November 2019 reports.

1071. We must also bear in mind that other points more favourable to BT may well have been made by Ms Blight and Mr Bunt, had they been given an opportunity to deal with them in cross-examination.
1072. On any view, however, it is difficult to see how Dr Hunt could properly have made the statements about improved NPS in paragraphs 430 and 431 of SH1, quoted at paragraph 1043 above, because the documents we have just reviewed do not support such statements. In re-examination, he said that the views he expressed in Section 7 of his report, on the one hand, and the material contained in the NPS documents were “two different stories so I think there are things that are broadly consistent across the two.... two very different stories about two very different customer bases and very different products and these kinds of things, just to be clear.” It is hard to square that with the evidence.
1073. We now turn to the other materials placed before us.

#### *Ofcom Materials*

##### Introduction

1074. Dr Hunt uses various Ofcom materials and surveys to support his conclusion that Class Members, especially VOCs, were very satisfied with their SFV Services, valued the reliability of their landlines more than dual-play customers, and that the former saw BT as a market leader in reliability and generally. They placed greater emphasis on trustworthiness of their product and perceived BT to be the most trustworthy. See paragraphs 383 and 457 of SH1. This, he said, was reflective of consumers placing positive value on BT’s brand.

##### 2016 Switching Tracker Data

1075. This is data taken by Ofcom from all telecoms customers, not just those of BT. However, it produced discrete results for BT customers, among others. This showed that 73% of BT VOCs were very satisfied and a further 23% were fairly satisfied overall with their service provider. The respective figures for SPCs were 61% and 32% for SPCs (excluding certain services) and 53% and 37% for dual play. In relation to satisfaction with landline VFM, it was 52% and 30% for VOCs, 47% and 34% for SPCs and 28% and 56% for dual play.

##### Comparison Documents

1076. Dr Hunt then refers to Ofcom’s 2016 and 2017 “Comparing Service Quality Reports” and its 2023 “Comparing Customer Service Interactive Report”. These looked at all landline customers and this was, of course, before the Commitments came into effect.

1077. For the period 2016-2022, the proportion of BT customers who said they were “fairly” or “very” satisfied was generally above average each year. BT came first or second for each of these years and on average was the second-best provider. At page 75 of SH1, Mr Hunt produced the following table, drawn from the 2016 and 2023 reports:

**Table 7: Overall satisfaction with landline service**

	Average	BT	EE	Plusnet	Sky	TalkTalk	Virgin Media
<b>2016</b>	89%	92%	[*]	[*]	90%	83%	85%
<b>2017</b>	87%	88%	90%	81%	90%	82%	84%
<b>2018</b>	86%	88%	90%	89%	86%	81%	83%
<b>2019</b>	85%	90%	82%	83%	88%	83%	77%
<b>2020</b>	77%	78%	81%	78%	79%	82%	69%
<b>2021</b>	77%	81%	80%	83%	79%	75%	69%

<b>2022</b>	77%	78%	90%	78%	77%	73%	70%
-------------	-----	-----	-----	-----	-----	-----	-----

<b>Average</b>	84%	85%	86%	82%	84%	80%	77%
----------------	-----	-----	-----	-----	-----	-----	-----

	Highest score
	Second highest score

1078. In addition, the 2023 report stated as follows in relation to customers perception of the clarity of their telephone line:

**Table 10: Satisfaction with clarity of the line**

	Average	BT	EE	Plusnet	Sky	TalkTalk	Virgin Media
<b>2017</b>	89%	90%	92%	[1]	90%	89%	88%
<b>2018</b>	89%	91%	91%	86%	88%	87%	90%
<b>2019</b>	87%	91%	85%	85%	87%	88%	82%
<b>2020</b>	80%	82%	77%	75%	79%	82%	78%
<b>2021</b>	80%	83%	80%	73%	81%	80%	77%
<b>2022</b>	80%	81%	88%	75%	77%	79%	80%

<b>Average</b>	84%	86%	86%	79%	84%	84%	83%
----------------	-----	-----	-----	-----	-----	-----	-----

	Highest score
	Second highest score



1079. The same report also yielded the figures shown below in Dr Hunt's Table 11:

**Table 11: Satisfaction with landline service reliability**

	<b>Average</b>	BT	EE	Plusnet	Sky	TalkTalk	Virgin Media
<b>2016</b>	<b>91%</b>	93%	[1]	[1]	91%	88%	91%
<b>2017</b>	<b>90%</b>	91%	92%	87%	90%	87%	91%
<b>2018</b>	<b>90%</b>	92%	93%	90%	89%	85%	89%
<b>2019</b>	<b>89%</b>	93%	83%	83%	89%	86%	85%
<b>2020</b>	<b>82%</b>	84%	85%	82%	83%	86%	77%
<b>2021</b>	<b>84%</b>	89%	87%	87%	86%	83%	76%
<b>2022</b>	<b>84%</b>	86%	91%	84%	82%	82%	81%
<b>Average</b>	<b>87%</b>	90%	89%	86%	87%	85%	84%

	Highest score
	Second highest score

1080. We should add that EE had been owned by BT since January 2016.

#### 2016 – 2022 Switching Tracker Data

1081. In addition, Dr Hunt looked at the cumulative results of Ofcom's Switching Tracker data from 2013-2016. This showed that for this period, between 78% and 82% of SFV customers were totally satisfied while between 9% and 12% were totally dissatisfied.

#### Analysis

1082. On those figures, there can be little doubt that there were high or relatively high levels of satisfaction with BT's landline services, especially by VOCs. This would reflect the results of the March 2019 Survey at least as far as its NPS were concerned. Moreover, the introduction of the Commitments does not appear to have made any real impact on the figures.

1083. As to all of that, the CR makes the point that this does not show that BT was providing services of distinctive value. For example, while Table 7 shows an average score for BT of 85%, this is only 1 percentage point above the average. The same could be said for Tables 10 and 11 where the performance for BT as an average was 86% as against 84% for the general average and 90% as against 87% respectively. It also pointed to the fact that in one year, BT came third and in another, it came fourth out (Mr Parker's summary of the results in paragraph 6.95 of DP4 do not appear to be wholly accurate).

1084. We should add that the 2016 Switching Tracker data was showing high percentages of satisfaction overall especially with VOCs. Here, however, it was not shown what the satisfaction levels for other providers were; it would be a reasonable assumption to suppose that they were of the order shown

in Tables 7, 10 and 11, in which case the point made by the CR noted in the preceding paragraph would apply here as well.

1085. As to the CR's point here, while the extent to which BT exceeded the average was not large in percentage terms, if one compares BT's performance directly with those companies which it did not own, i.e. Sky, TalkTalk and Virgin Media the percentages differences are generally larger. Also, if all satisfaction levels are very high there is not much headroom to show superior performance. Overall, we do not see why these tables do not provide evidence of the ascription of positive value to the BT brand.
1086. Mr Parker then made some more general criticisms of Dr Hunt's approach here. First, he said that overall satisfaction levels are not of any particular weight in the context of assessing economic value. That is because if it were otherwise, it would suggest that in a case where pricing was excessive under Limb 1, it would not be unfair for the purposes of Limb 2, simply because customers were satisfied. That said, in cross-examination he accepted that one could still have satisfaction as a relevant metric of assessing economic value without it meaning that satisfaction measures simply exclude the possibility of excessive pricing.
1087. Second, and particularly in relation to VOCs, they may respond positively despite having experienced frustrations with the service, as the March 2019 Survey suggests.
1088. On the question of satisfaction levels where they were high, Professor Loomes sought to diminish their significance by saying that if a customer had been with BT for 10 or 15 years, they were unlikely to say that they were dissatisfied because of "cognitive dissonance" i.e. their desire not to express a view which would appear to be contrary to the fact that they had stayed with BT for so long. We do not think there is anything in this, certainly not so as to render insignificant the figures on customer satisfaction.
1089. As to those points, BT accepts that by themselves, satisfaction levels do not somehow prove economic value without more (see paragraph 729 of its Closing). However, when taken together with other evidence they can (and do here) show economic value. We agree.
1090. Next, BT rejected Mr Parker's high threshold test for economic value such that there would have to be "massively higher" levels of satisfaction (in comparison to other products) and linked to some objective better performance before they could count. As already noted, we agree that this is too high a test for economic value.
1091. Dr Hunt said that satisfaction was quite a useful metric in relation to how customers feel about a particular product and it had been used in competition work. Mr Parker accepted that it came up

sometimes in competition investigations but said that he did not think much weight was placed on it.

1092. In fact, evidence of satisfaction levels was not simply rejected in the competition context as a metric when considering whether a particular market was working well. It could be of use, as Ofcom made clear in its 2013 Narrowband Markets Review, when it referred to customer satisfaction and switching as factors going to showing that the market remained competitive.

1093. Mr Parker relied specifically on the CMA's 2016 Retail banking market investigation final report which said this:

"5.100 Several parties submitted that the high levels of satisfaction suggested that the market was working well. However, we consider that customer experience metrics such as satisfaction will be determined at least in part by customers' expectations of product or service quality. Since this expectation is likely to be influenced by the range of service offered by current providers, high absolute levels of satisfaction cannot necessarily be interpreted as implying that the market is delivering good outcomes for customers. For this reason our analysis of customer experience measures is largely focused on the comparative performance between banks."

1094. However, as was pointed out in cross-examination, the CMA also said this in an earlier paragraph:

"Indicators of overall quality  
5.88 Customer experience metrics, such as customer satisfaction and advocacy ratings, can be useful as indicators of the overall quality of service received by customers, and are widely used as a measure of overall service quality, by both private companies and regulators."

1095. What we derive from the above is that it would be wrong to dismiss satisfaction levels as simply being irrelevant to an assessment of economic value; however, the weight to be placed upon them does depend on the other available evidence and is highly fact-sensitive.

1096. In this particular case, we consider that the weight to be given to the satisfaction levels reported by BT Customers must be ascertained in the context of two particular matters, namely the results shown by the NPS documents considered above, and the significance of switching (or not switching).

1097. So far as the NPS documents are concerned, while we give them some weight (while bearing in mind that they were not put to Mr Bunt or Ms Blight), they do not all point in the same direction and we consider that overall the Ofcom materials present a better guide to satisfaction.

1098. As to the significance of switching or not, we now consider this latter topic before expressing our overall conclusions on brand value.

#### **Provision of Economic Value: (d) Ability of Customers to switch**

1099. We consider first the evidence of Dr Hunt, since it is BT which makes a positive connection between the ability to switch (or not) and the ascribing of value to the landline product or BT's brand by reference to those who did not.

1100. His key point is summarised in section 6.3.3 of SH1 as follows:

**"6.3.3 Non-switching as a deliberate act**

336. I now turn to consider the extent to which Class Members who did not switch made a deliberate act. I do this by examining various sources of evidence including a range of evidence which I set out under Section 7 and which sets out the specific preferences of Class Members as well as the extent to which they derive value from their SFV Service.

337. As I explained in Section 5.5, analysis of switching rates alone ignores people who thought about switching but made a deliberate choice to stay put. Professor Loomes does not consider this. But the fact that so few Class Members consider switching to be difficult and the extensive outreach from BT and its competitors suggests that Professor Loomes should not interpret customers who do not switch as disengaged consumers.

338. Furthermore, his analysis is inconsistent with Ofcom, who has previously defined ‘engaged’ consumers both as people who actually switched as well as those considering and shopping around. For example, evidence from Ofcom shows that in 2016, 2% of BT

SFV customers were ‘actively looking to switch’ or had started looking, and a further 2% ‘considered switching but did not look’.

339. This means that in addition to those who did actually switch, a further 4% of Class Members were considering switching. Professor Loomes considered neither of these categories, which Ofcom and I consider to be relevant evidence regarding consumer intention and speaks to a portion of people who are assessing their options and on that basis can make a choice about whether to switch or not.

340. In addition, Professor Loomes ignores that consumers may not switch because they consider their current product offering best meets their needs, and on that basis are highly satisfied. For these consumers, staying put could simply represent reasonable decision-making rather than a lack of engagement.”

1101. All of this is developed in Section 7 of SH1. The key question is the extent to which it can be said that those who (at any time in the claim) did not switch thereby made a positive or deliberate choice to stay, and in that sense were sufficiently engaged, as opposed to being simply inert and disengaged so that no inference of any attribution of value could be made from them staying. We should add, of course, that merely because customers were engaged, it does not necessarily establish the relevant level of economic value, but it does at least enable an inference to be made that they were capable of making a positive choice to stay because of the value ascribed for example to the BT brand - if this is what they did.
1102. The CR’s position is that little or nothing can be inferred as to a positive choice to stay because the customers were indeed generally disengaged. It is important to note that this is not because the Class Members as a whole are considered to have some particular vulnerabilities or characteristics as a class. Professor Loomes specifically eschewed this approach. Rather it was because of what can be said from a behavioural economics point of view about how consumers act (or not) generally. Dr Hunt, for his part, noted that VOCs were generally in an older demographic (see paragraph 379 of SH1) for the purposes of his analysis of their engagement, and of course BT made reference to their age demographic in the March 2019 Survey.
1103. It is necessary therefore to consider what the level of engagement was, on the part of those who (at some point) remained as VOCs or SPCs.
1104. First, it seems to us that we can infer a level of engagement in those Class Members who later switched at some point. The fact of switching suggests that they were not inert and were sufficiently engaged to explore other options which included (in the case of about 50%) switching to other

providers. And in the case of the (former) SPCs, of course, they obviously had access to the internet and used it, otherwise they would not have had a broadband service. Moreover, on our findings, their reason for switching is not likely to have been price driven. We add that it was probably not quality driven either. Rather it was part of the secular trend. But this does not affect the question of engagement or otherwise. This reinforces the point that the SFV customers were not captive; there were no barriers to them taking alternative options.

1105. Of course, it is perfectly true that there remained, across all or much of the claim period a “rump” of those who never switched and who will be predominantly VOCs. However, they by no means constitute the majority of Class Members or anything like it, especially as they were not part of the Class at all after April 2018.
1106. Professor Loomes suggested that nonetheless, those who did not switch were a “different kind of person” from those who did. We do not accept that - it seems to us to be speculation on his part. The more realistic analysis is that certainly for most Class Members, there was an ongoing dynamic process by which they would switch at some point sooner or later.
1107. Next, there were of course those who remained BT SFV customers but who switched internally within BT by taking up call plans, for example rather than paying charges per call. BT was encouraging customers to do this. Professor Loomes said that such customers could not be called “switchers” otherwise there would be a huge number of such switches. We agree, but the point is that considering and moving to call plans because they were cheaper and more convenient is surely a sign of engagement.
1108. Another factor is that a significant number of Class Members are constituted by those who joined BT as VOCs or SPCs, having been with other providers. They constituted at least 10% of the total SFV customers each year between 2014 and 2019. See paragraphs 169-171 above. It may be that many of them later switched again. Nonetheless, it is some evidence of the existence of a positive choice in favour of BT and the existence of engagement.
1109. We next turn to the question of “triggers”. These are various forms of stimuli to customers which can then prompt them to become engaged about their BT service. We accept that Class Members received communications from BT either by email or by post. These would include price change notifications (“PCNs”) which BT was obliged to send to their customers, announcements of price increases in the press, bills and (where the customer had consented) marketing communications including promotional offers.

1110. The question then is the extent to which BT customers were engaged with, in the sense of reacting to or at least considering, the communications which they received.
1111. In relation to PCNs, it appears to be common ground that typically, the first page of a PCN letter (whether posted or emailed) tended to refer to the fact of a price change and also the non-price changes, with the detail of the actual price change appearing on the second page.
1112. An example of this is a letter dated January 2020 stating on the first page that prices would go up by CPI plus 1.3% from 31 March and making references to a new calling plan introduced, together with Call Protect. Page 2 then set out the detail of the price changes in a tariff.
1113. However, at least in some cases, page 2 could only be accessed on the BT website. Thus, a letter dated March 2021 which supplemented an earlier letter dealing with price changes said that line rental would increase by CPI +3.9% but did not identify the level of CPI or state what the new price would be. It also said that the cost of calls on “pay-as-you-go” plans would increase by that percentage from 20p to 20.9p. The letter then said this:
- “For details of all prices that are increasing visit [BT.com/tariff](https://www.bt.com/tariff) guide and head to page 2.”
1114. It is not clear if letters in that form were sent before 2021.
1115. It is worth adding at this point that Mr Bunt said in evidence that BT (and other telecoms operators) would have to have its PCNs approved by Ofcom. He said that as far as he was aware, BT’s always were, without changes being required whereas those of BT’s competitors had often to be rewritten.
1116. In addition, and as a result of the Commitments, BT was obliged to send annual statements to SPCs, to show their annual spend and potential cost savings as well as information on switching to a different provider. Also, since February 2020, BT had to send annual “best tariff” notices to all Class Members now out of contract as well as an “end of contract” notification. Finally, unless opted out, there would be marketing communications.
1117. It is likely that Class Members would also have received offers from other providers.
1118. There would have been other sources of information available to Class Members about their landlines. Thus the Ofcom 2015 Consumer Experience Report said that 19% of landline customers received information from family and 14% received information from friends about alternative tariffs.
1119. There then arises the question of the extent to which BT customers would actually read the communications sent to them.
1120. It seems reasonably clear that BT customers would at least be aware in general of price rises. In this regard Dr Hunt relied on a number of reports or studies.

1121. First there was a report produced for BT by a consultancy called Firefish in 2014. This suggested that older VOCs had a general awareness of their landline package including costs and call features. It also suggested that these customers were usually aware of what they were currently paying.
1122. He also relied upon Ofcom's 2015 Consumer Experience Research Report to the effect that the internet was the most trusted source of information. Further, Dr Hunt relied upon various FCA papers produced while he was at the FCA, which in particular found that older people tended to be more responsive to communications about their service because they actually have more time. In one case, 60% of those surveyed recalled a particular letter even two or three months after receiving it.
1123. A further point made was that for those customers still paying their bills at the Post Office they would obviously be aware of the current prices for their landlines. The same is likely to be true for those not paying by direct debit.
1124. On the other hand, in GL1, Professor Loomes relied, first on a qualitative study to support Ofcom's 2017 Provisional Conclusions. One of its aims was to understand the attitude of SFV customers to switching, and to explore what would encourage them to engage with the market and consider switching. The study was called "Enriching understanding of Stand-alone Voice Customers". The survey included VOCs and SPCs. It considered the impact of four different kinds of letter, all designed to encourage greater engagement. Professor Loomes accepted that the results had to be treated with some care because of the subjectivity of the responses to a qualitative survey, and also because there could be a bias in favour of greater engagement because the survey members had all agreed to be part of the survey.
1125. From this survey, Professor Loomes concluded that the VOCs were heavily dependent on their landline and were broadly content with their current provider and many had been with BT since before privatisation. They had little awareness of other providers and the products and did not know whether their own deal was good value for money. They were more likely to read correspondence from their own provider than from others. There were some barriers to switching including customer loyalty sticking to what they knew and believing that because BT owned the lines, they were more likely to offer the best service. So there was little incentive to switch. There was a lack of knowledge about the internet which made it harder to obtain information necessary for a switching decision. They tended to rely more upon family and friends for information. They also had insufficient information about the consequences of switching. Thus, Professor Loomes suggested that this was evidence that those customers who remained with BT were more likely to have done so as a consequence of not engaging with any exploration of switching rather than this being a conscious and informed choice.

1126. As for the SPCs, Professor Loomes said that there were various elements within the group with different levels of engagement, only one of which consisted of customers who had made a conscious decision to split their purchase. That at least suggested that the notion that all SPCs made active choices required substantiation.
1127. In answer to this, Dr Hunt suggested that this was nonetheless consistent with those customers being broadly content with the service they received and not therefore wishing to change. On the basis that there was some significant brand loyalty on the part of VOCs in particular, we can understand this. This would be consistent with the additional value placed on landlines by SFV customers, as noted in paragraph 964 above.
1128. A second study was commissioned jointly by Ofcom and BT in the course of the negotiations for the Commitments in 2016-17. This was called “Telecoms Sector: Engagement Trial for BT’s Standalone Voice Customers”. It concerned only VOCs and involved a set of field experiments to explore the effectiveness of different communication methods for promoting greater engagement. Here, engagement was taken to be the customer changing their calling package, adding a product to their plan or closing their account within three months of receiving a particular letter. Baseline levels of engagement in the control groups ranged between 7.5% and 9.9% with only a minority of these cases of engagement involving switching as opposed to some other course of action. The two letters which promoted the most engagement were the ones which dealt with landlines and specifically mentioned HPS with the price being fixed for three years, and an average spend letter which was a personalised statement breaking down the total charges that the customer had paid into recurring charges and extra charges. Overall then, for 9 out of 10 VOCs in the trial, there was no further engagement at all.
1129. Here, Dr Hunt made the point that while the various letters did not prompt a change in consumer behaviour, it does not mean that the customers did not read the letters. The lack of engagement (in the limited sense defined by the study) did not really say anything, since it would be consistent with the customers being broadly happy with the existing service and not wanting to undertake any of the three types of action specified. As a counter to this, Professor Loomes suggested that given the letters, one would have expected to see a significant reaction but that did not happen.
1130. In our view, and on the basis of the above materials, there would appear to be sufficient forms of information communicated to and available to the Class Members. In particular, the VOCs, even without access to the internet, were likely to read the letters sent to them. Professor Loomes suggested that there might have been too many communications, so that Class Members suffered from “information overload” and simply ignored them. However, we think that this is just further speculation.



1131. The next question is why there was not more switching to another landline provider or to a bundle. For those SPCs who did not switch, the position appears especially odd, given the price benefits available to them of moving to a bundle. That said, the position of SPCs, according to Mr Bunt, was more nuanced, and he referred to them as a “mixed bag”. Some of the SPCs decided to stay with BT, because they could get free broadband when taking Sky, while retaining their landline, and that was a positive decision so far as the landline is concerned. See Day 5/101-102. We see the force of that.
1132. Here, the experts both suggested various theories. Dr Hunt suggested that customers may have deliberately chosen not to read or act upon a communication as an act of “rational inattention”. Or perhaps to put it another way, they could not be bothered, by reason of time or other constraints. If this is what happened, we can see some force in his point. Another possibility suggested by Professor Loomes is that such customers were simply inert and gave the communications no thought at all, even if they read them. They were simply stuck in their ways and stayed with BT as a result. However, as we see it, this would not be inconsistent with such customers ascribing value to BT on the basis that they simply preferred to stay with the supplier they had known for a long time. We accept that there is a degree of speculation on the part of both experts here, but we are prepared to give some weight to what they say, with the upshot being a degree of value being ascribed to BT, however one wants to describe it. This favours BT rather than CR in this respect.
1133. At this point we should deal with HPS. Those customers who took HPS are, of course, excluded from this claim. Nonetheless, the point is made that if customers were fully engaged, surely more of them would have taken this product. The difficulty with that argument is that HPS as a product was, in our view, a retention deal and not fully promoted. See paragraphs 270-301 above.
1134. Overall, and in the light of the matters referred to above, we consider that it seems likely that a substantial number of those who stayed (while they stayed) probably did so out of a sense of loyalty to a brand to which they had been attached for probably many years. They were not generally inert, as is shown by the fact that most of them (eventually) did switch, and all the indications suggest that those who remained SPCs are continuing to switch to bundles, as there were 1.87m such customers in 2014 and only 0.49m by 2022.

#### *Conclusions on Brand Value*

1135. Overall we consider that there is significant evidence that the SFV customers as a whole did engage with their SFV products. We cannot possibly identify the individual motivation of each and every customer, and the evidence and interpretations offered by the experts, unsurprisingly, did not yield a definitive picture. However, for those who remained BT SFV customers (or while they remained),

we consider there is sufficient evidence that for at least a substantial number, their decision to do so implies a degree of positive value that they attached to the BT brand.

### **Provision of Economic Value: (e) Conclusions**

1136. Having taken into account all the matters referred to above, and recognising that they do not always point in the same direction, our overall conclusion is that the (relevant) Gives and value ascribed to the BT brand did constitute distinctive value. In the context where the excessive prices were at the level we found them to be (see paragraphs 932-934 above), we conclude that they did bear a reasonable relation to the economic value of the SFV Services.

### **Workable Competition Factors**

#### *Introduction*

1137. As has already been noted, the overarching test for abuse, in broad terms, is whether the dominant undertaking has reaped trading benefits which it could not have obtained in conditions of “normal and sufficiently effective” competition i.e. “workable” competition. Where the price bears no reasonable relation to the economic value of the product or service in question this is an example of such an unfair price. See paragraph 97 of *Phenytoin* cited at paragraph 49 above. Both sides noted this, also. See paragraph 488 of the CR’s Closing and paragraph 673 of BT’s Closing.

1138. It follows that it is relevant to consider what the position might be in the putative workably competitive market. This is a different and broader question than that asked under Limb 1, which is whether the price charged is excessive by reference to the notional competitive benchmark, itself set by reference to all direct and indirect costs plus the reasonable margin.

1139. There was, however, some divergence as to how this workable standard should be applied, with the most important difference between the parties being their view as to whether firms could earn profits in excess of the competitive level in conditions of workable competition. Specifically, Ms Kreisberger KC for the CR claimed that workable competition involved the market price being driven down to a level of zero excess profit. In her oral closing she submitted that in a workably competitive market, the price will be driven down to cost-plus, so zero economic profits, but if the firm could point to some unique feature that distinguishes it from the market, then it may be able to put its prices above cost-plus.

1140. BT did not agree, arguing that workable competition was consistent with a wide range of prices and price-cost margins, and that it certainly did not entail a zero profit constraint, which was a standard associated only with perfect competition. As the Tribunal stated at paragraph 129 of its judgment in *Liothyronine*:

“Normal, sufficiently effective and workable competition, as well as being distinct from abnormal, insufficiently effective competition, is also distinct from perfect, maximally competitive or idealised

competition. As the Tribunal noted in Phenytoin, normal, effective competition is the “most that should be expected in the real world” as distinct from “idealised or near perfect competition which is a theoretical concept.” ”

1141. We consider that BT’s approach is the correct one and that the zero profit presumption advocated by the CR is unrealistic. Of course, this does not justify an ‘anything goes’ approach to the definition of workable competition and we bear that in mind.
1142. For the purposes of the unfairness analysis in this case, we consider that there are two relevant considerations:
- (1) Price dispersion; and
  - (2) Cost efficiencies dispersion.

### *Price Dispersion*

#### Introduction

1143. BT’s primary position on the question of price dispersion was that it relates to the setting of the competitive benchmark under Limb 1. See paragraph 618 of its Closing. However, its alternative position was that it should be considered under Limb 2. Thus, in Mr Beard KC’s oral closing at he said this:

“The recognition of subjective economic value through Limb 2 can be taken into account by ensuring you use benchmarks that allow for the variety of outcomes you see in workable competition...the way that you can sensibly bring to bear the economic value subjective considerations in limb 2 is essentially to think about the benchmarks being higher for costs and margin, because in doing that what you are implicitly doing is affording the market that spread of prices...in order for the Class Representative to say that the price is unfair, they have to be saying, effectively, that in the conditions of workable competition, consumers would not have the sort of subjective preferences that can create the price dispersion which would be represented by their subjective appraisal of economic value, at the very least in relation to Limb 2.”

1144. For our part, we would not seek to “shoehorn” such arguments into the concept of economic value. We see them as more free-standing points raised within the broad ambit of workable competition. However on the substance of what Mr Beard KC was saying here, we agree that Limb 2 is the more appropriate forum for such considerations and we rejected an approach which brought them into Limb 1, consistent with our desire to take a “cleaner” and more “objective” basis for the assessment of whether the price is excessive under Limb 1. We said as much in paragraph 53 above when dealing with economic value, but we think that this reasoning applies as much to matters like price dispersion.

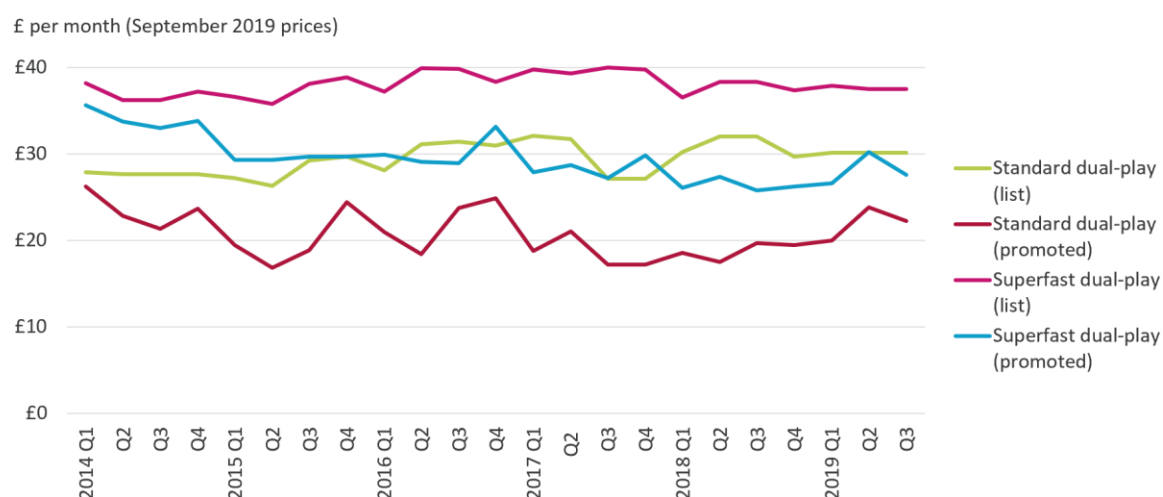
#### Relevant Facts

1145. To consider what price dispersion there might be in the putative workably competitive market for SFV Services, we consider it instructive to look at variations in pricing in the adjacent market for bundles, which is accepted by both parties to be workably competitive. We have already adverted to this in the context of considering Mr Parker’s price differential analysis as between SPC pricing and bundle pricing, noting that some customers for bundles were paying list (or “back book” prices)

while others were paying cheaper promotional (or “front book”) prices. See paragraphs 365 and 366 above.

1146. The figures quoted there were drawn from Ofcom’s Pricing Trends report of 9 January 2020. Its Figure 16 showed as follows:

**Figure 16: Average available monthly list and promoted prices for dual-play standard and superfast broadband**



Source: Ofcom / Pure Pricing UK Broadband Updates.

Notes: Represents average of the cheapest available tariff from BT, Plusnet, Virgin Media, TalkTalk, Sky and EE at the end of each quarter; promotions include the promoted price and any ‘gifts’ offered; adjusted for CPI (September 2019); standard broadband products are those with an advertised speed <30Mbit/s; superfast broadband products are those with an advertised speed ≥30Mbit/s.

1147. Ofcom noted that the differential between list and promotional prices had increased between 2014 and 2018 although it then narrowed in the year ending March 2019. At that point, the differential in relation to dual play bundles was £8 per month rather than £12 per month the previous year, while the differential in relation to superfast dual play bundles was around £10 compared with £13 previously.
1148. Looking at Figure 16 as a whole, one could take an example of a list price for standard dual play at £30 with the promotional price at £20. The latter is one third less than the former. So this is quite a significant price differential across an average of all the relevant suppliers. There could therefore be a greater (or lesser) dispersion when comparing any one supplier with another.
1149. Further, if one assumes from the above that the average dual play bundle price was £25, i.e. the mid-point between the promoted and list price, and where the typical BT gross margin on its bundles is said to be 38% (see paragraph 139 above), this would then suggest that BT’s gross margin on the list price was 48% and it was 22.5% on the promotional price. Again, this is a very significant

variation in the gross profit contributions made on different transactions in the same workably competitive market.

1150. Price and gross profit variations of this magnitude for what appear to be essentially identical products would not be consistent with notions of a perfectly competitive market, where the “law of one price” would hold. The fact that such variations are the focus of Ofcom’s published analysis of the market might reasonably imply that there is some legitimate scope for public and regulatory policy intervention to encourage measures (such as encourage greater consumer engagement and/or information) to bring about a reduction in such dispersion. However, the fact that we do observe this degree of dispersion, in a market that is the close neighbour of the SFV market, and in which workable competition is accepted to be present, does helpfully illustrate the kind of divergence from the law of one price that we might regard as normal, if imperfect, competition within a workable competition framework.
1151. BT did not put forward any particular figure or calculation taken from this which could be applied directly to BT’s SLR pricing. However it did submit that this feature of the putative competitive market should be factored into the assessment of unfairness and we agree. We therefore take it into account, and consider that this first element of dispersion counts against a finding of unfairness under Limb 2. We should add that we do not consider that this factor has already been taken into account when we dealt with the issue of the appropriate common costs recovery for BT under Limb 1. That was a separate exercise undertaken in relation to determining the “costs plus” figure. So there is no double-counting.

#### *Cost Efficiencies Dispersion*

1152. The premise for this point is that in many workably competitive markets there will be a range of cost levels among rival firms and if the equilibrium market price needs to cover the costs of the marginal source of supply, this will often mean that at the workably competitive price level, lower cost sources of supply (and lower cost suppliers) will earn returns in excess of that minimum level. One instance where this phenomenon can apply is in markets where there are significant economies of scale due to the existence of some fixed costs. In such markets, the more suppliers there are, the higher will be the price that is required to remunerate the costs of the firms that compete within it. This can give rise to a trade-off between the advantages that more suppliers can create for more rivalry and competition in a market, and a disadvantage associated with more suppliers increasing total industry cost. For the detail of this basic proposition (which we did not understand to be in dispute) see paragraph 139B of Mr Matthew’s DM1 and Figure 1 beneath it.

1153. To the extent that this point was used by BT to justify a higher level of profitability before its prices would be considered excessive, we rejected that argument in the context of Limb 1 at paragraph 782 above.
1154. However, and as with price dispersion, we can see that the differential in costs efficiencies resonates under Limb 2 instead. Again, this is because of the overarching workable competition test. In other words, even in the case of putative workable competition in the SFV Services market, there can be variations, perhaps significant variations, in the profitability of essentially the same service, sold by different suppliers. It would then be unreasonable and unfair to penalise BT, simply because of its lower cost base. This is the scenario that was explicitly recognised in the Tribunal’s *Hydrocortisone* judgment, in which its “Case 1” was described as a situation where, while prices may be relatively similar, one producer may enjoy a higher surplus because it is more efficient.
1155. The CR’s response to this (made in the context of Limb 1 but it would apply equally to Limb 2, if correct) is that BT enjoys its cost advantages simply because of its position as the legacy provider of telephone services from the time when it had a statutory monopoly over their supply. It is not as if it has achieved its market power through innovation or extraordinary levels of investment which took many years to recoup. Accordingly there was nothing unfair about disregarding the fact that BT had lower unit costs than its competitors.
1156. We do not agree with the CR here and consider that its response is over-simplistic. After all, BT was privatised some 40 years ago, in 1984. It then went through a long period of regulation where it was only free of control in 2006 and then the other restraints, including being unable to sell bundles, in 2009. It remained under positive regulatory scrutiny ever since, culminating, of course, in the Commitments. In other words, the environment was not one of “regulatory failure”. Moreover this is in a context where such barriers to expansion as do exist are due principally to a degree of brand loyalty on the part of those of BT’s customers in a declining market, who have not yet switched into the principal market where BT and its competitors now operate i.e. bundles (paragraphs 462- 467 above). In other words, this is not a case where BT, as a dominant undertaking has simply sat back on its corporate hands, as it were, and simply collected excess profits. This view of BT is mirrored by what we have said about the value of the Givès, brand value and the lack of any material exploitative intent on its part (see paragraphs 1159-1172 below).
1157. Accordingly, we consider that this second element of dispersion also counts against a finding of unfairness under Limb 2.
1158. We should add that we have considered whether this second dispersion point falls foul of the approach taken by the Tribunal in *Liothyronine*, as discussed in paragraphs 597 - 599 above. In our view it clearly does not. The point here is based on a simple observation about the discrepancy in

profitability rates between the competitors in the putative workably competitive market. It is not about “setting” a price in order to incentivise entry into or expansion by competitors in the market.

### **Existence or otherwise of exploitation by BT over its price insensitive customers (“the Exploitation Point”)**

#### *Introduction*

1159. Here we address the CR’s argument that BT did indeed exploit its market power in this way. If there was such exploitation, the CR contends that it effectively corroborates its claim that the excessive prices charged were not justified by economic value but can only be explained by the exercise of BT’s market power over this class of customers.

#### *Price insensitivity of SFV customers*

1160. We have already concluded in the Market Definition section above at paragraphs 216-303 that the primary reason for switching was not price-related, and that BT was aware of that fact.

#### *BT sought to maximise value from a declining market and regular price increases*

1161. It is common ground that there was a declining market for SFV Services. The switching data referred to at paragraphs 163-177 above shows this. It is not suggested that BT was not aware of it. BT sought to maximise value from that declining market and did so through regular line rental price increases that it judged to be beneficial for its SFV revenue. But as the flat ARPU figures show, there were other factors at play here and the ever-increasing gap between BT’s line rental prices and wholesale line costs did not generate successive increases in BT’s SFV profitability.

1162. The CR here relies on, first, a March 2012 Board Strategy document from Gavin Patterson, the then CEO of BT Retail entitled “Returning to Profitable Revenue Growth in UK Consumer and Business Markets”. At page 17, the document stated that:

“We will maximise value from our legacy fixed voice business and build new personal communications offers...

We are driving unlimited packages to defend ARPU and increase usage...

Overall the fixed voice market is in decline

We are managing revenue and margin via price rises and migration to unlimited plans

38% of our base are on Unlimited Anytime Plans, which drives increased usage”

1163. Mr Bunt accepted that this showed that one element of the strategy to maintain revenue in this declining market was to increase line rental prices. There were, of course, price increases between January 2013 and January 2016. In fact, this reflects the point already made in paragraphs 181-195 above that the immediate causes of the line rental increases were the revenue targets which the Voice Division had to meet. That said, as Mr Bunt also pointed out, another part of the strategy was to move customers on to UAC packages from the cheaper packages which they were presently on, but under which they had to pay per call. The thinking was that while the cost of the UAC package was more, the customer did not then need to be concerned about how many calls they made because they

were included in the price. This would lead to them making more calls and becoming more engaged with their landline product instead of, for example, switching over to just using a mobile phone.

1164. There is then the Price Change 18/19: Strategic Review document dated 14 July 2017. This noted that the base of customers from which BT could price change (i.e. increase prices) had decreased because there were likely to be limits on price increases for VOCs (which emerged in the Commitments), and some other pricing decisions were freezing out a large number of other customers. At page 9 it further stated:

“This means we have an even greater challenge to using price change to meet MTP—we need an intelligent approach to pricing what remains in our control...

We should recognise declining markets and price accordingly to maximise value (e.g. split purchase Solus).”

1165. In cross-examination, Mr Bunt agreed that the approach stated here was to maintain or maximise revenue through price increases, although he added that there was also the separate objective to move customers over to bundles anyway, which were regarded as more profitable in the long run, and we think that is a fair qualification. The objective stated in the document was realised in the sense that there were significant price increases for SPCs from September 2018 onwards, (though, as noted, these did not raise ARPU).
1166. BT points out that it was seeking to maximise revenue across the board i.e. across all of its customers; we see that but we do not think it detracts from the specific references in the two documents above to maximising value from the “declining market” which is SFV Services.
1167. That said, given we have been taken to just two documents, we do not place much weight on this factor.

#### *No price competition from competitors*

1168. We have already concluded that in respect of most competitors’ pricing, BT’s line rental price changes were typically followed by rival operators. See paragraph 480 above. However, that does not mean that BT could do what it liked on pricing. Indeed, Ms Blight was concerned that one day, its competitors might start to take advantage of the “headroom” created by BT’s pricing, and the risk of “churn” was one of the factors that deterred BT from increasing line rental prices more than it did. And certainly, although the proportion of all SFV customers who switched to the Post Office was relatively small, the internal documents show a real resolve to try and stem those customer losses to a competitor that had chosen to undercut BT on line rental prices.
1169. As an associated point, and for the reasons given in paragraphs 477 - 493, we do not think that this is a case where there is a significant price leadership factor pointing towards unfairness on the part of BT’s prices.



## *Conclusions*

1170. It is obvious from the above that when BT was increasing line rental prices, it felt that it was able to do so and it ultimately did so because there was an imperative to meet revenue targets. That is not to say that the question of any price rise and related matters like Gives were not carefully considered; see Annex 2 to BT's Closing, referred to at paragraphs 1016-1021 above, and in general, the detailed and numerous price change documents produced ahead of each proposed price change. Of course, there were not line rental price increases in every year of the claim, because line rental prices were frozen between April 2017 and September 2018. In addition, and more importantly, it is clear that the price increases, when other changes to call volumes and call package charges are factored in, did not succeed in increasing ARPU. However, we have already found that for each year of the claim period, the prices charged were excessive and so BT was able to use price increases to maintain that excess over the whole of the claim period. Further, BT seems to have been aware that SFV customers were highly profitable.
1171. We would accept that this perception by BT is some evidence of the fact that the excessive prices were brought about by the exercise of its own market power. We should also add that the fact that BT's price increases were driven wholly or mainly by the need to meet revenue targets cannot amount to a justification for the excess.
1172. However, looking at the documents and evidence referred to above, we do not think that this is a case where BT set out deliberately to target the Class Members with excessive pricing. The position was much more nuanced than that. After all, the Gives were the subject of real and genuine consideration, in our view, regardless of their ultimate value or not. Further, the major objective, or at least a significant aim, for BT was to "upsell" the Class Members to bundles. We are also conscious that we have been shown only a selection of documents here. We do not accept that in the context of a declining market, BT's aim was simply to "make hay while the sun shines" in terms of its pricing to Class Members.

### **Disproportionate impact of price increases on SFV customers ("the Disproportionate Impact Point")**

1173. The CR then makes a separate point that further evidence of unfairness is constituted by the fact that BT knew that the line rental increases had a disproportionate effect on SFV customers because they were not able to take advantage of the discounts available to bundle customers.
1174. The CR contends that this is an example of price discrimination which is a form of unfairness for the purposes of abuse of dominant position. It makes reference to the decision of the European Court of Justice in *Google v Commission* T612/17, 10 November 2021. The Court stated the following at paragraph 155 of the judgment:

“The abuse may take the form of an unjustified difference in treatment (see, to that effect, judgments of 17 July 1997, *GT-Link*, C-242/95, EU:C:1997:376, paragraph 41; of 24 October 2002, *Aéroports de Paris v Commission*, C-82/01 P, EU:C:2002:617, paragraph 114; and of 7 October 1999, *Irish Sugar v Commission*, T-228/97, EU:T:1999:246, paragraph 140). In that regard, the general principle of equal treatment, as a general principle of EU law, requires that comparable situations must not be treated differently and different situations must not be treated in the same way unless such treatment is objectively justified...”

1175. However, this statement was made in the context of a case itself where the allegation of abuse was not excessive pricing; rather it was an appeal against a Commission decision which had held that the favourable treatment, within Google’s general results pages, of links to Google’s own shopping services, as compared to links to competing specialised shopping services, was capable of infringing Article 102 TFEU. Since the main focus of the observations of the Court concerned the ability of Google to use its market power as a provider of search to distort outcomes between its rivals’ competing businesses in a downstream online shopping market, we do not see that the *Google* case is directly relevant here.

1176. That said, we deal below with the documents relied upon here by the CR.

1177. In notes made by Mr Bunt in October 2013 he said this:

“Solus Churn Trial – is owned by Kelly L. 5m solus out of 10, of which 60% are high propensity BB so we offer them BB bundles to upsell and ensure we keep. Of the remaining 2m what do we do with them... given their low propensity to BB (some we don’t want to touch because they are likely to wake up and realise how over-priced we are if we do), others are more sticky or already on the way out so we can try offers on them to keep them, especially the high value ones. Essentially high value customers are the least rational/conscious in behaviour. They will have UWC and the call on evenings and day times.”

1178. Mr Bunt accepted that (as in fact is obvious from the document) what he was saying there was about VOCs. These were notes that he made in his first week and they reflected the conversation he was having with one of his colleagues at that point. He said it was hard for him to say what the received wisdom was in the team at that point, but he did not demur from the views that he was expressing at the time. They included his perception that there was at least an element of the 40% of VOCs who did not have a high propensity to adopt broadband, so BT would not therefore try to “upsell” to them, and who were somewhat inert unless “prodded” as it were. That said, this amounts to a relatively small proportion of the Class Members as a whole.

1179. Then, in BT’s “Stakeholder plan for pricing” dated 4 April 2016, page 4 said this:

**“Problem statement:**

We face increasing regulatory scrutiny of price changes focussed particularly on the treatment of vulnerable customers. We face criticism that our increases in Line Rental disproportionately impact digitally excluded customers, who don’t benefit from competitively priced Broadband and associated discounts from that service.”

1180. This speaks for itself, but Mr Bunt accepted that it was identifying that the price rises hit the VOCs (being the “digitally excluded”) the hardest.

1181. A statement to the same effect was contained in another April 2016 document which was the draft of a briefing to go to Ofcom. In a marginal comment to this draft, Ms Blight wrote:

“Should we be as overt as accepting this?”

1182. We would also refer to the document quoted at paragraph 1164 above, because it is referring to maximising value from a particular sector.
1183. In a post-Commitments PR brief on voice elements of price change from June 2018, Mr Bunt noted that:
- “For me the important point in general is that customers who are Truly Solus, tend to be older, poorer, more landline dependent and by definition don’t benefit from the world of broadband, where prices generally are falling.”
1184. A similar point was made by BT in a January 2021 briefing document concerned with the origin of the Commitments and also this present litigation:
- “That price had steadily increased since 2009 at a rate of ~£1 a year as a mechanic for driving revenue growth in the consumer base (graph below as employed by Ofcom)
- Whilst average bundle price fell over the period, Landline-only customers did incur those increases along with increases to calls and calling plans, but offset for BT by declining volumes (c14% YoY)”
1185. In this context, we would refer back to our consideration under Market Definition of whether bundles acted as a constraint on SFV pricing, because we explain why we do not accept that overall, the line rental increases led to a pound for pound increase on bundle prices in the way that they did for SFV prices. See paragraphs 436-447 above.
1186. Overall in relation to the above, we accept that such materials show that BT was aware that it had much greater flexibility to raise prices with the SFV customers than it did with bundle customers. In a way, that is obvious because BT clearly knew that SFV Services were less competitive than bundles and knew it was making more profit on SFV than elsewhere. However, we do not see this as adding materially to the overall question of unfairness. It does not change the conclusion we reached in paragraph 1172 above.

**Price Rise revenue used to fund non-SFV investments (“the non-SFV Investments Point”)**

1187. A document dealing with Consumer Voice Strategy for 2015-16 onwards, dated 19 March 2015, stated that:
- Using core products to drive revenue to enable our bold and ingenious developments can undermine our warmth, care and honesty.
- Open to criticism that we exploit the vulnerable to subsidise new customers (e.g. caller display, increases to line rental, especially on true solus)
1188. In Mr Bunt’s Annual Price Change document dated 11 June 2015, ahead of the 2015/16 price change, increasing line rental by £1, he said this:

“Each year BT changes its prices. Historically this has been approximately inflationary, but increasingly super-inflationary price rises on largely inelastic products has provided significant upside for our business. This capital provides the oxygen for our business in the sense of its investment in content, spectrum etc. These changes are reported to different degrees in the media, usually defined by our transparency and clarity as well as how compelling our gives are. Reporting of these changes very much drives our thinking on timing (we try to only go once a year) and scale (we choose 6.94% because this is less than 7% which is associated with negative energy company price rises)... Our competitors have increasingly aligned their price changes with our in timing and scale:...”

1189. Mr Bunt accepted that “content” referred to the Pay-TV channel, for example BT Sport, and that “spectrum” refers to mobile phones. These were not SFV Services. He agreed that revenue from those services was used to invest in the former although he added that the revenue from price changes was used to invest in all products. In fact, the proposed £1 price increase was duly implemented.
1190. The CR contends that the fact of this investment in other products is itself a matter tending to show unfairness. We disagree. We would accept that investment in other products from SFV revenue cannot assist BT in showing fairness, but that is as far as it goes. The real question at this stage is the extent of the pricing excess considered alongside matters such as economic value.

### **Lack of Transparency (“the Lack of Transparency Point”)**

1191. The CR here argues that there was deliberate non-transparency on the part of BT in relation to customers, the press and Ofcom. Lack of transparency is a matter which can go to unfairness.

#### *Customers*

1192. The lack of transparency alleged here relates solely to HPS and the fact that, until BT was concerned about regulatory intervention it was not actively marketed. We have already agreed with that proposition when we dealt with HPS in paragraphs 270-301 above. We agree that this shows an element of seeking to keep SFV customers on the “normal” prices unless they were taking active steps to leave, for example. That said, this is a very limited point. Further, we have already found that there was sufficient communication with the SFV customers by which they could be made aware of price rises. See paragraphs 1109-1116 above.
1193. There is no evidence that there was a general lack of transparency with regard to the Class as a whole or over the whole of the claim period. Indeed, as noted below, BT made press announcements of price changes too.

#### *The Press*

1194. The first point to make here is that, unlike its competitors, BT did proactively announce its price changes to the press, as well as through its mandatory PCNs, and indeed many customers might learn about the price changes first from the press. However, that did not stop BT from considering ways of managing the story, as it were. Thus, Mr Bunt accepted that BT’s PR objective was to mitigate press attention or press response and so the less of a story they created, the better. He thought that the engagement of the media or the response of the media depended on how much information they were given in the first place.
1195. This approach was reflected in a “2014/15 Project Window: Execution Update” dated 24 June 2014, at page 13:

“Announce 22nd August to avoid Sport and spring and use the bank holiday weekend to buffer and fracture criticism.

Story will be seeded to journalists on late 21st so the print comms don’t appear until 22 August”

1196. Mr Bunt accepted, as is obvious, that the criticism referred to was that of the price increase.
1197. An additional point was made about how any percentage price increases were described. A draft of a briefing to a particular set of journalists said that prices were generally going up by around 6.5%. Against that, Mr Bunt added a comment that:
- “We are deliberately not raising a single price by more than 6.49% so that they can't round up to 7% in the headline which we saw last year {I'm told}. We could even claim 6%”
1198. We do not think there is much in this point. It would be understandable to wish to avoid journalists rounding up a 6.5% increase to 7%. Equally, it would have been disingenuous for BT to claim that the increase was only 6% but while Mr Bunt referred to this, it is not suggested that this is what BT did.
1199. Overall, we do not think that there was a real lack of transparency to journalists in the sense of, perhaps misleading them or withholding key information. The fact that BT wanted to “manage the story” seems to us to be little more than a desire to manage its PR as most large companies would.

#### *Ofcom*

1200. We deal here with a number of documents relied upon by the CR.
1201. The first is an exchange of emails between Mr Bunt and others, following a meeting with Ofcom which had taken place on 20 January 2016. At that meeting, Ofcom had presented a number of slides dealing with, among other things, BT’s Voice ARPU. Mr Bunt and his colleagues clearly took issue with some of the figures which Ofcom presented. In that context he said this:
- “Slide 4 BT Basic monthly call spend (excluding the small allowance) is £3.29 not £23! That’s disgraceful! Voice ARPU is 2014 was closer to £27 than £19 (I don’t want to tell them what our ARPU is but it that number is miles out.”
1202. Mr Bunt acknowledged in evidence (as is obvious from the text) that he did not want to reveal BT’s actual ARPU. This was in the context of his observing that the figure that Ofcom had come up with was wrong. However, Ofcom was not asking BT for its actual ARPU at that stage, it had simply been commenting on what it thought were comparative ARPUs between different telecoms providers, so it is not as if BT was misleading or withholding information from Ofcom. We accept that it could, no doubt, have told Ofcom more at this stage had it wished, but we do not think much turns on the fact that it did not.
1203. The next document is an email from Mr Bunt dated 26 May 2016 just ahead of a meeting with Ofcom later that afternoon and in respect of which he and his colleagues were finalising a deck of slides. In part of that email he said this:
- “Did we conclude on opening up HPS to all of COT? – I included the sizing in the email I sent to the chain yesterday at 5.35 (attached) and no one responded either way .....the costs are £0.6m in 16/17 and £3.6m in

17/18 and I'd recommend against it. Either way though, I'd definitely not talk to Ofcom about it, because it exposes the current position."

1204. In cross-examination, Mr Bunt accepted that he was "absolutely" saying that he did not want BT's position on HPS to be exposed to Ofcom and that it was "another example" of BT "holding back information" from it. However, in re-examination he explained that if Ofcom was told that HPS would now be opened to all of the COTs, this would suggest that this had not been the position before. This was not in the context of information sought by Ofcom, but the meeting was part of BT having wider conversations with it where BT was being proactive. Again, as we see it, it was not in fact an example of holding back information that had been sought from BT. It was not suggested to Mr Bunt that there was some overarching duty on BT to disclose all of its commercial information to Ofcom in some unstructured way.
1205. There was the lengthy email exchange from July 2016 about a letter which was to be sent to Ofcom following a recent meeting with them. Ms Blight was cross-examined about this at Day 8/39-59. One of the features which BT wished to emphasise to Ofcom was HPS and the savings which this would entail for customers who took it. Mr Petter, the then CEO, Ms Blight and others debated whether to give an actual price for the proposed new HPS products, because that might imply that BT would be increasing prices (again) in the following year, namely 2017/18. At this stage, the 2016/17 price change had just been implemented. (In the event of course, prices were frozen for VOCs until 1 April 2018 when the Commitments came into effect and until 16 September 2018 for SPCs).
1206. On the other hand, there was the concern that if actual prices for HPS were not given, this might give the appearance of concealing something. Thus there were the following comments within the email exchange:

"Re the new tariffs. I worry here that pitching the pricepoints cited here presume an increase to our base tariffs of £1 – the problem with that is that it confirms OFCOM's suspicion that we always take a £1 without thinking. Would it be clearer to say that the low volume of calls variant would be priced at the same price as standard line rental; and that the other variant would be priced in line with whatever change we make to standard LR prices today relative to the current HPS price? The one point where our meeting got awkward was where it was obvious we were assuming we could just take a £1 next year.[Murray,SC,Stuart,SLA1 R] I think we're stuck here. In the meeting we proposed pricing and agreed to confirm the pricing we would offer (we had a bit of confusion if you remember about what the price of each variant would actually be). I've adjusted the text for the HPS EWC product, but think we still need to include the proposed charge for the HPS UAC package, and least said here might be best. Would welcome James and Meg's thoughts." [email from Mr Petter]

"Not sure I'm getting the final point. The two price points for HPS are both compared with today's prices aren't they? I would agree with general point that we should not signal in any way our plans about future price changes" [email in response from Mr Tickel]

"What I really need is help on the text to deal with John's point, as we really have to put in a number, otherwise Ofcom won't take it seriously. The problem is that the number might indicate a plan next year to again increase standard line rental." [email in response from Mr Murray]

“I agree with John’s concern. The fact is, we have an MTP assumption for line rental but we don’t have an agreed decision on timing or amount. I just had a kick off with Hugo and Pete where we debated if we would go to £19.99 or £19.49 (on standard line rental) so it is definitely a live issue.” [email from Ms Blight]

1207. In respect of all of that Ms Blight commented:

“I agree with John’s recommendation as we shouldn’t really commit to a price point until we know what line rental price will be next year.... I can see how committing to the prices does help us a bit but if we do, there is actually a chance that we commit to higher prices than we need to!”

1208. The bottom line was that BT at this stage did not want to disclose its price change intentions for the following year especially if it was a further £1 increase. Ms Blight described it in cross-examination as a Catch-22 situation because setting the price now for the proposed HPS would necessarily reveal commercially sensitive information about any price increases for the following year. In this context Mr Murray had made a reference in the email chain to “the Devil and the deep blue sea”.

1209. Ms Blight explained the problem at Day 6/53 as follows:

“I think he is saying the options available to us: we either do not give them a price and talk about the delta, we give them a price that could be too high and reveals that we have been —we have a planning assumption of a £1 increase, or the third would be put in the wrong pricing and then either need to stick with it, or have a lower price than we would otherwise commit to. So none of the options in front of us are a good one. If we want to communicate in —we are trying to communicate as clearly as we can but when we do not have the answers.”

1210. Later, but in that context, she said this at Day 6/53:

“Yes, the challenge at this point was that we had not yet made the decision as to what next year’s price change would be, which would be the 17/18 price change. So we were —we had just launched or put into effect the previous price change. We were in process of planning for the next one. The budgetary assumption was this £1 that I have mentioned before. But we were being asked by Ofcom to make a commitment as to what Home Phone Saver would be the following year, but if you do not know what your line rental price will be, it is very hard to make a commitment as to what your Home Phone Saver price will be in a year’s time. So that is why there was a debate and a discussion: how do we —do we just make a commitment now, not yet knowing what line rental will be, or do we express it as a discount, or do we just make —decide that it is going to be £1 next year, without having gone through all the normal research we would do? That was the challenge we were in to.”

1211. In the end, the letter, as sent to Ofcom, did not state the actual price of HPS but described what the savings would be as against the current tariff, and noted that they would necessarily be more, if the price later went up.

1212. In the end, as Mr Armitage said, he was making a limited point in cross-examination here to the effect that BT did not want to give Ofcom the impression that line rental would go up the following year by £1. That is undoubtedly true, but Ms Blight explained why there was a concern especially at the point which was one year ahead of any further price change. Yet again, BT could have volunteered to Ofcom all of its commercial thinking for the following year at that stage insofar as it actually knew what would happen in the 2017/18 price change. However we do not think much turns on the fact that it did not, or that it had an obligation to do so.

1213. We then turn to three particular points made about passages contained in BT’s Response to Ofcom’s 2017 Provisional Conclusions.

1214. Under section G of the Response, contending that Ofcom’s pricing analysis had ignored the broader context of switching to bundles driven by lower incremental broadband prices, paragraph 168 dealt with each of the arguments made by Ofcom on pricing. In each subparagraph, the point made by Ofcom is in italics and then BT’s response follows.

1215. Paragraph 168 (c) read thus:

*“There is evidence that BT acts as a price leader, with other CPs following its increases in line rental in terms of both timing and magnitude;*

There is no reliable evidence of BT playing a price leadership role. Oxera has reviewed the limited evidence presented by Ofcom and concludes that (i) Ofcom’s sample is too small to reach meaningful conclusions (ii) in recent years BT has implemented price changes first but in prior years other CPs have changed their prices first, and price changes do not follow an annual adjustment pattern in any event.”

1216. We have found in paragraph 480 above line rental price changes were generally followed by its rivals, and in answer to a question from the Tribunal, Mr Bunt accepted that the passage at paragraph 168 (c) (which he did not write) was misleading. In fact, as can be seen from the whole of this passage, the answer was summarising what Oxera, instructed by BT, had said in paragraph 2.4.5 of its report (entitled “is Ofcom’s approach robust from an economic perspective ?”) which formed Annex 3 to the BT Response. Here, it said as follows:

“Despite this, Ofcom argues that prices have converged as a result of price increases and, in particular, that other CPs have followed price changes implemented by BT over the period April 2014 to January 2017 (RMSLTS, para. 4.52).

We do not consider that this provides any reliable evidence of BT playing a price leadership role for a number of reasons.

The period is too short to make any meaningful inferences. As noted by Ofcom, CPs appear to be updating their prices on an annual basis (para A8.63). As a result, the period considered by Ofcom (2014–17) contains a sample of only three price adjustments (Figures A8.26–A8.28).

What might appear to be price leadership is likely to reflect BT implementing its annual price changes earlier within the year for recent years—indeed, the assumption that price adjustments are annual is incorrect to begin with. In 2014, BT raised prices in December, in 2015 it raised prices in October and in 2016 it raised prices in July (Figures A8.26–A8.28).

If prior years are taken into account, other CPs adjust their prices prior to BT. In particular, in 2013, Virgin Media adjusted its price first; in 2012, Sky adjusted its price first; and prior to that price adjustments were implemented more than once per year, such that it is no longer meaningful to speak of a CP changing price before or after another CP.

The view taken by Ofcom—that BT is a price leader—is therefore not clear from the limited evidence Ofcom presents.”

1217. It can be seen that this is quite a nuanced and limited point. Once the context of what Oxera was saying (and addressing) is considered, it is not as misleading as might first appear. We accept, of course, that BT internally had considered that the line rental prices it did choose to implement were likely to be followed by the competition during the claim period, and it did not volunteer those thoughts here.



1218. Then, at paragraph 168 (d), the Response said this:

*“price discrimination to offer greater discounts to more engaged customers (for example, through its Home Phone Saver tariff) allows BT to increase prices for (largely unengaged) SFV customers whilst limiting the risk to the revenues it earns from more active customer groups.*

Given the active marketing by BT of the Home Phone Saver product, there can be no suggestion of a price discrimination strategy. Rather BT created this product in the face of competition from the Post Office.”

1219. We have dealt with this point specifically at paragraphs 297-299 above. The short point is that as at 19 May 2017, it may well have been correct to say that HPS was being actively marketed.

1220. Finally, at paragraph 12 of the Response, in the Executive Summary, BT said this:

*“Going forward, the ASA’s intervention (which prevents broadband providers from advertising the price of broadband and line rental separately) is likely to change these dynamics by reducing incentives to raise the line rental price. Firms may, therefore, consider line rental reduction as a further means of competing for voice-only customers alongside product innovation and discounts (although dual play providers may still balance this with promoting further uptake of bundles by keeping implicit broadband prices low).”*

1221. This was all in the context of disagreeing with Ofcom’s approach to market definition, and was the subject of detailed commentary at, for example, paragraphs 57 and 58, and where the former paragraph said that Ofcom itself had accepted that the ASA Ruling meant that there would be less pressure on CPs to increase line rental prices for SFV services to match increases in line rental prices for dual play tariffs. Oxera then dealt with the subject in its report, in connection with market definition, in its sections 1 and 2.

1222. What in fact happened, of course, was that prices were frozen for SFV customers and then reduced for the VOCs but with price increases for SPCs as from September 2018.

1223. Plainly, if one looks at SPCs’ line rental, it did not reduce and the economic point made by Oxera proved not to be correct. But this hardly means that there was some deliberate cover-up by BT.

### *Conclusions*

1224. While there were, no doubt, occasions when BT could have chosen to reveal to Ofcom in its discussions with it, more detail about its commercial strategies or plans (if made) and while there may have been some occasions when it could be said that BT was disingenuous, we do not conclude that there was an overall pattern of non-transparency in the sense required to act as a factor driving unfairness.

### **Effect of the Exploitation, Disproportionate Impact, non-SFV Investments and Lack of Transparency Points**

1225. We do not accept that these points, whether taken individually or collectively either “corroborate” the CR’s case on economic value, or otherwise materially act as factors pointing towards unfairness.

## Price Rises during period when Ofcom expressing concern

1226. A further point made by the CR is that BT knew that Ofcom had “rung the alarm bell” at the start of 2014 but continued to push through SFV price increases.

1227. By way of preliminary, the CR contends that if this was the case, then it contributes to or constitutes unfairness for the purpose of Limb 2. In this regard it cites paragraph 88 of *Aspen*:

“Aspen implemented this strategy, even though it was met with strong concerns from within Aspen and from Aspen’s distributors. [Aspen employee] expressed serious concerns about such a strategy: “*this is totally unrealistic in today’s environment*”; “*who ever came up with these numbers has no connection with the reality of the pharmaceutical market in Europe*”.

1228. This observation was in the context of the Commission’s narrative about Aspen’s pricing policy for the relevant drug product, where patients depended on them and where there was no substitute in Europe. We do not think that this assists on what constitutes unfairness in our case but in any event, as we shall show, we do not think there is much in the substance of this point.

1229. As to the facts, it is of course correct that in January 2014, Ofcom published its report on the Cost and Value of Communications Services in the UK (“the 2014 Report”). At Section 2.1.6, it commented as follows:

“Some standalone line rental charges have risen over recent years but cheaper alternatives are available. There is an active market in the UK for standalone (i.e. not bundled) fixed line rental services. Retail competition is enabled by regulated access to wholesale line rental, the price of which has fallen and will continue to fall. This has enabled the provision of competitive services by other providers. For example, the Post Office currently offers a standalone landline service for £12 per month.

Social tariffs are also available as a low cost option for low income users. The price of BT Basic, the principal social tariff, is lower now in real terms than it was six years ago. This is a good choice for eligible consumers with low outbound call usage (for example, for consumers who rely more on receiving than making calls to keep in touch). Eligibility is defined as being in receipt of certain benefits available to low income households

Despite this range of choice and the overall positive trend in fixed voice costs, some retail prices for line rental have increased in recent years. This is related to the fact that landlines generally tend to be sold as a bundle with other products – historically with voice calls, more recently with broadband. Market competition has tended to focus on the headline price of the bundle, which has generally fallen. Consequently consumers buying a landline service without broadband may not benefit fully from the effects of competition. Furthermore, some providers (TalkTalk and Virgin Media) have recently ceased their standalone landline service. Ofcom will continue to monitor this situation carefully.”

1230. A chart at page 10 showed decreasing WLR prices and BT’s line rental prices, which were generally rising.

1231. We accept that it is unfortunate, to say the least, that the 2014 Report was not included in the list of documents provided to Mr Matthew. It was also unrealistic for him to describe what was said at Section 2.1.6 as merely an “observation”. It was somewhat more than that, although not entirely negative. After all, the action point was that Ofcom would monitor the situation going forwards.

1232. In cross-examination, Ms Blight accepted that she would have been aware of the 2014 Report at the time and that it was not giving BT a “clean bill of health” in respect of landline only customers and

she was aware of Ofcom's concerns. Indeed, BT's Project Window 2014/2015 Pricing Update of 24 February 2014 (also referred to at paragraph 1023 above) at page 26 said that it would develop propositions to build a strong defence against the key issues highlighted in the 2014 Report. One such issue was described as non-switchers being subject to "punishing price changes". The recommended propositions were Fixed Phone Saver (to become HPS) and an online optimiser (which became Right Plan).

1233. That said, Mr Bunt said that the perceived level of urgency and focus on the part of Ofcom came after the speech by Sharon White in October 2015. Ofcom's concerns were then highlighted in an exchange of emails in December 2015 following a discussion between Mr Benson and Ofcom which was concerned that BT and other providers were too focused on dual play and that most of the marketing/discounts were for customers taking bundles and it asked for a meeting to discuss these matters. Ms Cheek commented that this was "a bit of a worrying development, although not unexpected...". Mr Petter was also reported as saying that the price increases were a worry for him. As that email exchange also makes clear, by this stage, BT had been engaging with Ofcom to a significant extent including by providing much information.
1234. This was followed in February 2016 by Ofcom's Initial Conclusions from its Strategic Review of Digital Communications, which noted that line rental prices were increasing, despite falling WLR prices. There was also BT's perception of criticism in relation to "digitally excluded customers" which is referred to in the document quoted at paragraph 1024 above.
1235. Reference is also made to Mr Oxley of Ofcom telling Mr Shurmer, BT's Group Director of Regulatory Affairs to "look into my eyes, we will re-regulate" in June 2016, and the fact that BT still made a price increase the next month. That is correct but the implied criticism of BT here is somewhat unrealistic. The price increase had already been notified in April 2016, and in any event BT was at the time engaged with Ofcom making various proposals.
1236. In answer to a question from the Tribunal about the LR price freeze in January 2017, Mr Bunt said that by then, BT was conscious of Ofcom's ongoing review and indeed that BT already had conversations with Ofcom about a price freeze and even a price decrease, prior to January 2017.
1237. We follow all of the above. However, we do not see that the fact that BT made some price increases since 2014 and up to January 2017 during which time Ofcom had expressed some concerns (but without intervening as such), really adds to or creates unfairness. Very large companies supplying consumer products in the position of BT are obviously aware of regulatory scrutiny and indeed Ms Cheek was in BT's Regulatory Group. A company such as BT may or may not react more or less quickly when there is a concern over prices. However, the real question, as it seems to us, is whether there was actual unfairness by reason of the prices charged and other factors. Put another way, if

BT's pricing was not otherwise unfair, the fact that some price increases took place when Ofcom was expressing some concerns would not make it so.

## **Market Dynamics**

1238. BT contends that (if necessary) there were two aspects of how it dealt with market dynamics which served as justifications for any excessive pricing, namely:

- (1) Migration Intent; and
- (2) Rebalancing.

### *Migration Intent*

1239. This can be dealt with briefly. We have already rejected the existence of any such intent on the facts. See paragraphs 317-326 above.

### *Rebalancing*

#### Introduction

1240. The argument here is that the line rental price increases prices offset the decline in fixed call volumes and revenue. The CR accepts that there was this phenomenon. However, it denies that it can constitute a justification for excessive pricing.

1241. We address this argument in the way in which it is now formulated in paragraphs 746-758 of BT's Closing.

1242. It begins with the (agreed) proposition that ARPU was broadly flat over the claim, and indeed for some time before. The flat ARPU is a reflection of the fact that although line rental prices went up, there were other changes, including declining call volumes and changes to the ways in which calls were priced that had an offsetting effect on BT's revenues. That, too, is uncontroversial.

1243. BT then makes two specific points under the subject of Rebalancing, although we think the first is not really a rebalancing argument as such.

#### Flat ARPU and subjective value

1244. BT first contends that the fact that prices for the customer had not gone up in "real terms", because of the flat ARPU, goes to the assessment of the subjective value which they would ascribe to their landline product. Reference is made to what Dr Jenkins said in cross-examination on Day 18/108-111. In fact, although Dr Jenkins certainly said that the flat ARPU goes to unfairness (or not) she did not bring in the question of subjective value, at least not expressly.

1245. At all events, we reject the general proposition that flat ARPU can affect the issue of fairness without more (which appears to be what BT is saying), in circumstances where the price across the claim period has already been found to be excessive under Limb 1. The fact that BT does not then change

the price in terms of what the customer actually pays does not seem to us to be relevant. After all, ARPU was itself taken as a measure of price for the purpose of the Limb 1 exercise.

1246. Secondly, we think it unrealistic to suppose that customers actually did place subjective value on their landline product because of the flat ARPU, i.e. because they know that the amount they were spending each year on their SFV Service was in fact about the same. There is no evidence to support this at all and indeed if it were correct, it is very odd that BT spent the time that it did considering its price increases, albeit that they tended in the end to be inevitable, save over the price freeze period.

1247. So there is nothing in this first point.

#### ARPU and rebalancing

1248. The second respect in which BT relies upon the flat ARPU is the rebalancing argument, properly so-called. Dr Jenkins deals with this at paragraph 7.25-7.41 of HJ1 and in her Annex 9. She says that the rebalancing effected by compensating for a decrease in call revenue by line rental increases is recognised and is a rational response on the part of BT. It is therefore a legitimate explanation and justification for the excessive prices charged.

1249. However, because Dr Jenkins has used ARPU as the “price” for the purpose of Limb 1 (so the rebalancing has been included, as it were) she says at paragraph 7.26 that the rebalancing argument is relevant for the CR’s alternative claim which is concerned with excessive pricing in relation to line rental only. However, we are here dealing with the CR’s primary claim. It is true that Dr Jenkins goes on to say that rebalancing is also relevant “to an understanding of the line rental price in the context of BT’s pricing as a whole” but it is not clear how. Indeed, she says that her assessment of the primary claim “includes any price rebalancing effects”. See her footnote 361, and also her comments at paragraph 8.1.7 of the JES.

1250. On that basis, we cannot see how the rebalancing argument is relevant to fairness on the primary claim. In any case, we think that there are further problems with it.

1251. First, if excessive prices are being charged, it hardly follows that there is a right for BT to charge or keep on charging them, just because of declining call revenues. It is not as if BT was now failing to break even on the landline product as a whole and its gross margin, at around 65% was significant.

1252. Second, BT itself recognised at one stage that declining call volumes did not result in a distinct cost increase that could justify the rate of line rental price increases. This arose in the context of when Ofcom was already engaged in discussions with BT about its line rental prices. There was the following email exchange in July 2016 in relation to some draft letters due to go to Ofcom:

“[From Mr Tickel to Ms Blight and Mr Murray]

Is there anything we can add in here about cost pressures and why we and other players have been looking to increase certain charges? The strength of points in the letter is undermined by fact that in competitive markets with informed and engaged customers, prices would be expected to converge towards efficient costs.

[From Mr Murray to Mr Tickel]

James, I get your point about prices falling towards efficient costs, but... the problem here is that Jonathan would say, looking at costs from a solus lines and calls made over those lines perspective only, that we are making a significant return. Whilst we can argue that the revenue and profit made on calls has reduced as: (i) call volumes have reduced, and (ii) more customers take – to a greater or lesser extent – inclusive call packages, the high profitability that Jonathan points to, does persist? I'm not sure how we get round this? I don't see an obvious argument to justify (in a way that would satisfy Jonathan [Oxley of Ofcom]) why line rental has increased at the rate that it has (leaving aside the justification this year created by the change in care level)?"

1253. Finally, the argument here is limited. This is because at paragraph 8.1.8 of the JES, Dr Jenkins said that according to her model, there was a clear decline in gross margin earned on fixed calls from 2014 onwards, which itself would explain approximately 28% of the increase in annual line rental charges. So it could not explain the major part of them.
1254. Overall, we do not accept the rebalancing argument as a justification for the excessive prices, nor even as a factor going towards the question of fairness or otherwise. It is, however, evident that the changes in call volumes and pricing do interact with line rental price changes, and mean that it is overly-simplistic to equate the growing gap between line rental prices and wholesale costs as reflecting ever-increasing profitability across the claim period. But all of this is incorporated in our Limb 1 analysis: BT's SFV prices were in excess of the competitive level at the start of the claim period and they remained so throughout it.
1255. We should add that there is other evidence from 2015 and 2016, in the context of press and Ofcom scrutiny, that BT itself was finding it difficult to provide a justification for the line rental increases. This goes to the migration intent as well as the rebalancing arguments, if further points were needed.
1256. In August 2015, Mr Bunt was being asked how a colleague should respond to a question from a journalist who had initially asked what had caused the cost of line rental to increase so sharply when inflation had been flat, and when he was given an answer which did not address the point he said that he wanted to know what were the factors that were causing the line rental increase specifically. Mr Bunt agreed with his colleague that she could say that the investments being made by BT affected the prices of all of its products, and further:

"His original question assumes there is a cost based cause for increasing Line Rental which there isn't. We can't answer in that way, so I would keep it vague."

Apart from a general remark about investments, Mr Bunt felt that there was nothing else that could really be proffered in relation to price increases.

1257. Then, ahead of a meeting with Sharon White of Ofcom, Mr Tickel emailed Mr Murray on 27 April 2016 thus:

"I am looking.

Trickiest Q:

Why have you/others been focussing price increases on line rental and calls charges?"

1258. Mr Murray replied:

“Whatever the answer, it's unlikely to be attractive...  
Story is probably not that there is a focus on increasing line charges, rather there has been a focus on the vast majority of customers who buy dual / triple play and getting the pricing right for those customers. And solus has been a secondary consideration, rather than primary focus?”

1259. Finally, the document referred to at paragraph 1252 above is also relevant here.

#### *Conclusion on Market Dynamics*

1260. It follows from the reasons given above that we do not accept that the two market dynamics points made by BT, on migration intent and rebalancing, assist it on unfairness.

#### **The significance or otherwise of Ofcom's 2017 Provisional Conclusions and Statement**

1261. The CR places emphasis on these documents (“the Ofcom Reports”) as supporting evidence for its claim here. We accept that Ofcom's findings there were adverse to BT in the respects there set out. We have referred to some of them at paragraphs 156-161 above. Indeed, at the certification stage, considerable reliance was placed upon them and the fact of the Commitments by Mr Parker in DP1 and DP2, although these reports included analysis by him as well. At that stage, we considered it right to give weight to Ofcom's Reports in the context of satisfying ourselves that the claim had at least a real prospect of success, as opposed to being hopeless. All of that was a legitimate approach at that point, but it did not mean that we would then be bound by the Ofcom Reports at trial (or, we would add, bound to give them particular weight at trial) as was noted by the Court of Appeal at paragraph 100 of the judgment of Green LJ in *FX*, referred to at paragraph 106 above. As we have noted generally at paragraphs 105 - 108 above, it is for us to decide what weight, if any, to give to the Ofcom Reports. Pursuant to what we said in paragraph 108, we have in fact made reference above to various aspects of the Ofcom materials (including the 2017 Provisional Conclusions) on specific points. However, what we are concerned with here is the CR's reliance on the Ofcom Reports in relation to their general findings.

1262. In fact, matters have moved on considerably from the certification stage in at least the following respects which were material so far as Ofcom was concerned:

- (1) Pricing Metric: The focus of the Ofcom Reports and indeed the CR, were very much upon increases in line rental across the claim period. In fact, and as both parties accepted, the appropriate price metric for Limbs 1 and 2 was ARPU; this is important because ARPU remained flat;
- (2) Switching: Ofcom grossly underestimated the level of switching. The actual levels were far greater than the 1% of customers which Ofcom thought had switched in the previous 12 months;

- (3) Customer characteristics: Ofcom saw VOCs having the particular characteristics of being elderly and vulnerable, and disengaged. Indeed initially, this was the focus of the CR; by trial, however, the CR's case did not essentially rest on any particular characteristics of this group of customers, as opposed to consumers in general;
- (4) Common Costs: this was the subject of much more evidence and consideration than under the Ofcom Reports;
- (5) Expert Evidence: by the time of trial, there was a very considerable body of expert evidence and the experts themselves have had access to far more data than had been available to Ofcom. That is hardly surprising given, in particular, that Ofcom did not proceed to a final conclusion and formal price regulation. There was expert evidence here on every step of the *United Brands* exercise, albeit that it was more extensive on some elements (for example Market Definition and Limb 1) than on others.

1263. We should add to this that of course, Ofcom was not obliged to and did not conduct a strict s18 analysis. It did not undertake a full Limb 1 consideration of excessive pricing, although it did find BT's prices to be above competitive levels. Nor did it address unfairness directly in the Limb 2 sense.

1264. Further, there remains the fact that Ofcom did not ultimately propose a reduction to the pricing for SPCs. We accept, of course, that it did find them to be above competitive levels and at that stage, it could not distinguish between VOCs and SPCs. However, it accepted the engagement undertakings offered by BT in respect of SPCs. The CR says that this difference of treatment is irrelevant because it only relates to a question of "remedy". We think it is rather more nuanced than that, because Ofcom clearly saw the two groups as different. Ofcom did not regard SPCs as vulnerable in the way that it regarded VOCs. And while Ofcom had another opportunity to reconsider the position of the SPCs in 2020, it simply maintained the existing position.

1265. Mr Parker ventured a speculative suggestion as to why Ofcom may have taken this approach to SPCs consistent with it regarding the position for them as unfair as it was for VOCs. For example, he suggested that this was simply a product of the negotiations with BT and Ofcom, who decided to go down the route of a speedy settlement rather than full-blown findings which could be appealed. However, at the end of the day he rightly accepted that what Ofcom did was ultimately a matter for it and he could not speak for Ofcom.

1266. In this context, we do consider there is force in Mr Matthew's point (which is obvious as a matter of analysis anyway) that at the end of the day, and notwithstanding what it said as recited in



paragraphs 156-161 above, Ofcom was dealing with *ex ante* regulation with regard to a number of factors. It was not making *ex post* findings. Ofcom's intervention on VOCs must also have partly been motivated by its duties to protect vulnerable customers, which is a distinct regulatory objective as opposed to the Chapter II considerations that lie before us in this case.

1267. In fact, this case demonstrates the pitfalls of attempting a rigid “read-across” from the findings of a regulatory body, especially where there was no final conclusion. Such pitfalls include experts being asked to divine the body's thinking at certain points and inviting a specialist tribunal such as this then to draw inferences as to why it did or did not make a particular finding or adopt or not adopt a particular remedy where its own documents do not themselves make the position clear.
1268. As against that, we have here been presented with what might be described as the primary materials on the issues in question (although we have pointed out where evidence which could have been adduced was lacking). In such a situation, it is very hard to see why it is then necessary to ascribe any material weight to the Ofcom Reports. The matter can be tested this way: if our conclusion is that BT's pricing was unfair without regard to the Ofcom findings, then they are not necessary. On the other hand if we would conclude that its pricing was not unfair, having taken into account everything but the Ofcom findings, it would be remarkable if they could then transform the position into one of unfairness.
1269. Of course, what weight to ascribe to related regulatory findings or decisions, or those of other tribunals, is highly fact-sensitive. Sometimes (as in *FX*), they may be of particular use. In this case however, and for all the above reasons, we do not consider that Ofcom's overall findings here amount to supporting evidence of unfairness to which we must give material weight.

### **Conclusion on Unfairness In and Of Itself.**

1270. For all the above reasons, we conclude that BT's pricing was not unfair in and of itself. We therefore turn to the CR's alternative case based on unfairness by comparison.

## **LIMB 2 – (2) UNFAIRNESS BY COMPARISON**

### **Introduction**

1271. We have explained above how the “by comparison” element of Limb 2 works, in the context of unfairness generally. Given our conclusion on the “in itself” element, the short point is that if we conclude that there is also no unfairness by comparison, then overall, the conclusion must be that BT's pricing was not unfair.
1272. We consider that the assessment of unfairness by comparison is often not a straightforward exercise. For one thing, even where the firm in question is in a dominant position, there can still be price

dispersion in the market, and it does not follow that because the firm's price is above that of its competitor, even if significantly so, this renders it abusive without more.

1273. Further, it can be difficult to obtain comparators which are truly comparable. In this case, the position is made more complicated because the "price" which we have been assessing is the ARPU for BT's SFV Services, rather than line rental in isolation. A comparison which only looks at line rental will certainly be incomplete and for this reason may therefore be inadequate.

1274. Yet further, the result of the comparison exercise has to be that the prices charged by the firm in question are unfair. As with the first approach to Limb 2 ("in and of itself") the mere fact a price exceeds those of comparators does not make it unfair without more.

1275. The following comparators arise for consideration here:

- (1) From the CR's perspective, line rental pricing (a) under the Commitments and (b) as charged by the Post Office; and
- (2) From BT's perspective, (a) its competitors' line rental pricing, (b) that of HPS and (c) pricing under BT's Business tariff.

1276. The CR contends that its comparators show that BT's pricing was unfair and that BT's own comparators are inapplicable. BT contends precisely the opposite.

### **Commitments Pricing**

1277. The preamble to the Commitments, which is in Recital (B) to the Ofcom Statement, says as follows:

"BT now voluntarily provides the commitments set out below and, in particular, provides the greatest possible price reduction for our true voice only customers consistent with a competitive outcome."

1278. The CR says that pricing under the Commitments is a good comparator because BT would not have agreed to price reductions below the competitive level. Further, it is not as if BT has adduced any evidence to show that the pricing under the Commitments was or has turned out to be uneconomic. Mr Parker has undertaken a comparison of line rental prices by subtracting £7 from each of the relevant BT SFV Services as adjusted for inflation. This reveals that BT's pricing exceeded the comparator price by 30-50% throughout the claim period. This amounts to a significant and persistent differential (using the language of Limb 1) and thus fortifies the conclusion that the pricing was unfair. As we understand it, there is no dispute as to these actual figures.

1279. However, BT contends that this is not a relevant comparison. First, it is said that this part of the Commitments was offered in respect of VOCs only, to address what Ofcom had said were specific concerns about what it perceived was a particular problem with vulnerable customers who did not have an internet service. In other words, Ofcom was addressing a different policy goal from that which motivated Chapter II. Moreover, Ofcom's proposal, as accepted by BT, was not in fact the

product of any formal or other actual finding of unfairness. It was also forward-looking only and therefore did not address previous pricing.

1280. Furthermore, although Ofcom proposed a price which it thought would enable competition from other suppliers to be sustained, this did not in fact happen. Indeed, suppliers such as TalkTalk and Sky had stopped actively marketing to voice-only customers before the Commitments, suggesting that even the pre-Commitment prices and high profits earned by BT at that stage did not provide an attractive commercial proposition for these rivals.
1281. We think there is force in these points made by BT. Moreover, the fact that BT was prepared to reduce its prices for VOCs (but not SPCs) does not itself mean that its pricing otherwise was unfair. This follows from the fact that, as we see with price dispersion, there is a range of possible pricing outcomes for any one product that is potentially consistent with workable competition. To conclude that the higher price is unfair requires a broader assessment of the differentials and their causes.
1282. The position of the Post Office is slightly different and we discuss this specifically below.

### **The Post Office**

1283. The one competitor who did match (in fact slightly undercut) the Commitments pricing, initially, was the Post Office. It maintained that position from May 2018 through to March 2020. It then raised its prices but stayed in the market until it sold its business to Shell in 2021.
1284. The question, of course, is why the Post Office put its price up significantly from March 2020 to around £15, where the Commitments price was £11.99. It may have been because it was not economic, at least not if it did not gain market share. In fact, BT increased its market share over the Post Office in this period. It may also have been that in the absence of any increased market share, it thought that it might as well try and earn more from the customers it already had. We do not have evidence from the Post Office about this.
1285. Overall, however, we do not think that the example of the Post Office, which was something of an outlier here, and over a relatively short period before increasing its prices, is a persuasive comparator. Nor does it make it easier to accept the Commitments price as a comparator.
1286. On that basis, had we stopped there, we would not consider that the CR had made out its case on unfairness by comparison.
1287. However, we should consider BT's comparators as well.

### **The Pricing of BT's rivals**

1288. First, BT relies upon the pricing of its rivals, principally TalkTalk, Sky and Virgin Media. None of them reduced their VOC prices down to anything like the level of the Commitments price.

1289. The CR's essential response to this is to say that the rivals' prices were not meaningful because they were not set in truly competitive conditions. Rather they were within a distorted market and this was symptomatic of price leadership by BT. As to that, we have already expressed the view that, although most of BT's rivals chose to follow BT's line rental price increases, there is no evidence that in doing so they were able to earn excessively high profits; see paragraph 492 above.
1290. Rather, and this does not depend on the presence or absence of price leadership, if one looked at call prices, BT's call prices were often similar to, if not below, those of its rivals and there was no suggestion that call pricing by itself, was unfair. The call prices were the same as those charged to bundle customers. Mr Parker thought that there could be a difference because a larger proportion of SFV customers than bundle customers would remain on "back book" (i.e. higher) prices due to the length of time they had been with BT. However, there was no real evidence about that, nor was Mr Bunt asked about it in cross-examination although he dealt extensively with call pricing in JB3. Further, it is not as if SFV customers did nothing about elements of their bills. For example, as at 2016, 88% had changed some aspect of their line or call plans, as BT noted in its s135 response to Ofcom. So they could equally have gone from back to front book, as it were.
1291. We consider, therefore, that the position of BT's competitors is at least some evidence that its prices were not unfair and in any event is a counterbalance to the CR's comparators, if it were needed.

## **HPS**

1292. We considered this product, in the context of market definition, at paragraphs 270-301 above.
1293. Originally, HPS was put forward as a comparator by CR. See paragraph 136B of the Re-Re-Re-Amended Claim Form. However, it was then deleted from the final iteration of the Claim Form dated 11 December 2023.
1294. Before that deletion, Dr Jenkins had addressed it in HJ1. She undertook a comparison of BT's SFV ARPUs with those of HPS. See Figure 7.13 under paragraph 7.87 of HJ1. This showed that BT's SFV ARPU was always above, or at least no lower than, HPS's ARPU. She pointed to the similarity of the services offered by HPS to SFV Services and the fact that (as she saw it) HPS was offered as a reaction to the competition of the Post Office. As to the latter point, we considered that this was not the only purpose - see paragraph 287 above. In any event, Dr Jenkins took note of some of HPS's bespoke features and that it was addressed to only one segment of BT's customers. Overall, she did not consider it to be particularly informative for testing whether BT's pricing was unfair.
1295. At trial, the CR's position was that HPS was positively inappropriate as a comparator, because it was itself excessive. Here, Mr Parker calculated a costs benchmark for HPS and said that the HPS pricing exceeded it by between 42% and 56%. Of course, those figures are based on Mr Parker's

conception of a competitive benchmark. Perhaps the better point is that on Dr Jenkins' figures, the SFV Services prices were around 11% above those of HPS. However, that would not, in our view, point to BT's pricing being unfair. To reiterate, merely because the price of a comparable product is cheaper does not itself show that the price in question is abusive.

### **BT's Business Tariff**

1296. This was the final comparator relied upon by BT. We have considered this separately in the context of quantum, and concluded it was not an appropriate comparator for the purpose of unfairness. See paragraphs 1324-1330 below.

### **Conclusion on unfairness by Comparison**

1297. It follows from what we have said above that we do not conclude that BT's pricing was unfair by comparison, either.

1298. That then leaves the CR's case on unfairness by reference to line rental prices alone. This was barely pressed in the course of the trial although Ms Kreisberger KC did not formally abandon it. Accordingly, we deal with it below.

### **ALTERNATIVE CASE BASED ON LINE RENTAL PRICE ONLY**

1299. In our judgment, a claim put in this way is bound to fail. This is because, on any view, it is not sensible to consider the question of line rental divorced from the elements of prices for SFV Services. Hence both sides accepted that the correct measure of price was ARPU. It is correct that in its 2017 Provisional Conclusions, Ofcom focussed on line rental. However, even if this made sense for Ofcom's purpose, it does not for ours. Accordingly, any alternative claim based on the pricing of line rental alone fails.

### **OVERALL CONCLUSION ON LIABILITY**

1300. It follows that the CR's claim as a whole must be dismissed. This makes it strictly unnecessary to deal with any further aspects of this case. However, because they have all been argued and lest this case go further, we propose to deal briefly with the following further matters:

- (1) The overall approach to quantum, the correct "excess" to apply and the Counterfactual;
- (2) The position of Business Customers;
- (3) The position of Class Members who were given free elements of their service.
- (4) Removal from the Class of those members who died without a personal representative;
- (5) Compound Interest;
- (6) Damages in respect of Inflation; and
- (7) The rate of any simple interest.

1301. What we will not address is the argument that even if successful on liability, the Class Members failed to mitigate their loss. This is because an analysis of this partial defence would have to be based upon the facts found which led to a finding of unfairness. But as we did not find unfairness, we cannot meaningfully discuss a defence which can only be raised if we had done so. It would involve us assuming too many factual matters. Therefore, failure to mitigate will not be dealt with. Accordingly we turn to the other quantum issues noted above.

### **QUANTUM (1): BASIS OF OVERCHARGE**

1302. Had we found that BT's prices were unfair, the CR would have invited us to take as the relevant loss per customer, the difference between the price (i.e. ARPU) for any given month, less the competitive benchmark.
1303. However, BT contends that this would overcompensate Class Members because, in any counterfactual which would require BT to have charged lawful and not unlawful prices, a lawful price would be any price which did not amount to a significant excess above the competitive benchmark. It should not be assumed that BT would have confined itself, in the counterfactual, to a price no more than the competitive benchmark itself.
1304. At first blush, there would appear to be force in BT's point. After all, there will be a margin for pricing above the competitive benchmark before it qualifies as a significant and persistent excess above it. Why should the undertaking found to have engaged in abusive pricing not be assumed to have set prices at the maximum it could do, before they would be rendered excessive under Limb 1?
1305. However, there are two obstacles to such an approach. First, in *Albion Water Limited v Dŵr Cymru Cyfyngedig* ("Albion Water III") [2013] CAT 6, which dealt with the quantification of damages on a follow-on basis, the Tribunal had to grapple with this very point. There, the previous Tribunal held that a price of 14.4p/m<sup>3</sup> would not have been an infringing price. This figure was itself the average of 3 different competitive benchmarks, being 15.8p/m<sup>3</sup>, 13.8p/m<sup>3</sup> and 13.6p/m<sup>3</sup>. On the evidence, the Tribunal found that the Defendant ("Dŵr Cymru") would have offered that price in the counterfactual.
1306. However, Dŵr Cymru submitted that the starting point of the assessment of damages should not be 14.4p/m<sup>3</sup>, but rather the highest of the 3 benchmarks i.e. 15.8p/m<sup>3</sup>, which, by definition, would not be infringing, and then an increase of 5% above it. This was to give effect to the argument that a price of 5% above the competitive benchmark would not be material (so could not be significant) and therefore would not have failed the Limb 1 test, as it were.

1307. It should be noted that Dŵr Cymru did not take the point there to its “logical conclusion” as the Tribunal put it. This is because, on that argument, there could have been a price which was more than 5% above the competitive benchmark, while less than the actual price under scrutiny, which would also not have been ultimately considered unfair, depending upon what factors were taken into account in the Limb 2 analysis.

1308. The Tribunal rejected Dŵr Cymru’s argument. First, it said that attempting to design the claimed counterfactual price would be extremely difficult if not impossible:

“69. We reject Dŵr Cymru’s submissions on this point as wrong in principle, as well as entirely impracticable. It will be very rare that an infringement decision, whether adopted by a domestic competition authority or by the European Commission, or indeed on appeal as in Case 1046, will determine the precise borderline between lawful and unlawful conduct. If Dŵr Cymru is right that the claimant in a follow-on damages claim will have to show precisely where that line should be drawn, that will often involve the court in re-doing much of the work done in the earlier infringement decision. Further, it is a task that is almost impossible to accomplish, as is demonstrated in this case. If 16.5p/m<sup>3</sup> is not abusive (a point we do not decide), what about 16.6p/m<sup>3</sup> or 16.7p/m<sup>3</sup>, or 16.8p/m<sup>3</sup>? We do not see how a claimant could prove that one rather than the other is the tipping point between lawful and unlawful conduct. Dŵr Cymru has recognised the impracticability of the test by making the two tactical concessions that we have described. The fact that the Tribunal’s task would be impossible in the absence of those concessions (which Dŵr Cymru was not of course obliged to make) indicates to us that the test proposed cannot be the right one.”

1309. The Tribunal then said that Dŵr Cymru’s position was wrong in principle, referring to what Lord Hoffmann had said in *Banque Bruxelles v Eagle Star* [1997] A.C. 191 at p.221, where the House of Lords considered the issue of counterfactuals in respect of a negligent valuation. Lord Hoffmann held that, if the figure put forward by the valuer is found to be wrong, the correct figure for the purposes of calculating the loss caused is the average one which a non-negligent valuation would have produced, and not the highest valuation which would not have been negligent. The Tribunal considered that the same approach applied by analogy to the position of Dŵr Cymru. The assessment of damages, therefore, used the price of 14.4p/m<sup>3</sup> as being the reasonable price which would have been offered in the counterfactual.

1310. Given what was said in *Albion Water III*, we do not think that it would have been open to us to accept BT’s arguments here.

1311. In fact, there is a further difficulty in our case, as the CR points out. This is that BT did not adduce any evidence as to what, in fact, it would have done in the putative counterfactual arising out of any finding of abuse. In a way, that is understandable, since BT’s position was that Limb 1 would never have been reached and even if it had been, its prices were neither excessive nor unfair. It is simply not possible, absent such evidence, for a Tribunal to make any assumptions as to what BT would have done. There are, of course, cases where the question of a counterfactual, in the context of causation and loss, is not dealt with until after a trial on liability has been concluded, so that it can be assessed in the context of the particular findings already made. But that is not this case.

1312. We should add, since it is a point made by BT, that if the real issue was the taking into account of factors such as price dispersion (see paragraph 855 of its Closing), these are matters for Limb 2, not quantum.

1313. Accordingly, had it been relevant, we would not have acceded to BT's overcharge point here.

## **QUANTUM (2): BUSINESS CUSTOMERS**

### **Introduction**

1314. There are three live issues on quantum which relate to members of the Class who were business customers, although taking residential SFV Services ("Business Customers") as opposed to those taking BT's Business tariff who do not form part of the Class anyway.

1315. These three issues are:

- (1) Should Business Customers be excluded from the Class altogether, so that the overall damages awarded would be reduced by the proportion of the Class represented by such customers ("the Exclusion Issue");
- (2) What proportion of the Class is made up of Business Customers? This question needs to be answered, not only if the Exclusion Issue is determined in favour of BT, but also because it is common ground that damages should be reduced by the amount of VAT which could be reclaimed by Business Customers. While the proportion of Business Customers who were VAT registered has been agreed at 24.3%, the overall proportion of Business Customers within the Class has not; this second issue is also relevant to the Pass-On Issue below; we refer to this as "the Proportion Issue";
- (3) Should there be any reduction in damages for Pass-On of charges paid by Business Customers (if not otherwise excluded altogether)? We refer to this as the "Pass-On Issue";

### **The Exclusion Issue**

1316. As foreshadowed in its Re-Amended Defence dated 27 July 2023, BT argued that Business Customers should be excluded from the Class. This is because BT's SFV Services were only for household personal use, not for trade, business or professional use, and this was clearly stated in its terms and conditions. In particular, BT relied on clause 6 (a) of the applicable BT Consumer terms as follows:

"Each service is just for you and your household for personal use (meaning that it should not be used for any trade, business or profession). You're responsible for how each service and the loaned equipment are used."

1317. As the CR pointed out in his Re-Amended Reply of 8 September 2023, BT had not made this particular objection at the certification hearing (as opposed to then raising a question about pass-on), nor had it sought to amend the Class at any stage earlier than the Re-Amended Defence. For



those reasons, the CR submitted to us that, for BT to take the point as late as it did amounted to an abuse of process and we should simply disregard it.

1318. We disagree. Notwithstanding the particular features of the certification of collective actions, including the important exercise of defining precisely the Class, the point now taken by BT amounts, in our view, to a late amendment. As it happens, the CR did not in fact oppose this particular amendment when it was made. Whether the point now taken by BT should be entertained is essentially a question of where the balance of justice lies.
1319. The point was raised some 6 months before trial and on analysis, it is a short point. The concomitant question of assessing the proportion of the Class that were Business Customers, has to be dealt with in any event, as noted above. Nor did the CR say that it was not able to deal with the substance of the point. Accordingly, we would reject the abuse of process argument and turn to the substance of the point.
1320. Any individual was entitled to purchase residential SFV Services for personal use. However, the question of entitlement also depended on the capacity in which, and purpose for which, the service was used. Occasional business calls from residential lines did not affect the purpose for which a residential line had been taken, but where businesses took residential lines for business purposes, BT says that they should be taking the BT Business tariff. There was therefore no basis for saying that these Business Customers were entitled to BT's SFV Services and thus they should not be entitled to damages in respect of their unfair pricing.
1321. Another way of putting the same point was to say that for Business Customers, the CR had failed to explain why BT's prices for services used by them would be excessive or unfair in circumstances where the services were sold only for their household use. Business Customers using those residential services paid less than they would have paid if they had purchased BT's Business tariff. Hence those customers had suffered no loss.
1322. In that context, from the evidence before us, it was unclear whether BT had in fact ever taken issue with customers using residential SFV Services for business purposes. The evidence did, though, suggest that business usage of SFV Services was well known to Ofcom and so BT was knowingly receiving revenue from Business Customers using residential SFV Services for many years. It is true that BT had written to Class Members who were operating businesses and using SFV Services at the time of the Commitments, but that was only for the purpose of eligibility for the discount, rather than pursuing any potential breach of contract. Thus, it was not clear to us exactly how an alleged breach of an unenforced contractual term, in itself, provided a defence to a claim to abuse of dominance in circumstances known to the dominant company and from which the dominant company has benefited.

1323. We also accept that there was no economic rationale for the exclusion of this group. Business Customers did pay for BT SFV Services. Also, many were micro-businesses or sole traders working from home and using BT SFV Services for both business and residential purposes, and BT's Business tariffs included services not required by these business users. We note the point made by BT that, if Business Customers had taken the correct service i.e. the BT Business Tariffs, they could have no claim. It is then said that it could not be unfair to them if they were deprived of their claim when taking the wrong product. That is all very well, but it is answered by the point that BT was aware of this phenomenon and chose to do nothing about it. Indeed, it did nothing about it, even though it made its own attempts to identify who the Business Customers were, for the purpose of eligibility for the discounted Commitments price.
1324. However, there was a more specific point about unfairness made by BT. This was to the effect that if one considered Business Customers as a sub-set of the Class, there was no unfairness by comparison. That is because the appropriate comparator for them would be BT's Business Plan, which, in broad terms, tended to be more expensive than the SFV Service which they were in fact using. In our Limb 2 analysis, we did not consider this point in the context of unfairness by comparison, but indicated that we would deal with it here.
1325. In the context of market definition, both experts agreed that the BT Business Plan services were in a different market. Thus, for example, at paragraph 4.36 of HJ1, Dr Jenkins said that the reason for treating those services differently included different pricing structures, product features and characteristics and the target audience for those services. See also paragraph 4.55 of DP3.
1326. However, at paragraph 6.89 of HJ2, Dr Jenkins said that for Business Customers, the obvious and logical comparators were products that were in fact designed for business customers. She considered that when the residential and business tariffs were combined in each case with an unlimited call pack option, they were sufficiently comparable. However, the monthly cost of line rental and unlimited calls was higher for the business tariff than for SFV Services. See Figure 6.1 under paragraph 6.94 of HJ2.
1327. Mr Parker disagreed that BT's business tariff was an appropriate comparator. In particular, one needed to consider some specific features of quality considerations. He summed these up at A6b in Annex A to the JES. As a starting point, and as recognised by Dr Jenkins, the unlimited call pack for BT Business included calls to all UK landlines and mobiles, whereas for the domestic tariff calls to mobiles were not included; instead, there was an allowance of minutes for calls to BT mobiles and a discounted price for calls to non-BT mobiles. Further, purchasers of BT Business plans could include additional features such as call barring and three-way calling and options for upgrades to targeted fault fix times. Further detailed differences are set out at paragraph 10.35 (a) – (f). These

include the free provision of 1571 voicemail for the Business plan, whereas it was chargeable on the residential tariff. Business plans also included a 24/7/365 support service. Certain business lines were also compatible with a phone system (involving multiple and interconnecting lines used for call handling, conference calling etc) which was not the case for residential lines. Finally, there were additional voice services available to BT Business customers which were not available to residential customers.

1328. In evidence, Mr Parker referred to lower call prices and some of the additional features such as assurances, quality of service, better fault repair, billing and call waiting for the Business plans. He maintained that the two tariffs were simply too different to provide a useful comparison.
1329. As for Dr Jenkins, she accepted that they were not perfect comparators and that she had not priced in better fault fix times and things which were not available to a residential customer. However, she saw the tariff essentially as “swings and roundabouts” so that residential customers would be no worse off than if they took the business tariff.
1330. We see that, but in our view, we think there are simply too many differences between the products to allow the BT Business tariff to act as an appropriate comparator for Business Customers on the question of unfairness. As a result, pricing for this sub-group within the Class would not be rendered fair in a context where unfairness generally had already been established by reason of the first element of Limb 2.
1331. For all the above reasons we would not have accepted that Business Customers should be excluded from the Class.

### **The Proportion Issue**

1332. There is a significant difference between the parties over the proportion of the Class represented by Business Customers. Thus for BT, Dr Jenkins provides proportions for each of the claim years which are between 14.1% and 28.6%; see Table A11.8 in Annex 11 2 HJ1. These figures are extrapolated from Ofcom surveys of SMEs undertaken in 2016 and 2018 which were designed to understand the communications purchasing behaviour of SMEs in the UK.
1333. On the other hand, Mr Parker for the CR says the figure should be 10.4% across the board. This figure is the average of two other figures. The first is 4%, taken from a number of internal BT documents. The second is 17%, taken from Ofcom’s 2016 survey.
1334. We comment first on the BT internal documents relied upon by Mr Parker. As an example, there is the BT Consumer Pricing document dated 27 April 2016. This states that out of a total of 2.6m SFV customers, 100,000 are to be treated as business customers. That would yield a proportion of 3.85%

as being Business Customers, which Mr Parker has rounded up to 4%. However, at least from the face of the document itself, the methodology used to calculate the 100,000 figure is unclear. Mr Parker did point to an email from Ms Cheek dated 4 May 2016 which said as follows:

“A mixture of data sources was used to arrive at the numbers that John presented to Sharon last week. 2.6m total BT Line Only Customers came from our BT Consumer customer database, as did the 520k on BT Basic, Line Rental Saver or Home Phone Saver. The 1.2m of those who have BB with another CP has been estimated from publicly-available competitor reports, analyst sources and some extrapolation. Income and age data came from Acxiom data matched to our BT Consumer customer database. The figure of 0.1m for second lines/businesses was sourced from our BT Consumer customer database. This was an aggregated count of customers with multiple voice assets on the same billing account, those receiving multiple bills at the same address, those receiving J type bills relating to VAT receipt request, and those with a name and address match to customers with business descriptions on their billing address e.g. & son & partner associates etc. All counts were de-duped for overlaps between the cohorts.”

1335. That gives some information, but it was not a document put to Ms Cheek in cross-examination. Further, it is clear from the way the figures are set out that the 100,000 figure could only relate to VOCs and not SPCs. So its usefulness is limited.
1336. Mr Parker himself accepted that such internal documents could not be entirely reliable, which is why he considered the 17% figure drawn from Ofcom’s 2016 survey. He felt that this could not be correct itself because this was a market-wide survey as opposed to one directed at BT customers only. There may have been a lower (or higher) proportion of BT customers who were Business Customers than would be the case for telecoms customers overall. This is why Mr Parker chose a midway point between the 4% and this 17% figure.
1337. By the time of DP4, Mr Parker had identified further relevant BT documents. One, from March 2018, indicated that 190,000 customers would be sent a coupon to opt-into the Commitments discount. They were told that they would only be eligible if (a) they had no broadband at all and (b) did not use their residential line for business purposes. They had been identified by BT as potentially Business Customers. On the basis of 2.1m SFV customers, this would suggest a proportion of 9%. On the other hand, later documents in 2019 and 2021 suggested that 1% of the SFV customers had multiple lines which was taken as a sign that they were business customers. Mr Parker also pointed out that the internal documents suggested that the proportion of Business Customers was decreasing over the claim period. He contrasted this with Dr Jenkins’ figures which suggested the opposite. In the light of that, and the fact that some of Dr Jenkins’ assumptions in extrapolating the figures from the Ofcom surveys were questionable, Mr Parker maintained that his 10.4% figure continues to be a reasonable one and indeed is probably an overestimate.
1338. On the other hand, BT points to significant deficiencies in the internal documents, for present purposes. This was explained by Mr Bunt at paragraphs 23-29 of JB1 on which he was not challenged. He explained that only VOCs were eligible for the discount and within them, any who used their landlines for business purposes were ineligible. However it was very difficult for BT to

identify such customers. It could only be done by running manual checks against Companies House records which would pick up business customers who were not registered for VAT. That is why the coupons sent to potentially eligible VOCs to a large extent trusted them when they said they were eligible.

1339. Further, most of the documents relied upon by Mr Parker were concerned with the proportion of VOCs who were Business Customers, and therefore the proportion of SPCs who were Business Customers would not be captured. In addition, insofar as BT focused on customers who had multiple lines, that was likely to lead to a large underestimate of true Business Customers as Mr Parker accepted in cross-examination.
1340. As for the Ofcom surveys, the 2016 survey sampled 1,501 SMEs based on a list of small and medium-sized enterprises from Dun & Bradstreet. The 2022 survey was based on a similar methodology for 2,109 SMEs. One of the questions asked in the surveys was whether the SME concerned purchased a residential landline. Using the responses to this and other questions, Dr Jenkins extrapolated the proportion of SMEs in the UK that used residential lines. She then estimated the total number of SFV customers in the UK and then the ratio of SMEs to residential SFV lines. Finally, she estimated the number of residential lines purchased by SMEs. All of this is set out at Annex 11C to HJ1. Mr Parker accepts that the surveys were in themselves valid data points.
1341. However, he questioned whether the preferences of SMEs across the whole telecoms market in the UK could be assumed to be the same for SMEs who were BT customers. We understand the point, but do not see why this assumption should not be made. The CR refers to the fact that in evidence, Dr Jenkins said that this assumption might be incorrect. But what she said in context was this:
- “But I disagree with Mr Parker’s view that those assumptions are problematic or increase uncertainty. I think all of the steps are reasonable. I am just using things like —the main assumption I have to make is that BT is similar to the whole market. That is the main assumption. That may be somewhat incorrect. However, I think it is the CR’s case that there are very few other split purchase suppliers other than BT. So, you know, overall I do not think this is an overly aggressive set of assumptions or likely to be unrealistic or make these estimates unreliable in any way.”
1342. Second, Mr Parker considered that these surveys might pick up customers who only made business calls from their home landlines very occasionally and who would not be regarded as Business Customers for our purposes. The surveys could therefore produce an overestimate. That is theoretically possible, but the surveys were themselves directed (and directed only) to SMEs which had to answer questions about their use of residential landlines. Also, if working from home was captured, it was likely to be so because the home was given as the SME’s registered address. Further, those surveyed were asked to state the SME’s primary place of business and to exclude homeworking if it was not the primary place of business. But if their home was their primary place

of business it is very hard to see why there would only be the occasional business call made from there.

1343. Broadly, we consider that the data relied upon by Dr Jenkins is much more persuasive than the BT internal documents referred to by Mr Parker. Since we can see no sensible objection to Dr Jenkins' exercise of extrapolating figures from the surveys, there is no real basis for simply choosing a half-way house of 10.4%. Indeed, we see no basis here for making any material reduction in Dr Jenkins' figures as this would be arbitrary. Accordingly, the percentages of the Class which should be treated as consisting of Business Customers are those set out in Table A11.8 in Annex 11 to HJ1.

### **The Pass-On Issue**

1344. BT contends that Business Customers would be expected to maintain their margins in the face of any overcharge, especially because of the prices they paid (for residential SSC BT Business Tariffs). Accordingly, they should be treated as having passed on the additional costs in their entirety.
1345. For her part, Dr Jenkins was less certain. She said that Business Customers may have been able to pass on some of the additional costs, though this could vary across different Business Customers, and she accepted that she could give no estimate of the extent of any pass-on. There was no specific evidence on this matter from BT, although in terms of factual matters, that was true of the CR as well. However, in collective proceedings, one would not expect to see individualised evidence from Class Members.
1346. In any event, Mr Parker did consider the question of pass-on specifically at paragraph 7.63-7.72 of DP3. In short, he did not consider that there would be any material impact from any overcharge on the prices charged by Business Customers; in other words, there was no real likelihood of any-pass on. This was because the Class Members were unaware of the overcharge at the time, the relative amount of the overcharge and the business in question were likely to be small and where other firms in the same market faced no such overcharges, and where there was no evidence of any direct relationship between BT's SFV Services and the products or services whose prices would have been increased due to any pass-on.
1347. We consider that there is real force in all of those points and accordingly we would have made no deduction at all for any possibility of pass-on.

### **QUANTUM (3): BT EMPLOYEES WITH GIFTED SERVICES**

1348. BT argues that a reduction should be made to the Class to remove nominated friends or relatives of BT employees who were in receipt of free gifted services. These were DP bundle customers who, because they received a gift in respect of their broadband component, were treated in BT's systems as split service customers. The net price they paid for the bundle was only the SFV price which was

accounted for in the BT systems accordingly. It was just an accident of the way the billing system worked to treat them as split service customers. However, in reality, they should be treated for present purposes as bundle customers, in which case they would be outwith the Class and/or they had not suffered any unfairness.

1349. As against that, the CR contended that regardless of the gift of broadband, the customers concerned had still paid any landline or calls price component found to be unlawful. BT's choice to offer a broadband price benefit is irrelevant to the high price of the SFV Services – the gift of free broadband would remain in any lawful counterfactual, absent the imposition of excessive SFV prices.

1350. We consider that the CR's analysis is clearly the correct one. In consequence, we see no basis for treating such customers differently from any other Class Members. So had there been unfair pricing, there would have been no reduction in damages on their account.

#### **QUANTUM (4): DECEASED CLASS MEMBERS**

##### **Introduction**

1351. The Class definition includes living Class Members and UK-domiciled personal representatives of Class Members who have, or will have, died before the distribution of any damages award. It is common ground that deceased individuals without a personal representative at the date of distribution are to be excluded from the Class and thus from any award of damages. The actuarial experts had therefore to produce percentage reductions from the aggregate award of damages which reflect that exclusion.

1352. According to Mr Punter, the reduction to be applied is 3.6% for VOCs and 2.3% for SPCs on the basis of an assumed final distribution date of 31 March 2026. For Mr Scott, on the other hand, the reductions are greater, being 13.4% for VOCs and 6.8% for SPCs. His reduction percentages are “translated” from the results of the “decrement” exercise he has performed – see the Table produced under cover of a letter from S & S dated 28 February 2024.

1353. In order to arrive at the final percentages, two issues have to be addressed.

1354. First, the method of calculating the number or rate of Class Members expected to have died by the distribution date (the “Mortality Question”). The differences between the experts have been narrowed here so that there is only one essential question which is the correct methodology to use; this dispute is reflected in Issue 25 in the Actuarial JES.

1355. In that regard, the parties have agreed to accept the mortality assumptions of the expert whose overall methodological approach is preferred by the Tribunal. See paragraph 1 of the Appendix to the letter from S & S dated 7 March 2024 (the “7<sup>th</sup> March Letter”).

1356. The second issue concerns the number or proportion of those deaths where there is no personal representative by that date (the “Personal Representative Question”). It is on this issue where there is most dispute between the experts.
1357. Once these issues are determined, the economic experts can apply them to their quantum calculations. We consider each of these issues below.

### **The Mortality Question**

1358. So far as methodology is concerned, Mr Punter arrives at an overall percentage reduction for each of the VOC and SPC sub-classes. He allows for every Class Member as they join the Class through time, with the putative adjustment for those likely to die without a personal representative stopping only at the point of the assumed distribution date. As he put it in evidence, in relation to Class Members, those who have been with BT for a long time within the claim period would have more substantial losses due to the overcharge than those who were only there for a short time. Because of his methodology, however, Mr Punter treats them equally.
1359. On the other hand, Mr Scott’s methodology is sensitive to the differing periods of time for which Class Members were with BT, in particular to those who were with BT for only a short time. Such “transient” members were generally considerably younger than average, even in relation only to SPCs, as opposed to VOCs who tended to be older. There were, according to Mr Scott, a significant number of such transient members. According to him, if they were simply treated equally with much more long-standing Class Members (as Mr Punter has done) the average age of the class and the mortality rate overall would reduce. This would ultimately affect the size of the percentage reduction to damages. Moreover, the loss suffered by the transient members would obviously be much less than for more long-standing members.
1360. Accordingly, there had to be some method of “weighting” the Class Members to take account of the differential in terms of the period for which they were a customer of BT within the claim period. The way that Mr Scott did this was to produce a set of monthly decrement tables, one for VOCs and one for SPCs. The percentage for each month represented the proportion of the members of the relevant sub-class within the total Class for that particular month, who were likely to be alive, alternatively deceased but with a personal representative, by the assumed date of distribution. What this meant was that Class Members who were such for only a brief period of time would not “count” to the same extent as those who were more long-standing Class Members. This “weighting” was achieved by the monthly decrement exercise, since in any given month, those who had already left, by definition, would not be counted. For these purposes, a “transient” Class Member was defined by Mr Scott as a customer who joined and left BT within one year.



1361. In this way, Mr Scott's exercise would take account of the fact that the effect on any award of aggregated damages would be much less for a transient Class Member than others. Equally, the mortality rate overall would be less because the putatively younger age of transient members would have less effect on the average.
1362. Mr Scott said that his methodology would avoid a significantly lower mortality rate. He said that over a one-year period, using a non-rated methodology would result in a lower mortality rate for the Class as a whole than the average mortality rate at any point during the year.
1363. Mr Scott demonstrated this in the hot tub discussion, by referring to the spreadsheet supplied under cover of the letter from S & S dated 28 February 2024. The basic point was that if there were 12 different transient members for each month during a given year, they would "count" for the purposes of working out the mortality rate much more than if there was assumed to be simply one transient member across the whole year.
1364. In the hot tub discussion, Mr Punter recognised that a calculation of this kind could be done if it was required, although he did not produce a competing one, as it were, himself. Nonetheless, the CR made a number of objections to Mr Scott's methodology.
1365. First, Mr Punter noted that the majority (70%) of Class Members were members at the start of the claim period or had joined by the end of 2015, and that over 95% of the Class had joined it by the end of 2020. He thought that the results concerning the Class would largely be driven by those joining at the start and, therefore, the impact of later (transient) joiners would be relatively slight. There is not much in this point because if Mr Scott's methodology was justified in principle, the fact that it might not make much difference is not an argument against it, and in any event, Mr Punter thought that it did.
1366. Second, the CR also criticised the approach taken by Mr Scott as encroaching on the Tribunal's role in distributing damages by an approach which was: "effectively weighted for Class Member loss", rather than confining himself to assisting "in calculating the size of the Class". BT disputed that Mr Scott's calculation amounted to any pre-judgment of the Tribunal's decision on loss and entitlement calculations. His work was based on the number of lines (as he confirmed in the hot tub on Day 20/173), if the Tribunal were to award aggregate damages, not a view as to the loss any Class Member may or may not have incurred, so there is no inappropriate pre-judgment of the Tribunal's assessment of loss. We agree with Mr Scott here.
1367. Third, the CR suggested that Mr Scott's calculations would somehow exclude transient Class Members who joined and left within a given calendar year. This was on the basis that Mr Scott's calculations involved taking snapshots at each 1 January, so that a Class Member who, for example,

came in in February and left in December would not count at all. However, Mr Scott explained that his age distribution did take into account their existence and characteristics across the relevant year, so that looking at the picture in January there would be, for example, one Member and one transient Member, and the same would apply the following year even though the identity of the transient Member would have changed. He explained all of this carefully on Day 20/128-131.

1368. Finally, the CR says that Mr Scott's methodology relies upon a number of assumptions which risk unsafe conclusions. For example, there were assumptions made as to age distributions and movements of transient Members. However, the basis for the assumptions was explained by Mr Scott in the hot tub on Day 20/124-5 and overall, our conclusion from the written evidence, argument and the discussion in the hot tub is that the assumptions were appropriate for the task in hand.

1369. For all those reasons, we would have approved Mr Scott's methodology for application in accordance with the agreement set out in the 7<sup>th</sup> March Letter.

## **The Personal Representative Question**

### *Introduction*

1370. The legal definition of a personal representative for these purposes is now agreed. There are four situations in which a deceased person will have a personal representative in place so that their estate is to be included in the Class for that purpose. They are as follows: where the deceased person:

- (1) had a will, with a named executor(s) to whom a grant of probate is made;
- (2) had a will, with a named executor(s) but these declined to act and, instead, letters of administration are awarded to an administrator (usually a close relative);
- (3) had a will, with a named executor(s) but no grant of representation (as in sub-paragraph (1) or (2) above) is made. In this situation, although the estate does not 'go through probate' a personal representative is in place. This occurs in roughly half of all deaths, as in many situations no such grant of representation is required;
- (4) had no will (died intestate) but nonetheless letters of administration are granted to a personal representative.

1371. In short, the experts thus agreed that it was necessary to determine the rates of Class Members dying:  
(i) with a (valid) will identifying an executor ("Category 1") and (ii) with no (valid) will, but an administrator appointed by letters of administration ("Category 2").

1372. The most significant difference between the experts in terms of their results here was attributable to the different ways in which they had applied the shared definition of "personal representative" to

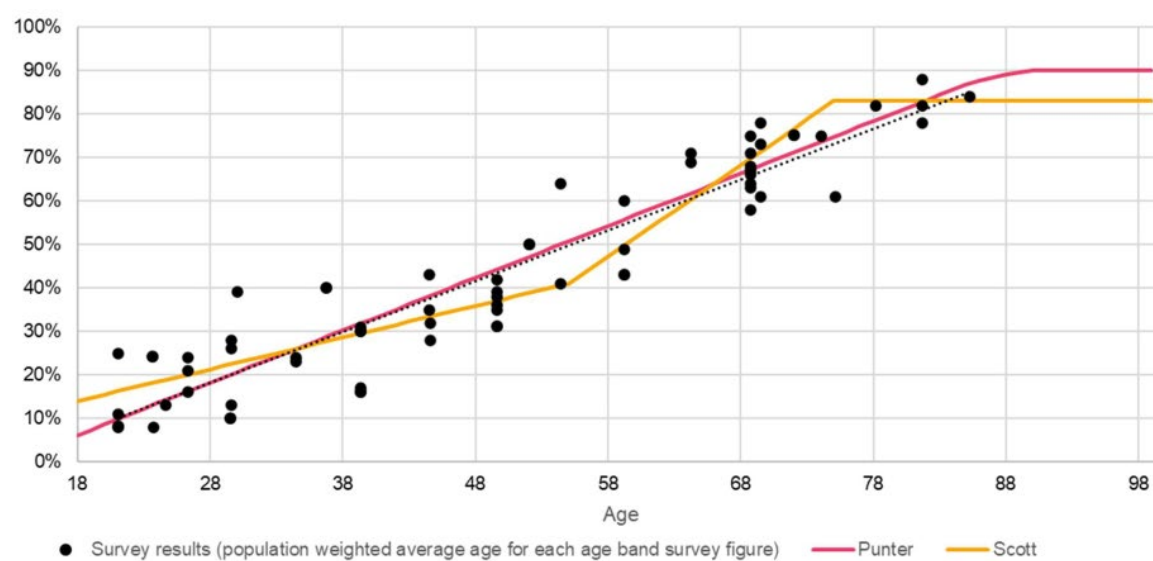
determining the rates of Class Members who will have died at the assumed date of distribution, without a personal representative.

1373. In relation to Category 2, Mr Punter (at paragraph 51 of the Actuarial JES) observed that the differences between the experts, in relation to the assumptions they adopted, did not produce a material difference in the results. The 7 March Letter thus records the agreement between the parties on how members of the Class who had intestate letters of administration should be dealt with.
1374. As a result, the parties agreed that there is now only the Category 1 issue to be dealt with, in other words, the likelihood of a deceased Class Member having an executor. This in turn depends on rates of will-writing. Once determined, the rate of will-writing will affect the calculations regarding Category 1.
1375. Here, Mr Punter produces a higher rate of will writing than Mr Scott. The only available evidence on this subject is a limited set of 17 surveys and studies undertaken between 2005-2023, there being no official statistics. The difference between the experts lies in their assessments of that data.
1376. There is a further difference because Mr Scott then makes a 20% reduction to the rates of will-writing that he derives from survey evidence. The CR regards any adjustment as unjustified on the evidence and points out that some factors may point towards the need for an upwards adjustment.

#### *Rate of will-writing*

1377. The difference between the experts' conclusions on the rate of will-writing can be seen from Figure 39.1 under Row 39 of the Actuarial JES:

**Figure 39.1 Assumed will likelihood by age (before adjustment for any of the factors in proposition 43)**



1378. Mr Punter's review of the evidence led him to undertake a meta-analysis, based on the available data, as seen at paragraph 4.4.7 of JP1. Consistent with that analysis, he assumed an upward linear relationship between the likelihood of having a will and a person's age up to 85 years, which then slows to reach a plateau of 90% at age 90 and above, accepting that the linear upward trend could not continue without limit. This is shown in the above Figure.
1379. On the other hand, while Mr Scott agreed in principle that the evidence showed a strong positive correlation that the likelihood of having a will increases with age, he assumed a constant likelihood of having a will after the age of 75 years. More particularly, as shown above, he models an upward linear relationship to age 55 years, a more pronounced upward linear relationship between 55 and 75 years, and a plateau at 83% of will writing at age 75 or more. His model is based on key reference points from that survey data showing a prevalence of will writing at 38% across all ages, 66% at ages above 55 and 83% at age 75 or more.
1380. Mr Punter considered that Mr Scott's approach was incorrect. He said that assumption that the upward trend immediately stops at age 75 was not supported. Mr Scott's approach also overstated the level of will writing between the ages 75 on the one hand and the weighted average age of surveys over this age, and understated it thereafter.
1381. Further, Mr Punter said that his percentages for those having wills beyond the age of 75 was supported by survey evidence. In particular, the NCSR and Cardiff University study 2010, the WillSuite 2020 report and the Canada Life survey all showed to varying extents that there were people over the age of 75 who started to think about writing a will for the first time. He also said that the surveys and academic studies also showed that people over the age of 75 had a greater likelihood of having a will. Here he relied upon the NCSR and Cardiff University and Canada Life studies which showed an upward trajectory in will-making over the age of 75 and a higher percentage of those with a will in that 75+ age group, and also the Just Group 2021 study which showed fewer people in the 75+ group having not already arranged a will, compared to younger age groups.
1382. Moreover, Mr Scott's flatline at age of 75 was not actually faithful to the survey evidence. This is because there was no reason or evidence to suppose that all those responding were in fact aged precisely 75. Rather, the age band "75 and over" represents some average age higher than 75. Mr Punter's evidence was that the average age of those within the '75 and over' group would be around 82.
1383. Finally, the Josphe Rowntree Foundation 2005 (JRF 2005) study showed that same upwards trajectory in the rate of will-making and also a higher percentage of those with a will in the 80+ age

group compared to younger age groups. The CR argued that Mr Scott had not taken that study into account in either of his reports, although he was aware of it at the time of the Actuarial JES.

1384. For all those reasons, the CR said that Mr Punter's approach should be preferred.
1385. For his part, Mr Scott said that whilst the prevalence of will writing does increase with age, there was no evidence that it keeps increasing throughout the overall age range. The highest age referenced in the surveys was actually 75, from which Mr Scott took the likelihood of having a valid will to be constant beyond that age. He regarded that as consistent with the Willsuite report which shows virtually no wills are written after age 85.
1386. Further, it was common ground that none of the surveys actually reported a will-writing result as high as 90%, and that only a minority broke down their results for respondents over age 55 years into narrower age bands, such as age 70 or more or age 75 or more. Yet further, the only survey that reported on respondents aged 80+, namely JRF 2005, concluded that 84% of respondents in their eighties had a will. This was close to the 83% plateau modelled by Mr Scott, and the survey anyway cautioned that its figures may overstate reality, being higher than reported in previous research and potentially reflecting some who felt that they ought to have a will and so said they had one when in fact they did not.
1387. Mr Scott added that Mr Punter's calculation of the prevalence of will writing was then applied to the average age in the age band. This might not be valid, because there were small numbers in each age band in the surveys and thus uncertainty about the average age of the people surveyed.
1388. He also said that the criticism of his model, that it flatlines at age 75, making no allowance for new wills written thereafter, was misplaced. The actual proportion of any age group having a will may not be constant. Mr Scott explained that over that age, there will be people making wills, people who had wills who die (reducing the group of age 75+ with wills), some will remarry (revoking their will), some may lose their will or destroy it, for some, their wills will turn out to be invalid, and some will-writing may be re-writing a will that has already been drafted.
1389. In discussion with the Tribunal, Mr Scott confirmed that the survey evidence to which he was being faithful showed the percentages at each age range, and they were the percentages that he mapped into. This mapping was reflected by Mr Scott's curve flattening at the data point for age range 75+.
1390. In summary, there was no good reason to assume that the modelled relationship between age and will writing continues on an upward trend to age 90, nor to assume that 90% of persons at or above that age have a will. Mr Scott's more closely modelled relationship, adhering more to the survey evidence, should be preferred.

1391. Overall, we found the position taken by Mr Scott to be more persuasive. On the evidence, we were not convinced by the assumptions of an upward trend to age 90, and of 90% of persons at or above that age having a will. It is common ground that none of the surveys reported as high a proportion as 90% with wills at any age and the only survey that reports on those aged 80 or more concluded that 84% of respondents had a will. We consider that Mr Scott's average of the surveys in respect of those aged 75 or more, which comes out at 83%, is, on the balance of the evidence, to be preferred. We think that his approach more particularly responded to such data points as could be derived from the surveys and reports on which both experts had to rely.

1392. Accordingly, on this first point, Mr Scott's analysis of the rate of will-writing should be used.

*The 20% adjustment*

1393. Mr Scott reduces his rates of will-writing derived from credible survey evidence by 20%. He does so for a number of reasons.

1394. First, he argued that that there was survey bias, in that people who responded to a survey by saying they had a will may, in fact, not have had a will, but did not want to admit that. However, this supposed bias was not supported by evidence, and considering there were 17 different studies/surveys over two decades without such adjustment, there is no reason to doubt their design. The surveys were carried out by professional firms or academics, well-versed in bias issues and how to structure their surveys to avoid bias. None of them suggest adjusting base results up or down for any purpose. Some of the surveys anyway used neutral, factual questions to avoid possible bias and since they show the majority of respondents across all ages saying they do not have a will, no social desirability or acquiescence bias is evident, and a significant proportion of these studies were online 'self-response' studies, so there was no questioner to 'please'. As to that, Mr Scott responded that many of the surveys did not contain sufficient information to allow the presence of such issues to be ascertained, and Mr Punter was taking it on trust that any bias issues will already have been adequately addressed.

1395. Second, it was suggested that will invalidity should be adjusted for. Most wills are, however, written with professional help. There was also no or little evidence that most or all of home-made wills were invalid, and the requirements for validity are long-established, obvious and straightforward. Furthermore, the Probate Office reported very few wills presented for probate as being (ultimately) invalid. While a significant number were poor quality, and required further work, they would be made valid. As to that, Mr Scott said that there was no quantitative assessment of "very few", nor of whether the Probate Office would see all invalid wills in any event.

1396. There was evidence from the 2011 Legal Services Consumer Panel that about 8% of wills were not validly executed, but that was based only on a sample size of 100 interviews. On the other hand, it

was not suggested that the number of wills invalid from the outset or becoming invalid could be zero. While Mr Punter said that any such risk was immaterial (pointing to the fact that will-writing tended to occur at older ages, when events that give rise to invalidity, such as marriage, have already taken place) this ignored wills invalidly executed in the first place and was anyway an over-generalisation, according to Mr Scott.

1397. Third, Mr Scott also argues that a downward adjustment is required because a will may not have been updated following marriage or civil partnership. However, since marriage typically occurs at lower ages, whilst will writing typically occurs in older age groups, this is likely to be immaterial. Moreover, marriage is often a prompt to will writing (as at least one of the studies observed) and there is no other evidence adduced to suggest a large number of such revocations, or that revoked wills are not replaced by valid wills. Finally, the revocation rule is not an absolute rule: wills written in contemplation of marriage or civil partnership are unaffected.
1398. Mr Scott then justified a downward adjustment on the basis that a will may have been revoked or destroyed. He accepted, however, that he had no evidence that will destruction was a common occurrence.
1399. He then said that the surveys, some of which were conducted online, and which reported results for those aged '75 and over', were not actually representative. He added that in fact he could arguably have made a considerably higher adjustment than 20% because 48% of deaths were likely to be intestate, placing reliance on a Law Commission comment. However, the Law Commission itself said it was not possible to know whether or not there was a will. Moreover, an estate does not need to go through probate for a personal representative to be in place and also, the Commission was looking at deaths at all ages, not just with deaths at older ages as are relevant to the case.
1400. Finally, Mr Scott pointed out he had to avoid the risk of double counting between will writing and intestate grants of administration.
1401. Having regard to all of those supposed justifications for the 20% adjustment, that figure was not allocated as between the various factors and indeed, as BT's Closing said, the issues and evidence in relation to bias and invalidity simply do not permit of a granular enquiry into every factor. Overall, Mr Scott was using his expert judgment in the round, taking into account all the relevant sources to reach a 20% reduction.
1402. We follow these general points of concern, although we have already pointed out their shortcomings in particular instances. Added to that is their general nature and the lack of clear evidence of their specific impact on the Class with which we are concerned. Overall, we do not accept that there

should be the claimed 20% adjustment. Nor is there a basis for selecting some other, lower, percentage adjustment.

1403. Accordingly, we would have found in favour of the CR on this second issue.

## **QUANTUM (5): INTEREST AND RELATED MATTERS**

### **Introduction**

1404. There are 3 issues relating to interest and other matters which we would have to have determined had we made an award for damages. Consistent with our approach in dealing with quantum issues anyway, we will still deal with these further matters, albeit in short order.

1405. The 3 issues are:

- (1) Inflation;
- (2) Compound interest;
- (3) Simple interest.

### **Inflation**

1406. The CR postulates that, had the Class Members not been overcharged, they would have more money than otherwise at the time. In relation to that extra money, they would either have saved it or they would have spent it. Mr Parker has used Class Members' marginal propensity to consume ("MPC") to conclude that of the extra money in any given month, 38% of it would have been spent and the balance of 62% would have been saved.

1407. As for the money spent, the CR contends that the appropriate way to compensate Class Members for not having had the use of that extra money at the time of their notional spending, is not by an award of interest. Rather it is to compensate them on the basis that it would now cost significantly more to purchase the goods or services that they otherwise would have purchased in the claim period because of inflation. Such compensation would be achieved by uprating the relevant portion of damages for inflation by use of the CPI Index.

1408. The principal question here, in our view, is whether such a claim to compensate for inflation is permissible as a matter of law at all, in this context. There is no authority to suggest that it is.

1409. Thus, for example, the *Judicial College Guidelines for the Assessment of General Damages in Personal Injury Cases* regularly revises its suggested awards to take account of the changes in the value of sterling. Equally, where the issue relates to damages to compensate the claimant in a personal injury or clinical negligence case for future loss in respect of expenses yet to be incurred, the Court will consider the likely costs as at the date of the judgment rather than the date of the underlying breach of duty. The case before us is quite different from those examples.



1410. Nonetheless, the CR prays in aid the general principle of “full compensation”. However, that simply describes the requirement that the successful claimant should be put in the same position they would have been in had the tort or breach of contract not occurred. It is not a mandate for uprating damages for inflation.

1411. The CR also relies upon what was said by the Tribunal in *Merricks v MasterCard* [2021] CAT 28 (“*Merricks Remittal*”). The context here was whether the Tribunal was in a position to award compound interest on an aggregate basis which arose for consideration on the application for a CPO. At paragraph 87, the Tribunal, following the decision of the Supreme Court in *Sempre Metals v IRC* [2008] 1 AC 561 noted as follows:

“We therefore do not accept as an accurate reflection of the legal position the submission of Ms Demetriou that compound interest is “parasitic” on primary loss. That is correct only in that if there is no primary loss, then there can be no claim for compound interest. But under the *Sempre Metals* principle, compound interest constitutes a distinct head of loss, which must be separately established and cannot be presumed. In that regard, it is fundamentally different from the award of simple interest under statute.”

1412. The Tribunal then considered if there was a sufficient basis for it to be able to award compound interest in the collective proceedings if it decided to award damages. It considered that there were different ways of calculating compound interest on an aggregate basis. So, for example, it stated at paragraph 92:

“The problem with both approaches is not any limitation on the data that might be available. As the SC Judgment made clear, that is not a basis for denying certification: the Tribunal has to do its best with the data that is available. But the first approach is based on the assumption that anyone who was a saver or a borrower would have used the small amount by which each of their purchases would have been cheaper (i.e. in the absence of the Overcharge) to reduce their borrowings or add to their savings. The second approach rests on the same assumption limited only to borrowers. However, as Ms Demetriou recognised in her oral submissions, the relevant question is: “if [the class members] hadn’t suffered the overcharge, what would they have done with the additional money that they would have received?” Both the above approaches assume the answer to this question and fail to take account of the need to show, as a matter of probability, that the money would not have been used simply for a little extra expenditure. Indeed, if either approach was valid, it would mean that most claims for monetary loss by individuals in the courts would result in an award of compound interest. But that is manifestly not the position.”

1413. The CR refers to the reference to extra expenditure in support of his contention that damages should be uprated by inflation but as the full paragraph shows, all the Tribunal was doing was to point out that, with the putative extra money available to Class Members, it did not follow that they would have saved all of it, as opposed to spending it. So this decision is no support for the CR’s position.

1414. We should add here that in the end, the Tribunal held that any claim for compound interest would be outwith the Collective Proceedings:

“96 In this regard, s.47C(2) which enables the Tribunal to award damages on an aggregate basis and on which Ms Demetriou placed great emphasis, does not assist. If there was a credible or plausible means of estimating the aggregate Overcharge paid each year by the proportion of the class that is likely to be entitled to compound interest on a *Sempre Metals* basis, we do not suggest that each relevant class member would have to establish his or her claim to compound interest on an individual basis.

97 In the SC Judgment, Lord Briggs, for the majority, held that the requirement of suitability of a claim for aggregate damages in r.79(2)(f) is to be interpreted in a relative sense, meaning “suitable for an award of aggregate rather than individual damages”. We consider that in the absence of a credible or plausible method

of estimating what loss by way of compound interest was suffered on an aggregate basis, this head of claim is not suitable for an aggregate award. We have regard to the various factors set out under r.79(2). It is accepted, in the light of the SC Judgment, that the claim for the principal loss is suitable for collective proceedings. But unlike the claim for the Overcharge, we consider that the claim here for loss by way of compound interest cannot be fairly resolved in these collective proceedings. Accordingly, we find that it is not suitable for collective proceedings and should be excluded. The class members will of course remain entitled to seek simple interest under statute.”

1415. For all of those reasons, and as a matter of principle, we would have rejected the claim for damages to be uprated for inflation. What is left, therefore, is an award of interest.

### Compound Interest

1416. As we have already noted, the Tribunal in *Merricks Remittal* was careful to note the restrictions on an award of compound interest as laid down in *Sempra Metals*. There can therefore be no doubt that *Sempra Metals* applies just as much to cases such as that before us as to cases outside the competition arena.

1417. However, the CR maintains that compound interest can be awarded on an aggregate basis here. At paragraph 749 of his Closing, he refers to what the Tribunal said in *Royal Mail v DAF Trucks* [2023] 5 CMLR 6. Here, we would refer to the following important paragraphs of its judgment:

“762 For some reason, lawyers and judges seem particularly averse to compound interest. By contrast, economists have no problem with compound interest as it is what happens in the real world in borrowing and lending arrangements. Both experts seemed to agree that it properly captures what Mr Earwaker described as the “the real-life consequences that Royal Mail would have suffered”. Mr Delamer did not disagree but said that he thought this was a legal issue and therefore was outside of his expertise...

764 Mr Lask, who made submissions on this topic and tax on behalf of the Claimants, referred to the helpful summary of the position by Males J (as he then was) in *Equitas Ltd v Walsham Brothers & Co Ltd* [2013] EWHC 3264 at [123]. This included the following:

“ii) Second unless there is some positive reason to do otherwise, the law will proceed on the basis, at any rate in the commercial context, that a claimant kept out of its money has suffered losses as a result. That represents commercial reality and everyday experience. Specific evidence to that effect is not required and, even if adduced, may well be somewhat hypothetical and thus of little assistance...Accordingly the question in such a case is not whether a loss has been suffered, but how best that loss should be measured.

...

v) If a conventional borrowing cost is to be adopted in this way, the question whether interest should be simple or compound answers itself. While simple interest has the virtue of simplicity as Lord Hope observed, it also has the certainty of error and injustice. As their Lordships noted, it is impossible to borrow commercially on simple interest terms. I respectfully agree with Lord Nicholls that the law must recognise and give effect to this reality if it is to achieve a fair and just outcome when assessing financial loss. To conclude that, at least in a typical commercial case, the normal and conventional measure

of damages for breach of an obligation to remit funds consists of compound interest at a conventional rate is therefore both principled and predictable, as well as being in accordance with what was actually awarded in *Sempra Metals*.”

In the light of those comments it is perhaps surprising that compound interest is not ordered more often and the law still seems to be wedded to simple interest.

767 As to the alleged lack of evidence, Males J’s comments in *Equitas Ltd v Walsham Brothers & Co Ltd* [2013] EWHC 3264 are relevant and in any event the sort of evidence that DAF are demanding would be hypothetical. There is ample evidence before the court and considered by the experts as to what Royal Mail actually did at the time in terms of investment and debt finance. For example, Mr Jeavons referred to Royal Mail having borrowed from the Government at a rate of 12%

768 We have no difficulty in favouring a compound interest calculation over simple interest. This accords with economic reality and there is no legal bar to compounding the appropriate interest rate that we find to be applicable. This is what happens in the real world and it therefore corresponds to Royal Mail's actual losses. If it is appropriate to charge interest on a financial transaction, then it is self-evidently appropriate to apply interest also on any interest that has accrued between one period and another."

1418. Since it is obviously the case that the Tribunal has the power to award compound interest the question is whether it can or should do so here.
1419. In our judgment, the fact that in collective proceedings, damages are to be assessed on an aggregate basis does not mean that there can be claims for compound interest which are not specifically evidenced in some way, as they clearly were in *Royal Mail* and as they clearly were not in *Merricks Remittal*.
1420. That approach is supported by what the Tribunal said in *UK Trucks Claims Ltd v Stellantis and others* [2022] CAT 25, where it approved a CPO on an opt-in basis. Here there was a claim for compound interest by the proposed class members in respect of their acquisition of new vehicles on finance by using a personal contract purchase or a hire purchase agreement. It was proposed to identify the proportion of vehicles purchased using finance rather than cash, and then to obtain information about the average period over which new vehicles were held under the financing arrangement and the average rate of interest for new car finance. This was the evidence in support of an award of compound interest.
1421. Nonetheless, at paragraph 91, the Tribunal said this:
- "Whilst the class in both of the present cases is very significantly smaller than in *Merricks*, the amount referable to each PCM is significantly greater and, as we have observed, the inclusion of compound interest makes a substantial difference in financial terms. Although the factual circumstances of some PCMs may support a claim for compound interest, those of other PCMs may not. In the counterfactual where they were not subject to an overcharge, some PCMs may have used the money they therefore did not have to spend on trucks (i.e. their avoided expenditure) to reduce borrowings (including financing costs of the trucks) and accordingly suffered a loss by way of additional payment of compound interest. But others may have used this money to increase expenditure on other aspects of their business. Accordingly, the fact that the PCMs here are businesses not consumers does not, in our view, mean that they are necessarily entitled to compound interest on the primary damages."
1422. In our case, what Mr Parker did to support the claim for compound interest is set out at paragraph 7.125-7.132 of DP3. Here, he explained why it would be appropriate to award any interest on a compound basis, by reference to the interest payable on typical savings accounts or the interest due on credit cards. At paragraph 7.130 he said that these examples illustrate that compound interest is clearly more reflective of real-world lending and borrowing.
1423. We see all of that, but it is a submission which could be made in virtually any case. However, it does not conform to the strict evidential requirements laid down in *Sempre Metals*. Accordingly, had it been necessary to award interest, it would not have been open to us to do so on a compound basis. We reach that conclusion with no particular enthusiasm, given that, as the Tribunal observed

in *Royal Mail*, to restrict the award of compound interest does not reflect the prominence of compound interest in the real world. Not to compensate consumers here seems anomalous.

### **Calculation of simple interest**

1424. BT proposes that simple interest should be awarded at the rate of 2% above base rate for the relevant periods. This conventional approach, where the claimant is an individual, has been accepted by the Tribunal in other competition cases.
1425. However, the CR proposes a different approach to calculating simple interest. See paragraphs 7.114-7.120 of DP3. What Mr Parker did here was to consider a mix of savings and debt which would apply typically to Class Members. In fact, his approach would apply to anyone, with the qualification that he took into account the age distribution of Class Members. He relied upon data from the ONS' Wealth and Assets Survey which included information on the average distribution of assets and liabilities across various categories of savings and debt for the UK population. He also looked at data available on the average rate of interest incurred on different categories of savings and debt from a range of publicly available sources. He combined this with the estimated distribution of assets and liabilities for an average Class Member across different categories of savings and debt to allow for a weighted-average rate of interest to be calculated. The ultimate rates of interest entailed by this exercise are shown at Table 34 of DP3. The lowest rate was -3.09% in 2018 which was the only year for a negative rate, and otherwise the rate varied between 2.34% and 10.15%. On any view, the total interest which would result would be significantly in excess of an award based on 2% above base.
1426. There was discussion about this approach in the hot tub on Day 22/63-70. A number of valid points were made by Dr Jenkins as to why this approach could be wrong, including assumptions about asset mix, the reality of part-payment of mortgages where the amount of extra money was relatively small, and factors of that kind.
1427. We consider that the better, and much less complex approach is the conventional one under Section 35A of the Senior Courts Act 1981. Accordingly, we would have awarded interest at the rate of 2% above base.

### **OVERALL CONCLUSION**

1428. In the event, and for the reasons given above, this claim must be dismissed. We are extremely grateful to Counsel for their most helpful submissions and assistance throughout the trial, as we are to the parties' legal teams generally.

The Hon. Mr Justice Waksman  
Chair

Eamonn Doran

Derek Ridyard

Charles Dhanowa O.B.E., K.C. (Hon)  
Registrar

Date: 19 December 2024