

UPPER TRIBUNAL (LANDS CHAMBER)



UT Neutral citation number: [2020] UKUT 0013 (LC)

UTLC Case Number: RA/47/2018

TRIBUNALS, COURTS AND ENFORCEMENT ACT 2007

*RATING – valuation – alteration of list – electronic communications provider – national fibre network – method of valuation – comparable evidence – whether regard to be had to assessment of BT Group plc’s operational property under the Central Rating List (England) Regulations 2005 – whether disaggregation of BT’s prescribed assessment possible – whether a difference in treatment breaching EU law – reference to Court of Justice of the European Union declined – appeal dismissed*

**IN THE MATTER OF AN APPEAL AGAINST A DECISION OF THE VALUATION  
TRIBUNAL FOR ENGLAND**

**BETWEEN:**

**INTERROUTE VTESSE LIMITED  
(FORMERLY VTESSE NETWORKS  
LIMITED)**

**Appellant**

**and**

**MS ALISON GIDMAN  
(VALUATION OFFICER)**

**Respondent**

**Re: Telecommunications Fibre Optic Network & Premises,  
England (incl. Kennet),  
Near Marlborough,  
SN8 5T**

**The President, Mr Justice Fancourt, and A J Trott FRICS**

**The Rolls Building, Fetter Lane, London, EC4A 1NL**

**5-8 November 2019, 27 March 2020**

*Aidan O’Neill QC*, instructed by Sherrards Solicitors LLP, for the appellant

*Daniel Kolinsky QC* and *Yaaser Vanderman*, instructed by HMRC’s Solicitor’s Office, for the respondent

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The following cases are referred to in this decision:

*Bradford (Valuation Officer) v Vtesse Networks Limited* [2006] RA 57  
*Bradford (Valuation Officer) v Vtesse Networks Limited* [2006] EWCA Civ 1339  
*Bradford (Valuation Officer) v Vtesse Networks Limited* [2009] RA 105  
*Bradford (Valuation Officer) v Vtesse Networks Limited* [2010] EWCA Civ 16  
*British Telecommunications plc v Office of Communications* [2017] EWCA Civ 330  
Case C-390/06 Nuova Agricast [2008] ECR I-2577  
Case C-112/16 Persidera SpA EU:C:2017:597  
*Hughes (VO) v York Museums and Gallery Trust* [2017] UKUT 200 (LC)  
*Telereal Trillium v Hewitt (VO)* [2019] UKSC 23

## **GLOSSARY OF TECHNICAL ABBREVIATIONS**

AVD:	Antecedent Valuation Date
BCMR:	Business Connectivity Market Review
CMA:	Competition and Markets Authority
DFA:	Dark Fibre Access
DWDM:	Dense Wavelength Division Multiplexing Technology
EOI:	Equivalence of Inputs
FTTC:	Fibre to the Cabinet
FTTP:	Fibre to the Premises
LLCC:	Leased Lines Charge Control
LLU:	Local Loop Unbundling
MIS:	Modern Industry Standard
NDR:	Non-Domestic Rates
NGA:	Next Generation Access
OCP:	Other Communications Provider
ODP:	Optical Distribution Point
PWNRC:	Profit Weighted Net Replacement Cost
SMP:	Significant Market Power
WLR:	Wholesale Line Rental

## DECISION

### Introduction

1. This is an appeal against a decision of the Valuation Tribunal for England (the Vice-President, Mr Martin Young) (“the VTE”) dated 21 May 2018 (“the Decision”). For reasons which will appear below, it is a most unusual appeal. However, as is usual, the appeal took the form of a re-hearing of the evidence and arguments of the parties.

2. In the Decision, the VTE rejected an appeal by the appellant ratepayer, Interoute Vtesse Ltd (“Vtesse”), against the respondent Valuation Officer’s (“VO”) assessment of the rateable value of Vtesse’s hereditament in the amount of £2,020,000 per annum in the compiled local non-domestic rating list with effect from 1 April 2010 (“the Material Day”). The respondent’s valuation was based on values on the Antecedent Valuation Date (“AVD”), 1 April 2008.

3. The hearing before the VTE arose from Vtesse’s proposal dated 6 September 2010 to amend the rating list. The proposal identified the property as Vtesse Telecommunications Network in England and stated that a rent of £1,731,000 per year was paid for rented parts of it. The proposal was to alter the entry in the local list so that the rateable value with effect from 1 April 2010 became £1. The grounds for the proposal were stated to be that the value shown in the list was inaccurate, the reasons for the inaccuracy being that the assessment “was incorrect, excessive and wrong in law”.

4. Vtesse therefore did not raise in the proposal, nor did it raise elsewhere, any question about the identity of the hereditament, its occupation or the lawfulness of non-domestic rates (“NDR”) in the context of this property or otherwise. The only challenge raised was as to the correctness of the value entered in the list for the hereditament.

5. The Decision rejected the proposal to amend the list. To understand the issues that the VTE had to determine, it is helpful to identify the points that were argued before it. The Vice-President did this in paragraph 12 of his decision, describing the issues raised by Vtesse as follows:

“In a nutshell, Vtesse is rated at levels far above the class of companies with which it competes or competed in the period covered by the AVD and 2010 list, and in particular, BT Group plc (“BT”) whose effective rateable value can be shown to be around £20 per kilometre. This has been proven under a full judicial process in the Competition and Markets Authority which concluded at paragraph 4.77 ‘We therefore conclude that TalkTalk has demonstrated that there is a material difference between OCPs’<sup>1</sup> NDRs and the attribution of BT’s NDRs in respect of the significant majority of circuits’.

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<sup>1</sup> Other Communications Providers

Vtesse's fundamental point is that EU law applies and governs the way in which the Valuation Office Agency should implement rating policy. To do otherwise would be unlawful. The telecommunications sector is the most highly regulated sector in the world, and is the only market where ex-ante regulation is imposed in most developed markets in the world on the incumbent operator, including in the UK on BT. Ex-ante regulation presupposes that in the absence of imposed competition remedies there will be monopoly abuse in breach of competition law principles.

The valuation of Vtesse is also incorrect under, and inconsistent with, the general principles of rating.”

6. The Vice-President described the two arguments raised by Vtesse as “the unlawful State aid point” and the “rating valuation point”. He noted that Vtesse contended for a rateable value based on £20 per kilometre for its network; that the proposal of £1 was not pursued; and that the respondent maintained there was a settled tone of the list for comparable networks underpinned by directly comparable rental evidence at £250 per kilometre.

7. The VTE rejected Vtesse's argument based on unlawful state aid. It rejected the argument that the decision of the Competition and Markets Authority (“the CMA”) was of assistance to it or justified reaching a different decision on unlawful state aid from that reached by the EC Commission, on an investigation into a complaint raised by Vtesse, on 19 October 2006. The Tribunal further concluded, in relation to the rating valuation point, that:

(a) the networks of Vtesse and BT were not in a comparable legal and factual situation;

(b) disaggregating the rating valuation of BT's network, which was done on an overall receipts and expenditure basis, was not possible so as to provide a valid comparator for valuation of the Vtesse network;

(c) the CityFibre Metro networks were not comparable to the long-distance network of Vtesse; and

(d) the respondent was correct to value Vtesse's network on the basis of the established tone of the list and evidence of comparable market rentals of long-distance fibre at or around the AVD.

8. Since this appeal takes the form of a re-hearing and the decision of the VTE was not based on expert local knowledge, it is unnecessary to set out in more detail the reasons for the Decision.

9. Mr Aidan O'Neill QC appeared for the appellant and called Mr Aidan Paul BSc (Hons), CDipAF, ACMA, MIET, CEng, a Director of Vtesse Harlow Limited as an expert witness, though in reality a witness of fact with expertise in electronic communications; Mr Martin

Duckworth BA (Cantab), an Associate Director at Frontier Economics, as an expert witness<sup>2</sup>; and Mr Dougald Robinson, Board Director of CenturyLink Communications UK Limited, as a witness of fact.

10. Mr Daniel Kolinsky QC and Mr Yaaser Vanderman of counsel appeared for the respondent and called Mr Daniel Cains BSc (Hons), MRICS, a specialist caseworker in the Valuation Office Agency's ("VOA") Telecommunications Team, as an expert valuation witness; Mr Andrew Larkins MRICS, a Telecommunications Specialist within the VOA's National Specialist Unit, as an expert valuation witness; and Mr Ian Johnson MRICS, Team Head of the VOA's Utilities, Transport and Telecommunications Team, as an expert valuation witness.

### **The Appeal to the Upper Tribunal**

11. Vtesse's Notice of Appeal against the Decision is dated 18 June 2018. It identifies various grounds of appeal, in three categories: errors of fact, procedural unfairness and errors of law. The ground of procedural unfairness alleged was not pursued at the hearing of the appeal.

12. The errors of fact identified in the Statement of Case are that the tribunal:

(1) failed to give proper weight to the fact that BT's fibre network is assessed on a receipts and expenditure basis, and that in practice NDR on BT is levied at a much lower rate per lit kilometre;

(2) was wrong to conclude that it was not possible to calculate a tax per individual circuit of the BT network;

(3) was wrong to conclude that it was not possible to disaggregate the BT network into fibre components; and

(4) was wrong to conclude that CityFibre's agreement with the VO was irrelevant to the assessment of the Vtesse network.

13. The errors of law identified in the Statement of Case are the following:

(1) failure correctly to apply the principles of state aid;

(2) failure to apply the principles of equal treatment and the maintenance of fair and undistorted competition between undertakings, which apply in the context of EU regulation of telecommunications on an objective, non-discriminatory, free market competitive basis;

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<sup>2</sup> Mr Duckworth adopted an expert witness statement dated 27 June 2016 which he prepared on behalf of TalkTalk concerning Ofcom's Business Connectivity Market Review – Final Statement 28 April 2016. It was primarily concerned with the price mechanism to access BT's dark fibre.

(3) failure to apply the principle of fiscal neutrality, namely that similar or identical factual situations should be subjected to tax in the same way and on the same basis;

(4) error in relation to rateable occupation of Vtesse's network.

14. In the event, the argument that the VTE had failed correctly to apply the principles of state aid and the alleged error in relation to rateable occupation were not pursued. Instead, Vtesse focused on the duty of the VOA, as an emanation of a member state, to give equal treatment in a fiscal context to comparable businesses and networks.

15. On this basis, Vtesse claimed that it should have been treated in the same way as BT, that is to say its network should have been assessed on the basis of £20 per kilometre, and its buildings and plant and machinery (the assessed value of which was not otherwise disputed in pure valuation terms) should have been discounted by 50% to bring them into line with the alleged assessment of BT's buildings and plant and machinery. On that basis, the correct assessment on the Material Day, according to Vtesse's approach, was £234,637, not the £2,020,000 in the list.

### **Agreed facts**

16. The parties helpfully agreed certain facts for the purposes of this appeal. These are set out in a Statement of Agreed Facts dated 22 February 2019. The following paragraphs in this section set out the material facts that are agreed.

17. The rateable hereditament comprises three elements: a fibre-optic network; network buildings, and rateable plant and machinery.

18. The fibre-optic network is wholly contiguous and on the relevant date the total distance was 7567.16 route kilometres. The network also extends 530 route kilometres into Scotland, but those kilometres are not included in the subject hereditament. Two fibres were lit by Vtesse (that is to say, signals were transmitted down two fibres) on the entire route. Vtesse lit the fibres with their non-rateable plant and machinery in their own buildings, or in co-location space and rack space within other telecommunications operators' buildings and in customers' premises. The network connected 55 data centres, the majority not being in Vtesse's rateable occupation, and 48 towns and cities.

19. The fibre network was constructed by Vtesse with a mixture of leased and own build fibres, the majority of which were leased from third-party providers. Vtesse declared 7142 km of leased fibre as at 7 May 2008. The leased fibres declared, with details of the provider, the distances, the amounts paid and the commencement dates, are set out in Appendix 2 to the Statement of Agreed Facts.

20. Vtesse operated in the commercial telecommunications sector only and had approximately 50 clients, including a large contract at the Material Day with Lloyds Bank.

21. Vtesse occupied only two major buildings and three small buildings, together with various items of plant and machinery, including electrical items such as generators, transformers, uninterruptible power supplies, batteries and switches, but excluding the fibres, cables and ducts.

22. The amounts entered in the local rating list on the effective date of 1 April 2010 for the buildings and plant and machinery was £166,587, of which £150,861 was entered for the buildings.

23. It was specifically agreed that Vtesse was the rateable occupier of the hereditament and that it was its underlying value that was being valued, not the business of Vtesse.

24. A schedule of fibre transaction evidence at Appendix 3 was agreed. This schedule comprises 16 transactions over a period from 19 November 2004 to 18 July 2014, under which leases of varying amounts of twin fibre (from as little as 501 km to as much as 7083 km) were made for terms of between 5 and 20 years. Of particular significance was a lease with effect from 30 January 2008, shortly before the AVD, under which Vtesse rented 1463.21 km of twin fibre from Geo at an agreed annual rate of 25p per metre (£250 per kilometre).

25. A schedule of rating settlements agreed between the VOA and the occupier for the purposes of the 2010 rating list was agreed as Appendix 4 to the Statement of Agreed Facts. This schedule comprises 20 agreed assessments and two withdrawn appeal assessments.

26. Appendix 5 to the Statement of Agreed Facts includes the rateable values assessed for the BT hereditament on varying dates, including an assessment as at 1 April 2010 of £244,460,000 per annum. At that time, it was agreed that BT had 10,448,000 active consumer lines.

### **History and Background to this Appeal**

27. In this section, we refer briefly to the main events concerning the Vtesse network that are relevant to the decision of the issues on this appeal. In a number of cases it will be necessary to refer to them further when assessing the evidence that we heard.

28. The background to Vtesse's appeal starts with the EU regulatory framework for the electronic communications industry. This comprises (and comprised at the Material Day):

- (1) Regulation (EC) No. 2997/2000 (unbundling of local loops), to force former state monopoly operators to allow potential competitors to have priced access to parts of their networks (the 2000 EC Regulation)



(2) Directive 2002/19/EC on access to, and interconnection of, electronic communications networks and associated facilities (the Access Directive)

(3) Directive 2002/20/EC on the authorisation of electronic communications networks and services (the Authorisation Directive)

(4) Directive 2002/21/EC on a common regulatory framework for electronic communications networks and services (the Framework Directive)

(5) Directive 2002/22/EC on universal service and users' rights relating to electronic communications networks and services (the Universal Service Directive)

(6) Directive 2002/58/EU on the processing of personal data and the protection of privacy in the electronic communications sector (the Directive on Privacy)

(7) Commission Directive 2002/77/EC on competition in the markets for electronic communications networks and services (the Competition Directive)

(These Directives are now recast in Directive (EU) 2018/1972, which establishes the European Electronic Communications Code and is to be given effect in member states from 21 December 2020. It remains to be seen whether the British Government will give effect to it in compliance with the Directive.)

29. As explained by the Court of Appeal in *British Telecommunications plc v Office of Communications* [2017] EWCA Civ 330, the common regulatory framework is intended to promote competition and impose regulatory controls on any undertaking found to have significant market power ("SMP"). This is in order to avoid the distortion or restriction of competition, but also to:

"... [reflect] the general principles of legal certainty and legitimate expectation in EU law, which also inform the interpretation of EU legislative instruments. The regulation of the market to ensure proper competition is supposed to allow market participants to be able to make commercial decisions (both as to what services to provide and what services to buy) by reference to prices which are declared in advance of transactions, and are to be set in advance without distortion as a result of the SMP of any market participant."

30. On 1 April 2003, an amendment to the rating list for the District of Slough for the 5-year period from 1 April 2000 was made to state a value for the Vtesse network (then much smaller and in course of construction) at an annual value of £110,000. On 27 October 2003, Vtesse proposed to amend the list to show an annual value of £3,095, on the basis that it was only in rateable occupation of its own build parts of the network, not the fibres that it leased from others.

31. A few months later, on 17 February 2004, Vtesse made a complaint alleging the provision to BT of unlawful state aid. The Commission of the European Communities ("EC Commission") later opened an investigation.

32. On 16 July 2004, the (then) Berkshire Valuation Tribunal ordered the entry in the rating list for Vtesse to be deleted, on the basis that Vtesse was not in occupation of the leased parts of its network and that its own build parts were separate rateable hereditaments spread around the country. That decision was appealed to the Lands Tribunal by the VO.

33. For the rating list having effect from 1 April 2005, under section 53(1) of the Local Government Finance Act 1988 The Central Rating List (England) Regulations 2005 designated all BT's communications hereditaments as being a single hereditament on the central rating list for valuation purposes and treated it as being occupied by BT. This was, it appears, the origin of the complaint about discrimination that Vtesse pursues in this appeal.

34. On 23 November 2005, the Lands Tribunal decided as a preliminary issue the question of whether Vtesse was in rateable occupation of its leased fibre network. In *Bradford (Valuation Officer) v Vtesse Networks Limited* [2006] RA 57 the President, George Bartlett QC, held that the VO had been correct to enter Vtesse's fibre network in the rating list as a single hereditament because Vtesse was in rateable occupation of the leased fibres as well as its own build fibres.

35. The following paragraphs of the decision are noteworthy:

“15. The agreements under which Vtesse had the use of fibres belonging to other operators were for the use of what is referred to as ‘dark fibre’, that is to say fibre that has not been ‘lit’ or activated. The fibres in each of the component parts of the network are lit by Vtesse using its own (non-rateable) plant and machinery. Fibres are lit by the generation of a laser pulse from Vtesse's own equipment so that photons, or particles of light, are pulsed through the fibres. The laser pulse operates continuously, *whether data is being transmitted or not*, and data is sent by changing the pattern of the laser pulse. The receiver has to be synchronised, and synchronisation is carried out by Vtesse.... [emphasis added]

.....

39. There are, in my judgment, three features of Vtesse's use of the leased fibres that are of the greatest significance. The first is that Vtesse's entitlement under each of the agreements is to the use of particular fibres. Reliance was at one time placed by Vtesse on the fact under certain of the agreements... the leasing company undertook to provide for Vtesse's use a pair of fibres, without tying the obligation to any particular identified fibres. However, as counsel for Vtesse accepted, once a pair of the company's fibres had been spliced to Vtesse's own-build fibres, Vtesse's rights under the agreements related to the particular fibres that had been so spliced. The leasing company was thus not providing a service for Vtesse through the routing of signals along any fibres that it might choose to employ for this purpose but was providing specific fibres for the use of Vtesse. The second significant feature is that Vtesse's use of the leased fibres was exclusive. No one, neither the leasing company nor another operator, could use those particular fibres. Thirdly, it was Vtesse, and Vtesse alone, that activated the fibres for the transmission of signals. It did this through the generation of a laser pulse on its own equipment, and it synchronised the receiver so that a meaningful signal could be transmitted. By this means, through its active operation of its system, Vtesse was able to provide a service for its customers. The leasing companies simply provided, and maintained, the fibres.”

36. The President then stated that those three features were decisive in determining that Vtesse was in rateable occupation of the leased fibres and that its system constituted a single hereditament.

37. On 12 October 2006, the EC Commission reached a conclusion that no unlawful state aid had been provided to BT. Its conclusion was summarised as follows:

“(174) In conclusion, it should be recalled that business rates are a tax on the value of the property concerned. They are not a tax on profits or revenues. They are normally applied on all non-domestic properties, and consequently are applied to all telecommunications networks. According to British case-law, all telecommunications networks are valued as a whole. There are several methods for valuing such property. When all methods can be applied, they should result in the same valuation; the use of a specific valuation method depends on the circumstances of the case.

(175) It now appears that the VOA has applied to BT and Kingston the general rules concerning business rates as laid down in the legislation and case-law. It is clear that the valuation of BT’s and Kingston’s hereditaments as well as the revisions of these rateable values, are carried out on the basis of a different method than in the case of their competitors. However, the Commission can conclude that there is no evidence that the use of this different method is not justified by the objective differences between those firms and their competitors and by the extent of the evidence available to the VOA.

(176) There is no evidence that the application of a different valuation method to BT and to Kingston has resulted in an advantage to these firms in comparison with their competitors. Since there is no evidence of an advantage, the Commission can conclude that the non-domestic rates system has not provided State aid to BT and/or Kingston within the meaning of Article 87(1) EC during the period considered by the Commission i.e. 1995 – 2005.”

38. On 19 October 2006, the Court of Appeal dismissed Vtesse’s appeal against the Lands Tribunal’s decision on the preliminary issue ([2006] EWCA Civ 1339). As a result, as a matter of domestic law, Vtesse was liable to pay non-domestic rates on the whole of its fibre network. A further hearing of valuation evidence before the Lands Tribunal eventually took place in May 2008.

39. Earlier in 2008, Ofcom had published a consultation paper on business connectivity, called “Business Connectivity Market Review” (“BCMR”), which included an analysis of prices charged by BT for its wholesale ethernet services and the cost of delivering those services. Annex 12 to the paper expressed views as to the right devaluation, or disaggregation, of BT’s overall costs (not network value) in order to identify the contribution to those costs made by the fibre-optic network.

40. Also in 2008, new statutory instruments relating to BT’s single hereditament came into force. These were intended to deal with the effect on NDR of unbundling BT local loops. By The Central Rating List (England) (Amendment) Regulations 2008 (SI 2008 No.429), unbundled local loops that were used by BT’s competitors pursuant to the 2000 EC Regulation were deemed to remain in BT’s rateable occupation. By The Non-Domestic Rating (Communications

Hereditaments) (Valuation, Alteration of Lists and Appeals and Material Day) (England) Regulations 2008 (SI 2008 No.2333), the unbundling of local loops was deemed to be a material change in circumstances, entitling BT to seek a re-assessment of the rateable value shown in the Central List for its single hereditament.

41. Thus, by statute, a deemed material change in circumstances could require an adjustment to be made to the value entered in the Central List for BT's hereditament. It would be expected that the value of BT's hereditament would be likely to be reduced by unbundling of local loops, since BT would lose the ability to provide services to those consumers at a profit and would gain instead the regulated fee payable by the other communications provider ("OCP") for use of BT's loops. There therefore could, theoretically, be value attributable to a quantity of unbundled loops that was identifiable from the amount of the re-assessment in respect of that unbundling.

42. On 7 November 2008, the Lands Tribunal gave its decision upholding the VO's case on the value of Vtesse's hereditament and deciding a separate appeal against a 2005 rating list entry ([2009] RA 105). That resulted in an entry of £110,000 p.a. from 1 April 2003 and £470,000 with effect from 7 November 2008. The VO appealed that decision to the Court of Appeal, seeking an earlier effective date for the higher valuation. Vtesse also appealed the decision, on the basis that the Lands Tribunal had failed to take into account the rateable value of a comparable and competing fibre-optic network, namely that of BT. Vtesse's appeal was advanced as a matter of national rating law as well as EU competition law.

43. In para [19] of his judgment in the Court of Appeal ([2010] EWCA Civ 16), Lloyd LJ said:

"BT's network is vast and complex, including many elements altogether foreign to that of [Vtesse], such as millions of local access copper loops, over 100,000 telephone kiosks, mast sites and two satellite earth stations in addition to its extensive national fibre optic trunk network. A central issue on valuation is whether any meaningful comparison can be made between [Vtesse's] network and that of BT given their different size and character. As part of that issue, it is relevant to consider whether the BT network can relevantly be disaggregated, in order to identify a figure attributable to the component part which is the fibre-optic network, or more specifically to that part of such network which is used to provide services of the kind which [Vtesse] provides."

44. The three principal arguments advanced on behalf of Vtesse before the Court of Appeal were:

(1) the VO was required to take account of BT's assessment in deciding Vtesse's rateable value because of EU competition law;

(2) the Lands Tribunal was wrong to reject Vtesse's argument based on the Competition Directive because of the Commission's decision;

(3) the Lands Tribunal was wrong to assume that the burden of proving the rateable value of BT's network lay on Vtesse, and in not referring to the Ofcom 2008 consultation paper.

45. The Court of Appeal identified the different methods of valuation available to assess the rateable value of a given hereditament: the rental method (direct rental comparison); the tone of

the rating list; a receipts and expenditure method to estimate the amount that a putative tenant would be prepared to pay to a landlord of the hereditament, and the contractor's basis, to assess the amount of interest on the capital sum needed to construct an equivalent hereditament. Lloyd LJ noted that it was common ground that, whichever method of valuation is used, the object was the same, namely to identify the hypothetical market rental figure for the hereditament.

46. After referring to relevant authority, Lloyd LJ continued, at [36]:

“Equality of rating is a fundamental principle of rating law: see for example *Poplar Assessment Committee v Roberts* [1922] 2 AC 93, Lord Atkinson at page 108 and Lord Parmoor at page 119. Accordingly it does not seem to me that Vtesse's contentions gain any additional force from reliance on European Union law. In the end Mr Green relied on European law for the proposition that the burden was on the government to ensure, and where relevant to demonstrate, that there was equality between ratepayers. This case is altogether unlike those he cited as examples of unequal treatment, where the inequality, whether obvious or not, was built into the system in one way or another. Here the whole basis of English domestic law is exactly that which European law requires it to be, namely that like cases are to be treated alike.”

47. The court held that the Lands Tribunal's task had been to decide between two different approaches to valuation: either the VO's case based on market evidence and the tone of the list, or Vtesse's case based on the possibility of relevantly disaggregating the BT rateable assessment in order to identify a component attributable to the fibre-optic element of the network and take it as a proper comparison for a unit of valuation applicable in Vtesse's case. The Court held that the Lands Tribunal had been entitled to deal with that as a matter of evidence, weighing the valuation merits of the two different approaches, and that EU law added nothing to the principle of equality as between hereditaments, which was a fundamental part of domestic law. The Court rejected the argument that the VO was obliged to make a comparison between BT's assessment and Vtesse's assessment.

48. In consequence, the court refused to refer any question to the Court of Justice of the European Union pursuant to article 267 of the Treaty on the Functioning of the European Union. None was necessary in order to decide the appeal.

49. In or about April 2010, a new valuation list was published. This gave Vtesse the opportunity (which it took) to appeal against the new rateable value assessment of £2,020,000.

50. On 6 October 2010, Ofcom published a consultation paper in connection with a request made by BT for continued exemption from competition undertakings that it had previously given. The exemption sought related to its Wavestream National UK-wide end-to-end fibre product. BT had previously been granted an exemption in relation to this product until 31 December 2010. It sought an extension for a further period. Ofcom proposed to grant the exemption sought, subject to a market review that it proposed to carry out subsequently, and noted that competitors had a number of options for supplying services similar to BT's Wavestream National service. Only five responses to the consultation paper were received. Vtesse was not among them.

51. In its consultation response and conclusions dated 14 December 2010, Ofcom stated that it would grant the exemption sought; and that in the event that a competition problem was discovered when the market review was conducted, the exemption would then be reviewed. Para 1.7 of the summary states that if, following the review, Ofcom finds BT to have significant market power (“SMP”) in a market that included Wavestream National services, the exemption would be reviewed; in the absence of a finding of SMP, the exemption would stand. It is therefore implicit that, as at December 2010, Ofcom did not consider that BT had SMP in services provided using long-distance end-to-end fibre networks.

52. By 2017, Ofcom and the CMA were concerned with regulating access to “dark fibre” to provide competition in the provision of next generation access (“NGA”) for high-speed broadband services. Ofcom had proposed terms of regulated access to BT’s dark fibre and calculated the price on the basis of a Profit Weighted Net Replacement Cost (“PWNRC”) assessment of the costs of BT’s fibre, including the amount of rates attributable to the fibre. Since any user of the fibre would be liable for rates in place of BT, there needed to be an adjustment in the price paid as regards the rates liability that BT would no longer have. Ofcom had proposed that this adjustment should be made on the basis of a cost of rates attributable to BT. TalkTalk objected to Ofcom’s proposal, contending that the adjustment should reflect the user’s own rates liability and its objection was determined by the CMA.

53. Talk Talk’s evidence to the CMA attributed an NDR liability to BT of between £70 and £100 per kilometre, as compared with an NDR liability for OCPs of between £488 and £1568 for a route length of 5km to 10km of fibre (para 4.53 and Table 4.2 of the CMA’s Final Determination). BT provided confidential evidence to the CMA, which appears to have persuaded it that the attributed cost of rates per kilometre was significantly higher, but that nevertheless a material differential remained. Importantly, however, this exercise was an attribution of cost to particular parts of BT’s single hereditament, not a valuation of any part of BT’s network. Further, the range of costs was as at 2018/19<sup>3</sup>, not as at 2008, the AVD for the purposes of Vtesse’s appeal, and also took into account a recent VOA decision to increase BT’s rates with effect from the year 2018/19.

54. In 2018, the Telecommunications Infrastructure (Relief from Non-Domestic Rates) Act 2018 made provision for 100% rates relief for new fibre infrastructure laid on or after 1 April 2017. Where new fibre is part of a rateable hereditament, The Non-Domestic Rating (Telecommunications Infrastructure Relief) (England) Regulations 2018 (SI 2018 No.425) provide a formula for partial relief from rates liability. This will involve identifying what proportion of the rateable value shown for the hereditament *appears to be attributable to* new fibre, any plant and machinery used in connection with it and any part of the hereditament occupied by the fibre, plant and machinery. That will therefore, necessarily, involve a VO certifying a proportion of a rateable value that is attributable to a component or to components of a single hereditament.

## **The Issues on the Appeal**

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<sup>3</sup> The estimate of BT’s NDR liability was at 2017/18.

55. Against the above factual background, Vtesse advanced its case in the VTE and the VTE found against it.

56. For the purposes of the appeal to this Tribunal, the parties agreed a Statement of Issues. These issues, as stated, are in the form of propositions advanced by the VO and the extent to which the proposition is contested by Vtesse. Mr Paul explained in his evidence that Vtesse had used the document to make further response to the VO's case. The issues are:

- a. The rental schedule (in the Statement of Agreed Facts) provides the best evidence to support the value of the hereditament;
- b. There is a settled tone for the value of long-distance fibre networks in the 2010 list of £250/km;
- c. The BT hereditament (which is valued on an R&E basis) is not comparable to the Vtesse hereditament;
- d. There is no means of disaggregating an R&E valuation, so the BT valuation cannot meaningfully be disaggregated to provide a reliable indication of the rateable value of part of BT's hereditament;
- e. CityFibre's hereditaments are not comparable to the Vtesse hereditament;
- f. The CMA determination is not relevant to the valuation of the Vtesse hereditament.

57. Vtesse takes issue with each of these propositions in the Statement of Issues, save that it says that issue (e) misses the point. It is instructive to consider Vtesse's response to issues (c), (d) and (f) in particular.

58. On (c) and (f), Vtesse states that both it and BT are electronic communications network providers, and EU law requires equal treatment and non-discrimination. The CMA determination is said to demonstrate discriminatory treatment and there is therefore a breach of competition law, which is superior to rating law.

59. Vtesse's response on (d) is that the assertion about disaggregation is untrue, based on evidence of NGA lines, which are alleged to be disaggregated from the overall BT assessment at a value of either £18 or £20 per connection.

### **The Parties' Cases**

60. In summary, the VO's case is that there is an established tone of the 2010 rating list for long-distance, twin-fibre networks, supported by open market comparable evidence, which gives a value of £250/km for the fibre. The comparables include a substantial length of fibre leased by Vtesse itself from Geo, which was agreed as a transaction at a rate of 25p per metre (£250/km) with effect from January 2008, only three months before the AVD. For the two principal buildings, the VO values on a conventional basis of a rent per square metre, supported by a

schedule of local comparables. The VO does not agree that a discount of 50% is appropriate, as Vtesse contends, in order to provide equality of treatment with what BT is alleged to pay by way of rates on the operational buildings within its single hereditament. The same point arises in relation to the (otherwise agreed) valuation of the plant and machinery.

61. Vtesse's case, in its proposal, was that a nominal value of £1 should be substituted for the value in the list. Vtesse has provided no valuation evidence in support of its case. When asked why, Mr Aidan Paul, a director of an agent of Vtesse (and formerly of Vtesse itself), who has a financial interest in the outcome of this appeal, said that it was not Vtesse's point in these proceedings to show that the rateable value was zero. He said that even though he claimed in evidence that an R&E valuation of Vtesse's relevant business would have produced a net divisible balance of zero, and accordingly a valuation of zero would have resulted. Nevertheless, in its Appeal Notice, Vtesse contends for a value as at the Material Day of £234,637<sup>4</sup>, based on £20/km disaggregated from BT's assessment and a similar exercise in relation to the value of BT's buildings.

62. Mr Paul said, in answer to the Tribunal's question, that the point of these proceedings was to establish fair and equal treatment of Vtesse with the dominant operator in the market with which Vtesse competes, namely BT. Vtesse's contention on this appeal is that EU law mandates that it and BT be treated equally as regards (the quantification of) liability to NDR, and that accordingly the VO is required to apply the same value (£20/km) that is alleged to represent what BT pays by way of NDR for its long-distance network and the same value as for BT's operational buildings and plant and machinery.

### **Consideration of Vtesse's Case**

63. We have considered carefully whether it is a proper purpose of a rating appeal, based on a proposal that contends only for a lower rateable value than that entered in the list, to seek to establish that there is unfair or unequal treatment of electronic communications operators. Vtesse was invited by the Deputy President of the Lands Chamber at an earlier, case management stage of this appeal, to consider whether it should provide a valuation, on the R&E basis if it saw fit, if its contention in this case was that Vtesse's hereditament should be valued on that basis, like BT's. But it has deliberately not done so. It argues instead that EU law requires the VO to adduce that evidence, since BT and Vtesse must be treated in the same way.

64. Instead of producing its own valuation evidence (which, we repeat, would on Vtesse's assertions of profitability have given a landlord's share of a nominal amount), Vtesse argues that it should be assessed at a rate per kilometre for a pair of fibres equivalent to what can (it says) be extrapolated from the R&E valuation of BT's own hereditament (with a similar approach in relation to buildings and plant and machinery). On a proper analysis, it therefore does not urge on the Tribunal an R&E valuation of its own hereditament on the basis that such a valuation approach would be the same as the valuation approach used for BT's hereditament. It argues

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<sup>4</sup> 7,567.16 km fibre x £20 per km = £151,343.20. Plus 50% of the value of buildings and plant and machinery = £166,587/2 = £83,293.5. Total = £234,637.



that, regardless of any physical differences between the BT and Vtesse hereditaments, an equivalent rate/km to that disaggregated from BT's own R & E valuation, namely £20/km (as it contends), should be applied to its own hereditament (with the same approach in principle in relation to buildings and plant and machinery). This is justified, it says, because EU law demands non-discriminatory treatment. This therefore *assumes*, without seeking to establish, that Vtesse's network and BT's network are comparable. It also assumes that a reliable value can be attributed to BT's own long-distance fibre network derived by a process of disaggregation from a single value for the whole of BT's hereditament.

65. This is, on any view, a thoroughly unorthodox approach to valuing a hereditament for rating purposes. Para 20.1 of IVS 105, produced by the International Valuation Standards Council and which prescribes mandatory considerations for professional valuation experts, states:

“the market [i.e. rentals] approach provides an indication of value by comparing the asset with identical or comparable (that is, similar) assets for which price [rental] information is available. When reliable, verifiable and relevant market information is available, the market [rentals] approach is the preferred valuation approach.”

66. In *Telereal Trillium v Hewitt (VO)* [2019] UKSC 23, Lord Carnwath JSC explained some of the basic principles of valuation at [7] as follows:

“the underlying principle is not in doubt. The valuation must be based on an estimate of the rent at which the hereditament ‘might reasonably be expected to let from year to year...’. In short, the valuer must imagine a hypothetical negotiation between a willing landlord and a willing tenant and arrive at the rent which best represents the resulting compromise:

‘You must assume a landlord willing to let, and a tenant willing to take by the year; and having done so, you must get in the best way you can at the rent which, under an agreement brought about by the compromise of the conflicting interests of the man who wants to receive as much as he can and the man who wants to pay as little as he can, would be arrived at under such circumstances.’ (*Smith v Churchwardens and Overseers of the Poor of the Parish of Birmingham* (1888) 22 QBD211, 219, per Wills J.)

In similar terms in *Robinson Bros (Brewers) Ltd v Houghton and Chester-le-Street Assessment Committee* [1937] KB 445, 470, Scott LJ said:

‘The rent to be ascertained is the figure at which the hypothetical landlord and tenant would, in the opinion of the valuer or the tribunal, come to terms as a result of bargaining for that hereditament, in the light of competition or its absence in both demand and supply, as a result of the ‘higgling of the market’. I call this the true rent because it corresponds to real value.’”

67. In *Hughes (VO) v York Museums and Gallery Trust* [2017] UKUT 200 (LC), this Tribunal said the following about methods of valuation:

“[112] Ascertainment of the rent at which premises might reasonably be expected to let on the statutory assumptions is a question of fact, not one of law. The selection of the most appropriate technique to be employed in answering that question is a matter of valuation judgment rather than legal precedent.

[113] The best evidence of rental value is provided by rents for comparable properties agreed in the open market. The greater the adjustments required to be made to mirror the statutory valuation assumptions or other differences, the less reliable a guide the comparable may be, but valuation by the comparative method always has the advantage over other methods of being rooted in evidence of the behaviour of real landlords and tenants in the market in which it is to be assumed the subject premises are being let. Regard may also be had to evidence of comparable assessments, which in most cases are likely to be based on evidence of lettings in the market.

[114] Where sufficient evidence of comparable lettings or assessment evidence is not available some other approach to valuation must be employed. Three alternative approaches were relied on by the experts: the contractor’s basis, the receipts and expenditure basis, and the ‘shortened receipts’ basis.”

68. It is, however, fundamentally important that the choice of valuation method, depending on the facts of the case and the judgment of the valuer, should not make a difference to the end result. That is because each method is calculated to identify the rent that would reasonably be agreed on the basis of the statutory hypothesis. Different valuation methods are not ways of obtaining different values. Comparability, so that only like or similar hereditaments are compared, and different hereditaments are not compared, is fundamental to valuation practice. Accordingly, if there is good market evidence of lettings of comparable hereditaments, or good evidence of parties agreeing rental values reflecting that evidence, then that is the best evidence of value. If such evidence is not available, it will be necessary to have recourse to another method of valuation, either the R&E method or the contractor’s basis.

69. Where the R&E method of valuation is used, what is done is to assess the likely profits attributable to a business conducted using the actual hereditament. Having identified the receipts and expenditure associated with that business, the net annual profit is then shared between the business (the hypothetical tenant) and the hypothetical landlord of the hereditament. The R&E method does not involve identifying a comparable business and then seeking to disaggregate the R&E valuation of that other business, with a view to seeking to isolate (or attribute) a value for one component of the business. That logically and practically cannot be done as a valuation exercise, because the R&E valuation produces an overall net profit for the whole business, taking account of all receipts and expenditure.

70. The only case as to value that Vtesse advances (amounting to a value of £234,637 as at 1 April 2010) is a hybrid calculation. It is based on seeking to attribute a cost or value to the long-distance fibre network part of BT’s single hereditament, to obtain a rate per km for BT’s network, which is then applied to Vtesse’s hereditament. The justification for that approach is that Vtesse and BT are competitors in the same market. It follows that neither market evidence of comparable lettings of long-distance fibre nor the receipts and expenditure associated with Vtesse’s own business or a notional business using Vtesse’s network are components of its case.

71. Although Mr Paul was reluctant to accept that he was not a valuation expert – he said that he had expertise in company accounts and owned a portfolio of investment properties – the truth is that he is not a qualified or experienced property valuer. Vtesse called no evidence from a qualified or experienced - let alone expert - valuer in support of its case.

72. Nevertheless, in our view the Tribunal can and should take Vtesse's case to be that a rateable value of £234,637 should be substituted for the value of £2,020,000 in the list. The gravamen of its case is that a different value from £234,637 would be unlawful because it would represent an unjustified difference in treatment from the valuation of a comparable component of a competitor's (BT's) business.

73. Vtesse also seeks to rely on the VO's valuation of CityFibre's Metro hereditaments. However, it does not rely on that valuation to derive a value or rate that should be applied to its own hereditament but to show that the VOA is unjustifiably treating similar networks in a different way, given that CityFibre, and not those who light its fibres, is treated as being in rateable occupation, and that therefore its treatment of Vtesse is discriminatory for that reason too.

### **Factual findings**

74. It is appropriate, at this stage, to make findings about the relevant facts as they relate to this appeal. That is to say, facts about the Vtesse hereditament as it stood on 1 April 2010 (which are largely agreed); about the state of the market for the rent of long-distance fibre as at 1 April 2008 (the relevant transactions being agreed), and the evidence adduced in support of each side's case on value, including the facts relating to BT's and CityFibre's hereditaments and assessments. We deal with the valuation approach of the Respondent first, identifying the evidence relied on; then the valuation approach of the Appellant, dealing with the evidence relating to it thematically, using sub-headings to indicate the different material on which the Appellant or the VO Respondent relied. We then deal with the evidence relating to the valuation of the buildings and plant and machinery.

75. In the light of our review of the evidence relied upon, we then explain our findings and state what - on the evidence that we have heard and on the basis of domestic rating law - is proved to be the value of Vtesse's hereditament at the AVD, and whether Vtesse has proved any of the errors of fact that it contends were made by the VTE. We will then consider whether, as a matter of EU law, any different value must be entered in the valuation list.

76. We do not need to repeat in this section the agreed facts about the Vtesse hereditament, which we have described in paragraphs 16-26 above.

### ***(1) The respondent VO's valuation approach***

77. Mr Cains gave evidence of the route lengths of 17 (mainly) national network operators (excluding BT but including Vtesse) where the fibre length was greater than 1,000km. The average (mean) length was 5,331 km, with the largest network being Cable & Wireless UK at 22,442 km (England) and the smallest Level 3 Communications Ltd at 1,647 km. The Vtesse network was above average at 7,567 km. No evidence was given about the length of BT's fibre trunk network but Mr Larkins said in cross-examination that it was probably two to four times that of Virgin Media (approximately 7,000 km), i.e. between 14,000 and 28,000 km. BT's total fibre length was much greater at 18,000,000 km of fibre pairs<sup>5</sup>.

78. Mr Cains produced a schedule of rental evidence for the letting of fibre pairs. The 16 transaction dates varied from March 2004 to July 2014. Many of the transactions included the payment of a capital sum as well as, or instead of, a rent and Mr Cains adjusted these (without explanation about how he did so) to obtain an annual equivalent. Five of the 16 comparable transactions involved a capital payment for fibre. Five other comparables involved a capital payment described as "additional" but which did not affect Mr Cains' analysis of fibre rental value. One comparable involved capital payments of both types. He gave such adjusted rents less weight than transactions which only involved rental payments. The length of fibre pairs varied and only two lettings were close to the total length of the Vtesse network: the letting (without capital payment) of 7,083 km from Virgin Media to EE in December 2011 (which devalued to £546 per km), and the letting of 6,321 km from SSE to JNT Network in July 2012 (which included non-fibre items and therefore was not analysed). All the other lettings were for considerably shorter lengths of fibre. Mr Cains placed most weight on the letting of 2,164.71 km of fibre from Geo to Vtesse on 30 January 2008 at an annual rent (without capital payment) of £250 per km. There were two other lettings to Vtesse: 1,241 km at £250 per km on 19 November 2004, and 2,663 km at £230 per km between September and November 2012. There were six other lettings that did not involve a capital payment for fibre ranging from 501km to 1,373 km in length. The rents varied from £180 to £353 per km, with an outlier at £640 per km and for which Mr Cains noted "basic details only held by VOA". The six transactions took place between February 2006 and July 2014. Mr Cains said his analysis "when looked at as a whole" supported his adopted figure of £250 per km for long distance fibre pairs.

79. Mr Cains also relied upon there being a settled tone of the list for fibre pairs. He said that except for Vtesse all appeals against the assessment of long distance fibre-optic telecommunications network hereditaments over 1,000 route km had been settled. There had been 23 such settlements, 20 of which were agreed and three appeals had been withdrawn<sup>6</sup>. These settlements were reached with 11 specialist telecom rating surveyors who Mr Cains identified in his evidence. There were a further seven agreements for networks of less than 1,000 route km which were valued at higher rates per route km. The settlements were in respect of the compiled list and Mr Cains said there had been many subsequent settlements of appeals arising from material changes of circumstance. Over the life of the 2010 list (except for Vtesse) all 171

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<sup>5</sup> Mr Larkins' expert report at paragraphs 6.1 and 6.3. This figure is for the whole of the United Kingdom.

<sup>6</sup> These are the same settlements and withdrawals shown in Appendix 4 of the statement of agreed facts (see paragraph 25 above). Mr Cairns included a further withdrawn appeal (Fujitsu) in Appendix 6 of his expert report.

appeals in respect of long distance (over 1,000 km) fibre networks had been settled by agreement (92) or had been withdrawn (79). Mr Cains' analysis of each of the 23 compiled list settlements showed the inclusion of two fibres at a rate of £250 per km<sup>7</sup>.

80. Mr Cains explained that the basis of all the settled appeals was a scale of values produced by the VOA. The market rental evidence had been analysed to derive bands of rateable value which depended upon the route length and the number of lit fibres. These formed the basis of two scales; one for networks wholly within London and, as here, one for national networks and networks wholly outside London. For networks over 1,000 route km the rateable value for two fibres was £250 per km.

## ***(2) The Appellant's valuation approach***

81. Mr Paul did not contest the rental or assessment evidence of the VO in terms but criticised the VOA's lack of a consistent approach to different ratepayers. He said the services provided by Vtesse and BT were identical in all material respects during the 2010 list. They used the same equipment and the same technical specification of fibre. But, said Mr Paul, BT received favourable treatment in respect of non-domestic rates which contributed to the loss by Vtesse to BT of a major contract with Lloyds Bank in 2010. This contract accounted for some 40% of Vtesse's then revenue. The differential treatment of Vtesse as compared with BT was unjustified and unlawful. The VOA should have valued the Vtesse hereditament using the same values as were used for BT's hereditament.

82. Mr Paul's evidence was that in its 2009 accounts, Vtesse had revenues of £19,674,000 and made a small profit of £965,000. The contract with Lloyds Bank represented about half those revenues. Mr Paul's evidence was that Openreach, which he said operated the majority of the assets of the BT Group (but not all), had earnings (EBITDA) of £1,960,000,000 at the start of the period. The summary of the R&E cumulo valuation for the BT hereditament at the Material Date, produced by the respondent, shows that the assessment of BT Group's business receipts was £8,136,740,000, with operational expenditure of £5,273,829,000. Whichever figures for BT are most accurate, it is self-evident that the businesses of Vtesse and BT are incomparable in size. As will be explained below, they are also incomparable in terms of the range of services provided.

### ***(a) The disaggregation of BT's Central List assessment***

83. The dispute between the parties regarding BT centred on whether it was possible to disaggregate the value of its long distance fibre network from the rateable value of its single hereditament, as determined for the Central Rating List (England) Regulations by the receipts and expenditure method, and then use that derived value to value Vtesse's hereditament.

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<sup>7</sup> It is not stated in terms that the rating agents agreed the analysis as well as the rateable value.

84. Mr Larkins said the BT and Vtesse networks were “vastly different” and were not comparable. The BT network was older, much larger and more diversified than the Vtesse network. It was primarily a local access copper network serving many millions of residential and business customers, whereas the Vtesse network was a fibre network providing leased line services joining some 350 customer sites. The prescribed BT central list hereditament included some 6,000 specialised properties throughout the UK, including 5,500 exchanges, satellite earth stations, transmitter stations and data centres; over 26.5 million copper loops; 18,000,000 km of fibre pairs; 56,000 telephone boxes and kiosks; 84,000 cabinets; millions of posts; and very many items of rateable plant and machinery. It also had approximately 400 properties that did not form part of the prescribed hereditament but were rated under local non-domestic rating lists at a total rateable value of some £75m. The Vtesse network on the other hand comprised 7,567.16 km of fibre pairs, a data centre of 522.51m<sup>2</sup> in Hoddesdon, 1,658.32m<sup>2</sup> of offices in Hertford and three small cabins and containers in Dorchester, Leicester and Peterborough as well as items of rateable plant and machinery.

85. BT also had a universal service obligation to provide basic telephone services to every residential and business customer across the UK regardless of cost or profitability and was regulated as to pricing, service standards and reporting standards in market sectors where its regulator, Ofcom, identified it as having SMP. It was also regulated in terms of local loop unbundling. Vtesse could operate freely in markets of its own choosing and was not regulated. BT and Vtesse only competed for the provision of leased lines to enterprise customers. Mr Larkins did not think such a limited area of competition between the BT and Vtesse networks meant they were comparable:

“The BT hereditament is unique given (a) its physical extent (b) the diversity of elements within the network (c) the regulatory responsibilities associated with the BT prescribed hereditament including the fact that the hereditament includes millions of local copper loops some of which are in the occupation of others. I therefore consider that the BT hereditament is not comparable to any other communication network including Vtesse” (report, para 6.14).

86. Mr Larkins referred to the guidance contained in the IVSC’s General Standard IVS 105: Valuation Approaches and Methods. This described the three principal methods of valuation as:

- (a) the market approach;
- (b) the income approach; and
- (c) the cost approach.

Mr Larkins equated these methods with the direct rental comparison method, the receipts and expenditure (“R&E”) method and the contractor’s basis respectively, which he said had all been endorsed as appropriate valuation methods in rating case law.

87. Paragraph 10.3 of the Standard<sup>8</sup> said that the goal in selecting a valuation method for an asset was to find the most appropriate method in the particular circumstances. Paragraph 10.8 stated:

“Although no one approach or method is applicable in all circumstances, price information from an active market is generally considered to be the strongest evidence of value.”

88. Mr Larkins said the Vtesse hereditament was comparable to similar hereditaments for which there was an active rental market (indeed, the majority by far of the Vtesse network is rented on the open market). A tone of the list had been established from such market rental evidence. Under these circumstances the Vtesse hereditament was most appropriately valued by means of direct rental comparison. BT’s prescribed central list hereditament was different; it was unique and could not be valued by direct rental comparison with another hereditament. IVS 105 stated that the income approach should be applied and afforded significant weight where:

- (i) the income-producing ability of the asset is the critical element affecting value from a participant perspective; and
- (ii) reasonable projections of the amount and timing of future income are available for the subject asset, but there are few, if any, relevant market comparables.

Mr Larkins said the absence of any comparable to the BT prescribed hereditament and the imposition upon it of an exceptional statutory regulatory regime explained the use of the R&E method of valuation, i.e. an income-based approach.

89. Mr Larkins did not think the rateable value of BT’s prescribed hereditament could be used to inform the assessment of Vtesse’s hereditament because:

- (i) the two hereditaments were very different and could not be compared; and
- (ii) even if that was not the case, the R&E method of valuation was incapable of disaggregation into its separate parts. The method was based on a “top-down” approach that considered the revenue and expenditure generated by the BT undertaking as a whole rather than as an aggregation of separate businesses. This was different from the direct comparison (market) method which took a “bottom up” approach, aggregating the value of individual components to give the value of the whole. The R&E method did not identify separate values for individual physical components and therefore could not be disaggregated.

90. Mr Larkins referred to the EC Commission’s acknowledgement of this difference in valuation approach to the hereditaments of BT and Vtesse in its decision dated 12 October 2006 (see paragraph 37 above).

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<sup>8</sup> References are to the version of IVS 105 published on 31 July 2019 which came into effect on 31 January 2020. The IVSC permits early adoption from the date of publication.

91. The Commission noted at [117]:

“OFCOM underlines the difficulty of making appropriate comparisons between very different telecommunications operators (e.g. the average rateable value of a route kilometre of a fibre network can be very different according to the characteristics of the network to which it belongs and to the number of lit fibres on that route).”

The Commission went on to consider whether it was appropriate for the UK authorities to apply the R&E method to BT instead of the rental method, the question being whether there was enough rental evidence to assess the BT network ([122]). The Commission said at [125] that even when rental evidence derived from other telecommunications operators existed, e.g. on optic fibres, the differences between the use of those fibres by operators and the use made of them by BT meant the rental evidence was not fully relevant to value the BT hereditament. The role of the BT fibre optic network was to provide a backbone which interconnected its local loops. The BT network<sup>9</sup> was for this reason unique and could not be compared with any other in the UK:

“It is true that parts of BT’s network may be used by BT to provide services that compete with Vtesse, but they remain physically and functionally incapable of being disaggregated from BT’s whole network. Therefore, on the whole, the two types of network do not fulfil the same function, and are unlikely to have the same rental value. This view is confirmed by OFCOM in particular, which pointed out that the average value of a route kilometre of a fibre network can be very different according to the characteristics of the network to which it belongs and that BT’s core network topology is likely to be very different to that of a backbone operator catering for the corporate market.”

92. The Commission noted the VOA’s view that the R&E method could not be applied to part only of BT’s hereditament for which rental evidence might be available because the method could only be applied to the whole hereditament and therefore component parts of it, such as the fibre optic network, could not be valued in isolation. The Commission said at [127] that there was no probative evidence showing that the VOA was wrong to conclude the rental method could not be applied to BT and that the R&E method was the appropriate method to use.

93. The Commission also dismissed Vtesse’s attempt to identify an alleged discrepancy between the rateable values per unit of the different components of BT’s network and those applied to other telecommunications operators ([152] – [160]). It noted that the VOA must value the hereditaments of telecommunication operators as a whole, without exception, and that:

“It is an inherent feature in any type of property valuation that the market rent of a whole property is usually different from the sum of the market rents of parts of that property...It is therefore likely that the market rent of BT’s property portfolio in isolation will be different from its value when included in BT’s hereditament.” [160]

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<sup>9</sup> The Commission’s comments also applied to Kingston Communications plc, the incumbent telecommunications operator and the owner of the only local access network in the region of Hull.



94. Mr Kolinsky QC submitted that although the Commission was not concerned with the same economic conditions as those at the AVD in this appeal, its reasoning was sound and could properly be applied to the facts now under consideration, i.e. given that the BT and Vtesse hereditaments were not comparable and that it was not possible to disaggregate parts of BT's hereditament from an R&E valuation, the Commission's conclusion at [175] remained sound that "there is no evidence that the use of this different [valuation] method is not justified by the objective differences between [BT] and [its] competitors and by the extent of the evidence available to the VOA".

95. The Appellant did not call any valuation evidence to address the ability of the VO to disaggregate a value for BT's long distance twin fibre network from the value of its entire hereditament. Mr Paul, who is not a valuer, argued that it could be done, and indeed that he had done it, resulting in a figure of about £20 per kilometre. The Appellant's case was that the requirement to adjust the rateable value of the BT single hereditament upon local loop unbundling, the approach of the CMA to attributing a cost to BT's long distance network, the financial adjustments for NGA connections and the 2018 Regulations that require new fibre components of a network to be differentiated from old components for NDR purposes all show that it is both possible and necessary to attribute value to component parts of the BT hereditament, so that the argument that it is impossible to disaggregate a single R&E valuation of the single BT hereditament is no longer credible. We address the material on which the Appellant relies under the sub-headings below.

96. The differences between the hereditaments of BT and Vtesse were considered by the Lands Tribunal in *Bradford (VO) v Vtesse Networks Limited* [2009] RA 105. The Tribunal, His Honour Judge Mole QC and N J Rose FRICS, said at [30]:

"In summary, the valuation officer's view was that:

'no useful analysis can be made of BT's agreed assessment when looking at the rental value of fibre optic networks. The networks are significantly different in scale, age and diversity. BT's assessment is clearly not a direct or even an indirect comparable and any attempt at comparison is spurious in my opinion.'

The Tribunal said at [58]: "we accept, as a matter of fact and judgement and for the reasons recorded in paragraphs 29 and 30 above, the view of Mr Bradford that BT's assessment is simply not usefully comparable with that of Vtesse."

97. The Lands Tribunal's decision was challenged by Vtesse on appeal on the ground, among others, that the Tribunal had not taken sufficient account of Ofcom's BCMR published in January 2008. The Court of Appeal ([2010] EWCA Civ 16) rejected this ground of appeal (Sedley LJ dissenting). Lloyd LJ said at [59]:

"The position advanced on behalf of Vtesse was not altogether clear, but it did at any rate proceed on the basis that it was possible, relevant and appropriate to disaggregate the BT assessment in order to identify the component attributable to the fibre optic element of the network and ascertain the unit of valuation of that element which went towards the overall assessment, and to take that as a proper comparison for the unit of

valuation applicable to Vtesse. Moreover, Mr Partridge [for Vtesse] put forward a specific devaluation on that basis. Although this underwent a degree of modification in the course of the proceedings, from the time when he put forward his expert evidence the case made on behalf of Vtesse was identifiable, both as to the possibility and utility of disaggregation, and as to how this was to be done. The Ofcom 2008 report was used to support, in a general way, the first proposition. It formed no part of the second aspect of the case made.

60. In those circumstances it seems to me that it is not correct to assert that the Ofcom report was a vital, a central or a significant element of the case, such that the Lands Tribunal was obliged to deal with it in the course of its decision.”

98. On the evidence before it the Court of Appeal found that the Tribunal had been entitled to reach the conclusion it did as a matter of valuation judgment. Vtesse’s expert (Mr Partridge) in *Bradford* disaggregated and devalued BT’s central list assessment to give a value of £19 per fibre pair kilometre, which, as the Court of Appeal noted, was not supported by the Ofcom 2008 report. The Tribunal said of this evidence at [76]:

“Both [Mr Bradford] and Mr Partridge agreed that Mr Partridge’s attempted deconstruction of BT’s assessment was unprecedented in rating history. We have no hesitation in concluding that the exercise which Mr Partridge has undertaken is wholly unreliable. We obtain no assistance from it.”

99. Mr Kolinsky QC acknowledged that the Court of Appeal decision in *Bradford* [2010] was not binding on the Tribunal in this appeal but he said that in upholding the Lands Tribunal’s decision the court had indicated the importance of considering the relevant evidence. The Lands Tribunal determined that to compare the hereditaments of BT and Vtesse and to attempt to disaggregate the R&E method used to value the BT hereditament was unsound valuation practice. The fundamental logic of that decision applied in the current appeal, he submitted.

100. In its 2008 BCMR Ofcom made a high-level comparison of the price of BT’s wholesale Ethernet services with Ofcom’s preliminary assessment of the fully attributed cost of delivering those services. Mr Kolinsky QC submitted that insofar as this exercise involved disaggregating the BT network, e.g. in determining per metre charges for backhaul (exchange building to exchange building) services, it was concerned with BT’s costs, not the disaggregation of its valuation as a prescribed central list hereditament.

***(b) Local loop unbundling***

101. In 2008 two statutory instruments were introduced to deal with the consequences of local loop unbundling (see paragraph 40 above). Local loops are the single pair of copper wires that connect a customer’s premises to the local telephone exchange through which the customer receives both telephone and broadband services. The unbundling of such loops refers to the grant of access to new entrants (“alternative operators”) to the existing telecommunications infrastructure of the incumbent operator, in this case BT, who was exercising SMP in this sector

of the market. Under regulation 8 of the Central Rating List (England) Regulations 2005 BT is treated as in occupation of a single hereditament comprising, among other things, all unbundled local loops. Regulation 8(3) provided that unbundled local loops would cease to form part of this prescribed hereditament on 1 April 2008 and therefore BT would cease to be treated as in occupation of them on that date. The Central Rating List (England) (Amendment) Regulations 2008 (SI 2008 No.429) omitted the said regulation 8(3) so that BT continued to be treated as being in occupation of all unbundled loops indefinitely, notwithstanding that these loops were in fact now used, i.e. occupied, by alternative operators.

102. Under regulation 3 of The Non-Domestic Rating (Communications Hereditaments) (Valuation, Alteration of Lists and Appeals and Material Day) (England) Regulations 2008 (SI 2008 No.2333) the letting or licensing by BT to any person of a fully unbundled local loop shall be assumed for the purpose of valuing the hereditament pursuant to paragraph 2(5) or (6) of Schedule 6 to the Local Government Finance Act 1988 to be a matter affecting the physical state or physical enjoyment of the hereditament; i.e. BT could in future make a proposal to alter its prescribed assessment on the grounds that there had been a material change of circumstances arising from local loop unbundling. This reflected the fact that BT was assumed to be in occupation of the unbundled loops even though these were now occupied by alternative operators.

103. Mr Larkins said that while BT lost the revenue from the unbundled loop it received instead a standard regulated charge, determined by Ofcom, from the alternative operator for continuing to maintain the local loop. Part of this regulated charge included an amount estimated by Ofcom to reflect the rates liability that remained with BT since it was deemed to be in occupation of the unbundled local loops under SI 2008 No.429 as part of its prescribed hereditament. The amount of the regulated charge for local loop unbundling was effectively a charge for the cost to BT of supplying the service to an alternative operator and included such items as a return on the cost of capital, maintenance, testing and sales, some of which related to non-rateable equipment and services, and services that were not linked to the prescribed hereditament. The loss of the loops required the reduced hereditament that remained with BT to be valued as a whole (by the R&E method) to reflect the consequential impact on costs and revenues. There was no simple mechanism to deduct an amount per unbundled loop. Mr Larkins said the regulated charge was therefore not equivalent to a rent determined under the statutory hypothesis and could not be used to determine the value of an unbundled local loop. This point was accepted by the EC in its decision dated 12 October 2006 at [156].

104. Mr Paul noted that the definition in *Bradford* of the “lighting” of fibre as giving rise to rateable occupation meant that unbundled local loops should be rated in the hands of the OCPs, since there was no difference between lighting a fibre and powering up a copper line: both operations involved connecting the line to equipment which supplied electromagnetic energy. It was the prospect of thereby creating millions of separate hereditaments that led to BT being kept in rateable occupation of unbundled local loops under SI 2008 No.429. Mr Paul also described the regulated rent for unbundled local loops as being like a tied (not a market) rent with an effective obligation to buy additional services from BT in order to use the loop.

105. Mr Paul analysed BT's rateable value in Annex 2 of his witness statement. This included an analysis of unbundled local loops and NGA, which is considered in the following section.

*(c) Next Generation Access*

106. The parties were also in dispute about the treatment of NGA lines in the assessment of BT's prescribed hereditament. NGA essentially refers to a range of technical changes to improve the speed, consistency and reliability of broadband. Foremost among these changes is the replacement of copper wires by optical fibre. There are two versions of NGA: fibre to the cabinet ("FTTC") in which fibre replaces copper wire from the telephone exchange to the street cabinet but not from the cabinet to the premises, and fibre to the premises ("FTTP") in which fibre entirely replaces copper wire between the exchange and the premises. The less copper wire, the faster the speed of transmission will be. Both FTTC and FTTP are commonly referred to as superfast broadband and are largely provided through BT Openreach and Virgin Media's cable network.

107. Mr Larkins said that at the AVD (1 April 2008) and compiled list date (1 April 2010) BT had negligible amounts of NGA local access fibre and by then the R&E model that formed the basis of BT's 2010 Central List assessment had already been finalised. Under these circumstances, said Mr Larkins, "It was agreed by all parties at that time" that the best way to reflect NGA would be to make an end adjustment for each FTTC/FTTP connection. The end adjustments were taken as £18 per connection for FTTC and £20 per connection for FTTP. These figures were based on limited evidence from the assessment of cable TV access networks. Mr Larkins said that the valuation considerations in adopting this approach were contained in the relevant VOA Guidance<sup>10</sup>.

108. The valuation guidance for NGA in the 2010 list<sup>11</sup> states that £20 is the proposed rateable value per home or SME<sup>12</sup> premises (less than 14% of total connections) connected in respect of urban and suburban mainly residential networks. The £20 figure "includes the backhaul to a local exchange ..., the street cabinets and the final customer connection, other than a BT local loop." Where the final connection from the cabinet was by an unbundled BT sub-loop, the proposed rateable value was £18 per connection. The guidance states this is because "BT retains the rates liability on the sub-loop." Large businesses were "to be considered on their individual merits".

109. Mr Paul said that local loops were replaced by NGA and that, according to data from Barclays Investment Bank, the number of FTTC and FTTP lines by March 2017 was 7,698,000 and 98,000 respectively. Valuing these at £18 (FTTC) and £20 (FTTP) gave a total rateable value for NGA of £140,524,000 for the UK. He apportioned this figure to England at 85% or £119,445,000 and deducted this value of NGA from the lowest rateable value for England in

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<sup>10</sup> VOA Rating Manual section 6 part 3; section 873: Tertiary Telecommunications Networks, section 6: Valuation Considerations.

<sup>11</sup> Ibid, section 7.

<sup>12</sup> Small or medium sized enterprise.

2016/17 which was £154,520,000. This gave £35,075,000 which he grossed up to £41,264,000 for the UK.

110. Mr Paul said it was generally accepted that there were some 25 million BT local loops in the UK. He deducted from this total the FTTC and FTTP numbers (7,796,000) to give a total of 17,204,000 local (copper) loops. Local loops were valued at the same amount whether bundled or unbundled as the rent was the same for internal or external use (by regulation) and the effect of unbundling was a diminution in trunk network value, not loop value, according to BT's Regulatory Financial Statements. Assuming the whole of the non-NGA rateable value of £41,264,000 was solely attributable to these local loops, Mr Paul said it represented a figure of £2.39 per line. If one assumed instead that the non-NGA was evenly split between the remaining assets (trunk network, fibre, operational buildings and local loops) this figure reduced to £0.60 per line. The corresponding figure for fibre, assuming no value was attributable to other assets, was £20.87 per km based upon a total of at least 1,977,146 km of fibre in use<sup>13</sup>. Assuming the residual (non-NGA) rateable value was evenly split between assets gave a value of £5.17 per km.

111. Mr Larkins said in his rebuttal report that the figures of £18 and £20 for FTTC and FTTP were not a disaggregation of the BT Central List valuation and did not represent the value in isolation of a NGA asset such as a length of fibre:

“The adjustment represents the net overall effect of the revenues and costs arising within the BT valuation due to the addition of a NGA customer subscription.”

### ***Competition Commission determination 1192/3/3/12***

112. On 7 March 2012 Ofcom published a statement entitled “Charge Control Review for LLU and WLR<sup>14</sup> Services”. The statement imposed charge controls on BT in relation to both types of service. Ofcom identified that Openreach<sup>15</sup> had SMP in both markets and that charge controls were necessary as a remedy to address Openreach's ability to fix or maintain prices at an excessively high level for those services. The charge controls set the prices that Openreach could charge OCPs (including other parts of BT) for LLU products and ancillary services.

113. Sky and TalkTalk jointly appealed to the Competition Appeals Tribunal on the ground, among others, that Ofcom had set price controls at an inappropriate level because it had erred in allocating cumulo rates<sup>16</sup> between different products using a method based on PWNRC. The essence of Sky/TalkTalk's appeal was that Ofcom's approach to allocating BT's cumulo rates costs did not reflect the causality of those costs since: (i) the VOA did not use net replacement costs; (ii) did not distinguish between individual products on the basis of relative profits; and (iii)

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<sup>13</sup> Derived from BT's Regulatory Financial Statements 2016/17 as shown in Annex 3 to Mr Paul's witness statement.

<sup>14</sup> Local Loop Unbundling and Wholesale Line Rental.

<sup>15</sup> Openreach is an operating division of BT functioning as a separate business responsible for managing BT's copper access network (local loop) and ensuring that alternative communication providers can access that network on an open and equal basis.

<sup>16</sup> i.e. the prescribed central list assessment.

was not sufficiently simple or transparent because it relied on BT's internal models. Sky/TalkTalk said the appropriate methodology for allocating such costs would be to seek to apply the principles of the aggregate calculation of BT Group's cumulo rates to individual products. They acknowledged that a full receipts and expenditure calculation, similar to that used by the VOA, had been impossible to replicate and had adopted what they called a "Proxy RV method" as a practical alternative methodology which they considered approximated this calculation.

114. Disputes about pricing matters are referred to the Competition Commission (now the CMA) to determine<sup>17</sup>. The Competition Commission issued their determination on 27 March 2013.

115. Ofcom argued that the Proxy RV method should produce results similar to those of the VOA's method, given that it sought to replicate them. But the published rateable value for BT's English assets at April 2010 (£244.46m) was a fraction of the amount calculated using the Proxy RV method. BT said that if it was accepted that the Proxy RV model was not a remotely good approximation of the VOA's approach, then the premise for Sky/TalkTalk's ground of appeal fell away.

116. The Competition Commission was concerned about the Proxy RV method's failure to even approximately replicate the results of the VOA's aggregate calculation. The Proxy RV method also failed, in disaggregating the VOA's calculation, to reconcile with the results of the VOA method, a fact which the Competition Commission considered undermined Sky/TalkTalk's claim to have produced a causal model<sup>18</sup>. The Commission said at 11.104:

"In our view, Sky/TalkTalk's method did not evidence that there was a suitable closer approximation to the VOA calculation that Ofcom could have used for allocating cumulo rates to products."

The Commission was not persuaded that the Proxy RV method offered the close approximation to the VOA's method that was claimed for it and found that Ofcom had not erred in allocating cumulo rates between different products using a method based on PWNRC.

117. Mr Larkins noted that Ofcom considered two alternative allocation methodologies to the PWNRC method that it adopted. The first was to look at net profit. It rejected this because it saw cumulo rates as a tax on rateable assets rather than profit. Allocating on the basis of profit could lead to costs being allocated to a product which made little or no use of rateable assets. The second alternative was to use the VOA's profit calculations. The CC said at 11.10(b):

"Ofcom saw these calculations as complex and hard to replicate. It said they were not feasible or appropriate to replicate for individual parts of BT for the purpose of allocation."

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<sup>17</sup> Section 193 of the Communications Act 2003 and rule 3(5) of the Competition Appeal Tribunal (Amendment and Communications Act Appeals) Rules 2004 (SI 2004 No. 2068).

<sup>17</sup> Paragraph 11.102.

118. Mr Larkins said that Ofcom, the professional representatives of Sky/TalkTalk and the Competition Commission had all recognised that it was not feasible to disaggregate an R&E valuation into its constituent parts. The VOA had emphasised this in correspondence to Vtesse dated 25 February 2014 in which it referred to the Commission determination in March 2013. The letter concluded:

“In summary, the Valuation Officer does not need to disaggregate to meet his valuation responsibility for this hereditament and the BT assessment is not and never has been, disaggregated by the VOA to determine rateable value by constituent elements. Significantly, the BT valuation is necessarily made using a receipts and expenditure approach and each physical element of the property is used for many service products, driving revenue and costs in variable proportions. Given the interrelated nature of property and product, disaggregation is neither realistically possible nor relevant to the rating valuation of BT.”

119. Mr Paul emphasised that “this allocation, disaggregation or apportionment” was necessary for BT’s product to be correctly priced to comply with EU competition law. PWNRC had been subject to a vigorous judicial process and it was not open to the VOA to dismiss it casually because it found it to be an inconvenience in this appeal. The Competition Commission found that PWNRC was preferable to the “proxy RV” because Ofcom said it satisfied the requirement for causality, it directly linked to BT’s Regulatory Financial Statements, was traceable and available and could be used consistently across all regulated products.

*(d) CMA determination 1259/3/3/16*

120. On 28 April 2016 Ofcom published details of, and gave effect to, a BCMR. As part of its review Ofcom proposed a remedy for Dark Fibre Access (“DFA”) which was based on passive access, i.e. a requirement that BT should offer its competitors access to the physical elements of its networks, such as underground ducts or optical fibres, without the associated electronic equipment.

121. Ofcom imposed obligations on BT in respect of the level of charges it could make for wholesale leased lines services in markets where it had SMP, such obligations being described as Leased Lines Charge Control (“LLCC”). The LLCC set the rule by which BT calculated the maximum charges it could impose for DFA. Ofcom set a cap for the price of DFA by reference to the price of comparable active (or “lit”) services<sup>19</sup>, less an amount calculated by BT using rules specified by Ofcom and referred to as the “Active Differential”. Ofcom described this price setting regime as an “active-minus” calculation. The calculation of the DFA cap therefore required two inputs: first, the price of the active reference product; and second, a calculation of the Active Differential. There were three components in the Active Differential: first, the costs avoided by BT when providing DFA, as opposed to an active service; second, the NDR

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<sup>19</sup> The price of BT’s wholesale Ethernet 1 Gbit/s leased line service.

associated with the corresponding active service; and, third, any objectively justifiable cost differences between dark fibre and the corresponding active service.

122. Ofcom noted that NDRs were different for BT than OCPs and that it was not straightforward to identify them on a like-for-like basis. Since BT and OCPs faced different NDRs, a measure of the Active Differential used in setting the DFA cap could have regard to either BT's or the OCPs' NDRs. If the difference between them was significant then the decision on whether to use an attribution of BT's or OCPs' NDRs could significantly change the effects of the DFA remedy. Ofcom recognised this difficulty and acknowledged that its objectives could be adversely affected by the NDR differential. In the absence at that time of any indication from the Government that it would change the system for calculating NDRs so as to remove this differential, Ofcom had to decide on the level of NDRs to be used in the Active Differential. It considered three options:

- (a) an attribution of BT's NDRs based on existing rules set by Ofcom;
- (b) an estimate of BT's incremental NDR costs assuming a move from active circuits to dark fibre, based on the VOA rules; and
- (c) a measure of access-seeker's (OCP) NDRs.

Ofcom rejected options (b) and (c). It said that identifying incremental NDR costs for BT "would be unlikely to be feasible as such a degree of disaggregation had proved difficult in the past."<sup>20</sup> It rejected option (c), among other reasons, because it might lead to unstable and unpredictable dark fibre prices and could result in a price that was below BT's costs of supply.

123. Ofcom therefore decided that the Active Differential to determine the DFA price should be based on an attribution of BT's NDRs (option (a)).

124. TalkTalk appealed to the CMA against Ofcom's decision to calculate the Active Differential using an attribution of BT's NDRs. TalkTalk said that Ofcom should have used instead a measure of OCPs' NDRs since, where dark fibre was provided to OCPs, it was OCPs, and not BT, that became liable to pay the NDRs on the circuit. TalkTalk estimated that it might pay NDRs between 11 and 35 times the attribution of BT's NDRs for 2014/15, depending on the characteristics of the circuit concerned.

125. Mr Duckworth gave evidence on behalf of TalkTalk at the CMA appeal and has adopted the same evidence on behalf of the appellant in this appeal. He said that an OCP which was equally as efficient as BT at providing active equipment would be materially worse off by taking

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<sup>20</sup> Final Statement Annex 23, paragraph A23.107.



up dark fibre rather than an active service, because it would face such a significantly higher NDR cost than BT's attributed NDR cost assumed in the Active Differential<sup>21</sup>.

126. The CMA concluded that:

(i) TalkTalk had demonstrated there was a material difference between the OCPs' NDRs and the attribution of BT's NDRs in respect of the majority of circuits (paragraph 4.77 of its Final Determination).

(ii) Ofcom's NDR approach would significantly reduce the take-up of DFA compared with a scenario in which there was no NDR differential or where the assumed levels of NDRs in the DFA price was significantly more reflective of OCPs' costs [4.103].

(iii) All or most OCPs would be at a significant commercial disadvantage because of higher NDRs resulting from the NDR differential [4.105]. The NDR differential resulted from the different approaches to rating BT as the incumbent network operator on the one hand and OCPs on the other [4.144].

(iv) Ofcom's NDR approach would significantly reduce the take-up of DFA compared with the case in which there was no NDR differential or where the DFA price assumed OCP NDRs which were significantly more reflective of OCPs' costs [4.150].

(v) Ofcom's response to a material NDR differential and the DFA price arising from its approach was not consistent with its objective to promote efficiency and to ensure a high level of take up of the DFA remedy [4.216 to 4.219].

(vi) Ofcom was wrong to decide that, in the absence of the Government changing the rating rules, the NDR costs adopted in calculating the Active Differential when deriving the price for DFA, should be based on an attribution of BT's NDR costs to the fibre (rather than on some other appropriate measure) [5.2].

127. Mr Paul said the CMA final determination made it clear that in respect of 2017 and onwards<sup>22</sup>, BT gained a substantial advantage through the rating system. He thought such an advantage existed previously since there had been no change in the approach to the assessment of BT's and OCPs' NDRs.

128. Mr Robinson thought there was unfairness in the way Centurylink Communications UK Limited's hereditament had been assessed compared to BT and said that the CMA final determination had shown for the first time public and compelling evidence that the NDR regime as applied to optical fibres distorted competition. He noted that the BT assessment was based on £18 per connection for FTTC. Given that the average FTTC connection was over 2 km Mr Robinson said that this part of BT's network was therefore assessed at less than £10 per km compared with Centurylink's average assessment of £40 per km for trunk and access networks.

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<sup>21</sup> Mr Duckworth's first expert witness statement at paragraphs 7.15 and 7.20; CMA Final Determination at paragraph 4.55.

<sup>22</sup> Ofcom's Final Statement came into effect from 1 October 2017.

129. Mr Larkins disagreed with Mr Paul and Mr Robinson and said that the CMA did not say there was unfairness in the rating system but had determined that an NDR differential existed. He noted that the CMA had said at [4.31] that both TalkTalk and BT had employed independent rating experts who had agreed with Ofcom's view that the cumulo assessment would be difficult to disaggregate and that the incremental NDRs associated with any switch to dark fibre could not be reliably calculated. At [4.32] the CMA said that as it was not feasible to allocate BT's NDR costs to individual products, the NDRs used for regulatory purposes were based on an *attribution* of the cumulo rates. Mr Larkins noted that the CMA also emphasised at [4.146] the problems caused by the NDR differential were specific to the case it was considering. An attribution of NDR was not equivalent to a disaggregation of value. The latter was not possible where the valuation was obtained by the R&E method since the value arose from the use of the whole hereditament, i.e. a top down approach. It was not a valuation that was built up from its component parts and therefore could not be disaggregated. BT's prescribed hereditament was unique in its scale, size and complexity and could not be compared with the hereditaments of other OCPs. There was no unfairness in valuing different hereditaments in different ways according to the best evidence available in each case.

130. Mr Larkins noted that the introduction of regulated BT dark fibre access was a continuing process. Ofcom had proposed further changes in its 2018/19 BCMR in which its original proposal was dropped and a charge based on a price per fibre kilometre proposed for the inter-exchange connectivity market only<sup>23</sup>. Mr Larkins said that this was not relevant to the AVD in this appeal.

*(e) Wavestream National*

131. On 6 October 2010 Ofcom published a consultation report on BT's request for an exemption for BT Global Services' Wavestream National product from the undertakings BT gave in 2005 to Ofcom under section 154 of the Enterprise Act 2002 (undertakings in lieu of market investigation references).

132. Wavestream National provides connectivity between two end user sites based on dense wavelength division multiplexing technology ("DWDM"). Each wavelength enables point-to-point transmission speeds of up to 10 Gbits/s and can carry multiple protocols. BT sold Wavestream National to large corporations for high bandwidth applications, including data centre connectivity, where demanding reliability and security requirements had to be met through the resilience and protection specification of the product. Wavestream National was therefore in competition with Vtesse for longer distance services.

133. Mr Paul said that the exemption, which Ofcom said it was minded to agree, meant that BT would not have to provide equivalence of inputs ("EOI") for this dedicated end-to-end service. EOI means that BT provides the same product or service (Wavestream National) to all communication providers (including BT) on the same timescales, terms and conditions

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<sup>23</sup> The connection between BT exchanges in different locations. The proposed maximum charge was £250 per km pa for a dual fibre circuit.

(including price and service levels) and by means of the same systems and processes. Mr Paul said that the EOI exemption meant that BT could supply other parts of BT with dark fibre on terms that were not available to other operators. He said that BT would only have requested this exemption if the resulting costs were below the regulated product cost, including rates. Other parts of BT could acquire and light dark fibre for non-regulated purposes but were not charged to rates on a comparable basis to Vtesse and other operators.

134. Mr Larkins noted that BT argued there was no evidence of a competitive problem in this market and BT itself faced a high degree of competition from eight OCPs on an unregulated basis. BT estimated its own share of the market was less than 30%. In its conclusion Ofcom did not find that BT had SMP in this sector. Mr Larkins said that BT's cumulo valuation inherently reflected the extent of regulation that the hypothetical tenant might reasonably anticipate across the full range of services that contributed revenue to the R&E valuation. Just because BT and Vtesse competed in the same market sector did not mean their respective hereditaments were comparable.

#### ***(f) Valuation treatment of Cable and Wireless UK***

135. Mr Paul referred to the VTE decision in *Cable and Wireless UK v Subacchi (VO)* (2014)<sup>24</sup> which he said introduced an important new concept in the valuation of networks. The Cable and Wireless network had a significant number of fibres (18) on the same trunk routes because they used old (non-rateable) equipment that could not support the very high capacities allowed by the modern industry standard ("MIS"), i.e. DWDM technology. The use of (non-rateable) MIS meant there was a substantially reduced need for fibre. Cable & Wireless did not install new equipment because of the operational impact that would have, but it argued that on the vacant and to let principle a hypothetical tenant fresh to the scene would have applied MIS to reduce the fibre count. The VTE determined that the rateable value should not reflect the total number of fibres actually lit but, in the case of the trunk network, should be limited to the lower number required using MIS. Mr Paul said that this decision was not appealed and was reflected in the VOA's Rating Manual<sup>25</sup>.

136. Mr Paul said Cable & Wireless would not actually have reduced the 18 fibres to two and therefore it was effectively receiving a rates discount by the VTE notionally shrinking the number of fibres actually in use.

137. Furthermore, said Mr Paul, Vtesse's traffic was such that on all but a few links it could easily have been carried by another operator. That would have been cheaper and because the other operator was in control of the trunk network with Vtesse only using a particular wavelength, Vtesse would have avoided the liability to rates. The precise fibre route that carried Vtesse's traffic was of no value to Vtesse. For instance, the link from Portsmouth routed along the south coast via Dorchester. There was no operational reason for that route, it just happened to be an accident of the choice of Cable and Wireless who owned it. Mr Paul said that by 2008

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<sup>24</sup> Appeal numbers 0002M58050/001N05 and 0002M58070/001N05.

<sup>25</sup> Rating Manual Section 6 Part 3; section 871: Telecommunications fibre optic networks.

Vtesse had no need for long distance fibre at all and were it not for operational constraints it would have used other operators' networks and reduced its own network by some 87%. It had already rationalised some of its fibre use, retiring links from Manchester to Scotland and to the continent.

138. Mr Cains said that Mr Paul had misinterpreted the *Subacchi* decision which had determined that all the fibre routes were to be valued (up to a cap on the number of MIS lit fibres) whether or not they were required by Cable and Wireless for their hypothetical MIS network. Nor did the *Subacchi* decision support Mr Paul's argument that there was no value in the precise route the fibre took. All the routes in *Subacchi* were agreed and ratified by the VTE on an amount per kilometre basis determined by the actual route lengths.

**(g) CityFibre**

139. In its statement of case the Appellant said that the VTE had erred by holding that the agreement reached between the VOA and CityFibre in respect of "Metro" dark fibre circuits, which made CityFibre the party in rateable occupation at a rateable value of £100 per fibre pair irrespective of distance, had no application to the assessment of Vtesse's long distance network circuits.

140. Mr Johnson explained that CityFibre operated two types of fibre services: (i) traditional dark fibre lets; and (ii) a relatively new type of open access (Metro) network. CityFibre's dark fibre lets were assessed to rates in the same way as other OCPs, i.e. by reference to rental evidence and the tone of the list. Exclusive occupation was granted to the lessee and rateable occupation therefore passed to the lessee.

141. Metro networks were open access networks within a town or city over which CityFibre allowed its customers to transmit data. Those customers did not have exclusive possession of the fibre. When a customer wanted to transmit data over a CityFibre Metro network a short piece of fibre was laid between the customer's premises and the network. The connecting fibre was under the customer's control and did not form part of CityFibre's occupation. The customer's fibre was connected to the network via an optical distribution frame under CityFibre's control. The connection between the customer's fibre and the network was made via a ceramic connector which very precisely aligned the two fibres but, said Mr Johnson, held them apart by 1mm. He said the two fibres were not physically joined and that the connector could be easily removed. The connection was therefore not permanent and the two strands of fibre were in separate ownership and occupation. In cross-examination Mr Johnson said that he had been told about the 1 mm gap by CityFibre's advisers, GVA Grimley, during meetings to explain CityFibre's business model. Mr Johnson said he verified the existence of a gap from a Fibre Optic Association paper.

142. The Metro fibre was lit by the customer and not by CityFibre. The data was transferred across the CityFibre Metro network between optical distribution points ("ODP"). The customer had no rights over the network between the ODPs and was not in exclusive occupation of any part of the network. The route of data transmission was not defined or guaranteed and could be

sent by CityFibre along any route within their Metro network over which they retained paramount control. The Metro networks were located in towns and cities and formed individual rating assessments with lengths of around 100 km. Unlike Vtesse they were not national networks and did not transmit such large volumes of data.

143. Mr Johnson explained there was no market evidence for Metro networks and therefore they were valued for rating purposes on a shortened R&E method based on the revenue generated by each connection. (There was insufficient data to enable a full R&E valuation to be undertaken.) CityFibre charge a price per connection to an end user which is not based on route length since the route is not fixed. At the Material Day the connections were predominantly commercial and, said Mr Johnson, were still in their infancy. CityFibre and the VOA reached an agreement that a percentage would apply to the connection price to calculate the rateable value of each connection. For the 2010 rating list this gave a figure of £100 per commercial connection and £8 per residential connection. Mr Johnson gave no details of the percentage adopted or the connection prices but said that a comparison had been made with full R&E valuations such as those used in the assessments of KCOM, BT and Virgin Media.

144. Mr Paul said the VOA had completely changed the interpretation of occupation in the case of CityFibre by moving the liability to rates to the owner and not the user of dark fibre. He thought this discriminated against Vtesse and OCPs. He denied there was a physical gap in the connection between the user's fibre and the CityFibre Metro network and he adduced a diagram showing how such a connector worked. The diagram was produced by OSF (Optical Fibre Solutions), part of Furukawa Electric Company. It showed that when the two cable ends are mated, the springs within the connectors act to apply compressive loads on spherically-polished ferrule end-faces, so the cores of fibres in opposing connectors physically contact, leaving no gap between the cores of fibres in mated connectors. The fibre was contiguous between the user and the Metro network and there was no discrete "break" to justify the VOA's decision that CityFibre, rather than their customer, was in rateable occupation. If it was accepted that a connector divided a network in the way suggested for CityFibre then Mr Paul said Vtesse's assessment should be reduced to nothing because, with some 1,000 to 1,500 connectors in Vtesse's network, it would be the owner (lessor) of the fibre that controlled the network and was therefore in rateable occupation rather than the user (lessee) who lit the fibre.

#### ***(h) Virgin Media***

145. Mr Cains said that Virgin Media was a large national network, which was valued overall on the R&E basis from information contained in its accounts. During cross-examination, Mr Cains said that the result of the R&E valuation for the whole of Virgin Media was £100m. Of this amount approximately £2m was the value of its trunk fibre network, as described in Mr Cains' evidence. It was valued by reference to direct rental comparables and was agreed between the VOA and Virgin's advisers, GVA. The settlement was reached on the basis that a fibre pair (4,839 km) was valued at £250 per km. The balance of £98m included approximately £1.9m for the buildings and plant and machinery associated with the trunk network with the remaining £96m or so being the assessment of the remainder, including Virgin's local access networks. Unlike BT, the Virgin Media hereditament was not a single prescribed hereditament and did not appear in the central rating list. Its local access network assessment was split into 66 separate

entries corresponding to the relevant billing authorities. The assessment was apportioned by reference to the number of premises passed in each authority area and not by route kilometres, as these were said to be unknown.

146. In cross-examination Mr Larkins was asked why, if it was possible to disaggregate the value of Virgin Media's trunk network from the overall result of an R&E valuation, it was not possible to do the same in respect of BT. Mr Larkins said it would be "possible to force a mathematical solution" but that it would not be a reliable or meaningful indicator of value. With a total of 18,000,000 km of fibre, BT was "vastly different" in scale and diversity (with 590 different types of service in numerous sectors) to Virgin Media. "Highly subjective" adjustments would be required and although "hypothetically you could do the same with BT as you do with Virgin Media, ...BT isn't comparable."

147. Mr Larkins agreed that BT, by taking leases of lengths of dark fibre, had helped to set the tone of the list upon which the Respondent relied to value Vtesse and he accepted that this evidence had not informed the valuation of BT's fibre trunk network.

*(i) New regulations*

148. The Telecommunications Infrastructure (Relief from Non-Domestic Rates) Act 2018 together with The Non-Domestic Rating (Telecommunications Infrastructure Relief) (England) Regulations 2018 (SI 2018 No.425) put into effect<sup>26</sup> an announcement made in the Autumn Statement of 2016 that the Government intended to provide 100% rates relief for the installation of new optical fibre for five years from 1 April 2017.

149. This was to be achieved by introducing a new term "T" into the formula for calculating the chargeable amount. "T" was defined as  $1 - (CRV/RV)$ , where CRV is the proportion of the rateable value (RV) in the central list certified by the VO in accordance with regulation 6(2), i.e. the VO must certify the proportion of the rateable value shown in the central list which appears to the VO to be:

- “(a) new fibre;
- (b) any plant and machinery used or intended to be used in connection with the new fibre; and
- (c) the proportion of the hereditament which is exclusively occupied by (a) or (b).”

150. Mr Paul said the 2018 Act and Regulations required the VO to identify those parts of the BT fibre network built and used after 1 April 2017 and to assign a value to them. He said that, in order to comply with regulation 6, the VO would have to separate the assessment in the relevant year between fibre and non-fibre values. Mr Paul considered this to be an exercise in breaking

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<sup>26</sup> By the insertion of section 54ZA into the Local Government Finance Act 1988.

down the hereditament into its constituent parts, i.e. the disaggregation of BT assets for rating purposes, a task which the VO had consistently maintained was impossible.

151. Mr Larkins referred to the Department for Communities and Local Government's Consultation on the Draft Regulations dated August 2017. This stated:

“12. Determining the rateable value of the fibre eligible for relief will be a new exercise and require the Valuation Office Agency to make subjective estimates beyond the data which is already held for the existing valuation. In particular, for some telecom networks the courts have recognised that rateable values should be set using the receipts and expenditure method of valuation. This method examines the trading position of the hereditament as a whole and does not within the evaluation identify the value of any constituent part of the hereditament.

13. Having regard to these considerations and the challenges in assessing the rateable value of only part of a single telecommunication network, the Government considers that it will not be appropriate to base the relief upon the rateable value of the new fibre as if that fibre were a separate assessment. Instead, the Government believes that the relief should be based upon the opinion of the Valuation Officer as to how much of the rateable value of the whole network is attributable to the new fibre.

14. Therefore, the draft regulations adopt as the measure for the relief the proportion of the rateable value shown for the hereditament which appears to the Valuation Officer to be attributable to the part of the hereditament covering the new fibre and associated plant and machinery...”

152. Mr Larkins said it was the duty of the VO under the 2018 regulations to form an opinion about the proportion of the rateable value of the hereditament (whether on a local list or the central list) that “relates to” new fibre. He said the VO might be able to form an objective opinion where an aggregated (bottom up) valuation had been undertaken using the direct rental comparison method. This would allow fibre to be disaggregated based on length and rateable value per fibre kilometre. However, “there is a clear recognition that for Receipts and Expenditure valuations the VO's opinion of the relevant proportion will be subjective.”

153. Mr Kolinsky submitted that since the 2018 Act and regulations only applied to new fibre, i.e. since 1 April 2017, it had no relevance to the AVD in the appeal. No decisions on the method of apportionment had yet been made and the VO in each case would have to make a subjective judgment.

### ***(3) Buildings and plant and machinery***

154. There was no dispute about the identity or description of the buildings and plant and machinery occupied by Vtesse. The two main buildings were the headquarters building in Unit B, Foxholes Business Park, Hertfordshire and a data centre in Hoddesdon, Hertfordshire. There were also some minor buildings, i.e. small cabins used for repeating/amplifying signals along the fibre network. Rateable plant and machinery was identified in accordance with the Valuation for

Rating (Plant and Machinery) (England) Regulations 2000 (SI 2000 No.540). Such plant and machinery was all located in the two main buildings.

155. The buildings were valued by Mr Cains using direct rental comparables and settlement evidence with a 10% end allowance being made to reflect the management of a geographically dispersed estate. The plant and machinery was valued using figures from the 2010 rating list VOA Costs Guide and the statutory decapitalisation rate of 5%. Mr Cains estimated the rateable value of the buildings at £150,861 and that of the plant and machinery at £15,726, making a total of £166,587.

156. In its statement of case Vtesse adopted this figure and discounted it by 50%. In cross-examination and in answer to questions from the Tribunal, Mr Paul said this discount reflected the lower value of BT's operational properties, i.e. exchanges forming part of the prescribed hereditament included within the R&E valuation, compared to that of Vtesse's equivalent property, i.e. its data centre, which was valued at a higher rate using the direct rental comparables method despite fulfilling the same function. Mr Paul said that the discount was "shorthand for saying this is not what [BT] is charged for a telephone exchange."

157. Mr Paul supported this adjustment in Annex 2 of his witness statement where he analysed BT's operational buildings. He estimated BT to have 5,581 such properties measuring 4 million m<sup>2</sup> in total. Taking the figure of £41,264,000 as BT's non-NGA rateable value (see [108-109] above) he calculated the average value of this floorspace at £10.32 per m<sup>2</sup> (assuming no value was attributable to the trunk network, fibre or local loops). This compared with Mr Cains' valuation of Unit B, Foxholes Business Park at £65 per m<sup>2</sup> and the data centre at Hoddesdon at £78 per m<sup>2</sup> overall.

#### *(4) Discussion and factual conclusions*

158. We agree with Mr Cains that the letting from Geo to Vtesse at £250 per route km for a fibre pair is strong evidence of value at the AVD. The route length of this letting was 2,164.71 km<sup>27</sup> or 28.6% of the total length of the Vtesse network at the AVD. It is possible that the rent per kilometre would be different for a longer route length; the usual valuation adjustment is a discount for larger hereditaments (quantum). This possibility is not supported by the largest letting in the evidence; the letting (without a premium) from Virgin Media to EE in December 2011 of 7,083 km at £546 per km. The remainder of the comparable letting transactions took place over a long period of time either side of the AVD, for widely different (relatively short) lengths of fibre pairs, for different terms and often (in six of the 16 transactions) involved the payment of a capital sum for fibre, the analysis of which was not explained. We think Mr Cains overstates his case by saying the totality of the rental evidence supports his adopted figure of £250 per km. There is certainly some good rental evidence for it, and it sits comfortably within a

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<sup>27</sup> The letting included the "Northern Ring" of 701.5 km. So the letting was £541,177/(1,463.21 km + 701.5 km) = £250 per km.



range of values<sup>28</sup> and is less than the average of £306 per km<sup>29</sup>, but the rental evidence does not point conclusively towards it.

159. But there is strong evidence of a settled tone of the list for national networks based on a value per fibre pair of £250 per km, for both compiled list assessments and subsequent appeals arising from material changes of circumstance. We are satisfied that the combined rental and settlement evidence supports the respondent's adopted figure of £250 per km for a fibre pair.

160. There is no dispute in terms about Mr Cains' valuation of the buildings and plant and machinery comprised in the hereditament. The adopted values are not challenged as to their accuracy, only as to their application. Mr Paul says that BT is only paying 50% of this value for its equivalent buildings, i.e. BT's exchanges compared to Vtesse's data centre, and for its plant and machinery. (In fact, Mr Paul's analysis - see [157] above - suggests that BT was paying considerably less than 50%.) The valuation dispute is therefore not so much one about the absolute accuracy of the rateable value of the Vtesse hereditament as one about its relative accuracy compared with that of BT. In a sense it does not matter to the Appellant whether Vtesse's hereditament is valued at the figures Mr Paul attributes to BT's equivalent facilities (and which forms the basis of the appellant's contended rateable value of £234,637) or whether those equivalent facilities are valued at the same figure as those of OCPs (£250 per km per fibre pair), provided, for the purposes of competing in the same market sector, Vtesse and BT are on a level rating playing field. But this approach assumes that the two hereditaments are comparable, and they are not.

161. Vtesse's hereditament is included in the local non-domestic rating list and is narrowly defined as its fibre network, buildings, and plant and machinery. Although such items also form part of BT's hereditament and are occupied in competition with Vtesse's services, they are only a small part of BT's prescribed central list hereditament. In seeking to disaggregate the value of BT's equivalent fibre network from its cumulo assessment the appellant is assuming that a hypothetical tenant would pay the same rent as Vtesse, i.e. £250 per km per fibre pair, as it would to occupy that network as part of BT's whole undertaking, which is orders of magnitude larger and more diverse than that of Vtesse (see [83] above). BT's prescribed hereditament cannot be valued as the aggregated sum of its parts and attempts to isolate the value of its fibre network have been unsuccessful, e.g. in *Bradford* (see [95-97] above). It is most sensibly valued, as a whole, by the R&E method, albeit Mr Paul thought the contractor's basis could also be used (although the same problems of disaggregation would still exist if that were done). It should not be assumed that the value of BT's fibre network is constant regardless of the context of the valuation.

162. Conversely there is no reason in domestic law and practice why the Vtesse hereditament should be valued on a R&E or contractor's basis, given the strong market rental evidence and settlement tone for the letting of fibre networks and associated buildings, plant and machinery where these are to be valued as an independent, locally listed, hereditament. Direct rental

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<sup>28</sup> £180 to £546 per km for the comparables that did not have a capital payment for fibre and excluding the outlier at £640 per km for which only basic details were known.

<sup>29</sup> *Ibid.*

comparison is the preferred valuation method because it closely aligns with the statutory rating hypothesis and is a more direct and straightforward approach which does not depend on the more complex assumptions of the other two methods.

163. The Appellant argues that if it is possible to disaggregate the value of the Virgin Media fibre network from the total value of its rateable assets as calculated by the R&E method, it should be possible to do the same for BT. Mr Larkins said that although it would be possible to do this mathematically, it would require highly subjective adjustments. We do not doubt that this is the case, but it is not to the point. Virgin Media does not have a prescribed hereditament; it has 67 hereditaments, each of which *must* be valued separately. That is not the case with BT's prescribed hereditament which *must* be valued as a whole. This is done in practice by using the R&E method, which is correctly described as a "top down" approach. This does not depend upon the summation of the values of the constituent parts of the hereditament and to isolate the value of BT's fibre network using direct rental comparison would potentially lead to distortions in the value of its remaining operational assets. There is a single value for BT's prescribed hereditament – the value of BT's fibre network, included as part of this single hereditament, cannot be disaggregated from it. There is no justification for the VO to undertake a direct rental comparison valuation of BT's fibre network, even if this could be accurately identified and the practical difficulties described by Mr Larkins could be overcome, because it would make no difference to the valuation of the BT hereditament as a whole and it would have no other statutory purpose.

164. This distinction between the Vtesse and BT hereditaments has been recognised many times by courts, tribunals and regulators in recent years, both domestic and European. These decisions have been described at length above and none of them supports the contention that the two hereditaments are comparable. They are not comparable and there is no evidence to support the argument that they should properly be valued by the same method; on the contrary, Vtesse is properly valued by the direct rental comparison method and BT by the R&E method, given the very substantial differences between the hereditaments that we have summarised in detail above.

165. We are satisfied that the Respondent's submissions on this issue are correct and that to try and disaggregate the R&E method in order to ascribe a value to that part of BT's prescribed hereditament which aligns with Vtesse's hereditament is wrong in principle and represents unsound valuation practice. We agree with Mr Larkins that it could not be done in such a way as to provide any reliable value that could safely be used as a means of valuing the Vtesse hereditament.

166. Given the impossibility of disaggregating the value of the BT fibre network as a valuation exercise, regulators have imposed a proxy for it by attributing costs to individual parts of BT's undertaking, e.g. the regulated charge for LLU which the EC Commission accepted was not equivalent to a rent determined under the statutory rating hypothesis; or the adjustment for NGA based on charges for FTTC and FTTP which were not discrete calculations of the value in isolation of a length of fibre but which reflected the net overall effect on BT's revenues and costs arising from the addition of an NGA customer subscription.

167. The 2012 Competition Commission determination found a proxy rateable value method had failed to approximate the allocation of BT's cumulo rates to different products more closely than did Ofcom's use of PWNRC.

168. The 2016 CMA determination recognised there was a material differential between the NDRs paid by BT and OCPs and that this needed to be reflected in the calculation of the Active Differential. The CMA rejected Ofcom's attribution approach under its existing rules, which it considered would not be consistent with Ofcom's objectives. But the recognition of such a material differential and the CMA's rejection of Ofcom's decision to calculate the Active Differential by reference to an attribution of BT's NDR costs is not an endorsement of the view that BT's fibre network can be separately valued by reference to the rating assessment of OCPs using direct rental comparison.

169. Nor, in our opinion, is the appellant assisted by the evidence concerning Wavestream National, Cable & Wireless UK, CityFibre or the introduction in 2018 of regulations concerning new fibre.

170. Wavestream National concerned a dispute about EOI and does not inform the question of how to value BT's fibre network.

171. Cable & Wireless UK concerned the rating assessment of multi-fibre trunk routes where the MIS DWDM technology rendered most of such fibres redundant. Mr Paul's primary objection was to the effective rates discount said to be received by Cable & Wireless UK as a result, but this does not sound with the valuation issues in this appeal. The fact that by 2008 Vtesse had no need for long distance fibre at all and, absent operational constraints, could have reduced its network length by 87% is not to the point; at the material day its fibre network comprised the agreed length of 7,567.16 route km of fibre pairs and it was valued accordingly.

172. Mr Paul's main point about CityFibre was that there was no gap of 1mm between fibres in the connectors employed to join the user to the Metro network. The fibre was therefore contiguous which meant there was no justification for the VOA's view that the owner (lessor) rather than the customer (lessee) of the fibre was in occupation of it. But the VOA's argument rested also upon there being no exclusive occupation by the lessee of any particular fibre route and this point alone would justify the decision that it is the owner of the fibre, rather than the lessee, who is in rateable occupation of it.

173. The 2018 regulations require the VO to certify the proportion of the rateable value in the central list which appears to be new fibre. That apportionment does not require new fibre to be valued as though it was a separate assessment and the regulations do not lend support to the Appellant's case. It requires a subjective apportionment of the value depending on the relative amount of new fibre.

174. In any event, none of these factors would have been known to the market at the AVD and so would have been of no relevance at that time. They are, in truth, relevant to Vtesse's complaint about differential treatment and not relevant to valuation as such.

175. The buildings, plant and machinery forming part of Vtesse's hereditament have been valued by the Respondent on a conventional direct rental comparison basis and by reference to standard costs and discount rates respectively. There is no challenge to the accuracy of these valuations, only to the perceived discrepancy between their result and that of BT's equivalent operational buildings, plant and machinery which Mr Paul says are included in the central list at 50% of the Vtesse figures, albeit his analysis (which is based upon vague generalised assumptions) shows a much lower figure. BT's operational estate is valued as an integral part of its whole undertaking on the R&E basis and not as individual hereditaments. Since the creation of BT Openreach non-operational BT buildings are not included in the regulated financial statements and therefore there is no need to deduct their rateable value from the result of the R&E valuation. Such non-operational buildings are valued as separate hereditaments.

176. As summarised in paras 82-85 above, the undertakings of Vtesse and BT as a whole are not comparable either in size or in terms of the variety of services provided. BT's undertaking involves the use of a long-distance twin fibre backbone to its network, in part for purposes of the same kind as Vtesse's use of its long-distance fibre network, but there the similarity ends. BT and Vtesse could be said at the time to compete for the limited business services that Vtesse provided, but not otherwise.

177. We are satisfied that the Respondent has correctly valued the Vtesse hereditament in accordance with conventional valuation principles. The Appellant does not challenge this valuation in terms; instead it seeks parity with BT on a like for like basis. Vtesse's concern is that the two operators should be treated the same for the assessment of NDR in respect of market sectors where they compete directly. The Appellant considers that by being valued as a single hereditament on the R&E method BT gains a competitive advantage. That perceived discrepancy can be resolved either by valuing BT's fibre network at £250 per route km for a fibre pair or, as the Appellant seeks, by reducing Vtesse's rateable value in line with the basis upon which the BT fibre network has been assessed by Mr Paul by an attribution of cost. Neither approach is justified in our view. The Vtesse and BT hereditaments have been fairly and properly valued on their own terms but, necessarily, by different valuation methods. That is because the hereditaments are fundamentally distinct. The mode and category of occupation of the Vtesse hereditament is but a subset of the mode and category of occupation of the BT hereditament, which must be valued as a whole and which is orders of magnitude larger in scale and diversity.

178. It would be contrary to valuation principle to value the Vtesse hereditament by taking an attributed cost of BT's long distance fibre network for part only of the use of that network by BT within its incomparably greater undertaking, and then using that attributed cost as evidence of the value of Vtesse's hereditament. That would be contrary to the statutory rating hypothesis; contrary to the reality principle that the subject hereditament should be valued as *it* stands on the valuation date; contrary to all professional guidance about what amounts to good evidence of rental value and the hierarchy of such evidence; contrary to basic principles of comparing like

with like but not like with unlike; and it confuses the fundamentally different concepts of cost and value. It would be unjustifiable, as a matter of valuation practice, fact and domestic law, to seek to value Vtesse's hereditament by attributing a cost to part of BT's business and then transferring that cost without adjustment and using it to value a very different network.

179. We therefore dismiss the appeal made on the grounds of errors of fact.

180. We must now consider whether, as a matter of EU law, a different value must be entered in the valuation list as the value of Vtesse's hereditament.

### **Legal conclusions**

181. The Appellant's case is essentially a simple one. It is that there is a requirement under EU competition law for a Member State (as the United Kingdom was at the relevant times) to treat undertakings competing in the electronic communications market in an equal, non-discriminatory way, so as to facilitate fair and undistorted competition between them. This prevents the VOA from valuing one undertaking's network on one basis and another undertaking's network on a different basis, unless the difference can be justified by the VOA as being proportionate to ensuring and achieving fairer competition between them. Further, any such justification must be transparent.

182. The Appellant says that it is being treated differently, without any transparent justification, by having its network valued for NDR purposes in one way, whereas BT has its network valued in a different way. The consequence is that it is being discriminated against because its rates liability is unjustifiably substantially higher per kilometre of long distance twin fibre than BT's liability. The tax treatment is also alleged to be contrary to the principle of fiscal neutrality, in that similar factual situations are not being subjected to tax in the same way and on the same basis.

183. The Appellant contends that, even though such differential treatment may be justified as a matter of valuation principle and domestic law, as we have found, on the basis of the difference between the respective hereditaments, it cannot be justified under EU law because NDR charged on networks like that of Vtesse are, for the purposes of EU law, to be treated as taxation on the provision of services. That is because, it says, electronic communications operators only "occupy" fibres, and so become liable to NDR, if they have exclusive control of the fibres and pass electronic pulses down them, which is precisely the activity that amounts to the provision of a service by an undertaking. The tax therefore being in substance, under EU law, a tax on services, there is no justification for differential treatment of competitors in the method of calculating the tax, nor any justification for calculating the tax based on the length of the network, which reflects the distance between a provider in a Member State and the customer. Further, the Appellant contends, not all providers of the same service are taxed on the basis of their deemed "occupation" of the lit fibres, so there too there is discriminatory treatment between competitors in the same market.

184. The Appellant contends that important questions of EU law arise, which need to be decided by this tribunal in order to determine the appeal, and on which there is no precedent or clarity under EU law. Accordingly, it submits that the tribunal should refer the following questions (using its formulation and emphasis) to the CJEU for authoritative determination before issuing a decision on the appeal:

- a. Given that the “event” which triggers the Appellant’s liability for NDR is its “lighting” or “data activation” of optical fibres leased or owned by it - this lighting being necessary to allow it to provide its electronic communications services to its customers - does this mean that, as a matter of EU law, the NDR at issue in this case is to be classified and treated for the purposes of EU law as a tax on the appellant’s provision of electronic communication *services*?
- b. Is the differential treatment by the VOA among electronic communications providers as regards the triggering event for their *liability* for NDR (with some electronic communications providers - including the Appellant - incurring such liability when they “light” optical fibres while for others, such as BT, the lighting of optical fibres does not trigger any NDR liability) permitted under EU law?
- c. Is the different *methodology* adopted by the VOA among electronic communications providers as regards the manner in which their liability for NDR is *quantified* - in that for some electronic communications providers, such as the Appellant, the VOA quantification is undertaken by reference to its “valuation” of the individual optical fibre assets actually lit by the Appellant; whereas for other electronic communications providers, notably BT, the VOA does *not* carry out a valuation for the individual fibre assets used or owned by it and instead makes a cumulative estimate of the total rateable operational assets of the provider, without disaggregating this cumulative valuation down to individual assets - permitted under EU law?
- d. Does EU law permit the quantification of the Appellant’s NDR liability to be calculated by the VOA on the basis of the *length* of fibre-optic cable which is used by the Appellant to provide its electronic communications services to its customers, (thereby making the calculation of NDR tax due dependent upon the distance between the location of the relevant fixed assets of the Appellant and the location of the customers’ premises to which it supplies economic communication services)?
- e. On the basis that the evidence shows that use of the buildings/fixed assets occupied by the Appellant is inextricably linked to (because wholly necessary for) the provision of its electronic communications services along the optical fibres which it leased, does the proportion of NDR which is assessed by the VOA as referable to the heritable property and fixed assets (in the form of buildings and street cabinets) which the Appellant occupied for the purposes of providing its electronic communications services to its customers also fall to be assessed for

its compatibility with EU law (including, among other things, the EU law general principles of equal treatment, fiscal neutrality, fair competition and transparency)?

185. From this brief summary of the Appellant's case and the wording of the questions for referral, it is evident that the Appellant's case, based on EU law principles, has relatively little engagement with the facts that the tribunal has found. The essential facts, so far as the Appellant is concerned, are (a) that BT and Vtesse are both electronic communications providers, (b) both have long distance twin fibre networks, but (c) a different method of valuation of the network is used in the case of each of them. The rest is a matter of EU law. Mr O'Neill, when the tribunal put this summary to him, did not dissent. He said that all the other facts are "normative" facts, and that historical reasons for the difference in treatment of BT (as a former monopoly provider) and Vtesse (as a new competitor) are no justification for the difference.

186. Mr O'Neill further accepted that his first question is a "gateway" issue, following which the other questions arise. So far as this first question is concerned, it is not quite correct to say that the "lighting" of the optical fibres that form the network is identical with the provision of services. As set out in para 35 above, in para 38 of his decision in *Bradford (Valuation Officer) v Vtesse Networks Limited* [2006] RA 57, the President, George Bartlett QC, found that the "lighting" (which gave rise to NDR liability) took place when Vtesse connected its equipment to either end of the fibre, generating a laser pulse at one end that could be received at the other end. That is not the same as the transmission of data to a customer.

187. The tribunal asked Mr O'Neill whether there was really any difference between an electronic services provider leasing fibres and connecting its equipment, to be ready to transmit a customer's data, and a professional services firm leasing offices and fitting them out, in order to be ready to receive customers. His answer was that there was an inextricable linkage between occupation of the fibre and provision of services: the fibre and the connection is essential for an electronic communications provider to provide services; an office is not necessary for a solicitor or accountant to provide professional services.

188. We accept that there is a more immediate connection between occupation of the fibre and the provision of electronic communications services, and that it could therefore be said that rateable occupation of the network is inextricably connected with the provision of electronic communications services. We can see, therefore, that the first question is a relevant question, though the appellant does not argue that NDR are linked to the rights mentioned in Article 13 of the Authorisation Directive. That being so they are not to be treated as a fee for the right to install facilities on, over or under public or private property within that Article, where such a fee is required to be "objectively justified, transparent, non-discriminatory and proportionate in relation to its intended purpose". Nevertheless, Mr O'Neill submits that the application of EU competition law to NDR in the cases of providers of long distance twin fibre networks means that the VOA either has to value the hereditaments of competing providers in the same way or be able to justify a difference in approach. Mr Kolinsky accepts that the principles of EU competition law apply but says that a different method of valuation is justified by the difference in the hereditaments.

189. We accept that the first question is a question of EU law the answer to which cannot be described as *acte clair*. If the Appellant were to succeed on the “gateway” question, the application of EU law means that the VOA must not discriminate in the valuation of providers’ hereditaments in an unjustified way. In Case C-390/06 *Nuova Agricast* [2008] ECR I-2577 at [66], the Grand Chamber stated:

“the principle of equal treatment requires that comparable situations must not be treated differently and that different situations must not be treated in the same way unless such treatment is objectively justified”.

Treating different cases differently is no breach of the principle of equal treatment; indeed, it would be a breach of EU law to treat them alike, unless that were objectively justified in a particular case. The relevant question is: by what criteria is difference or similarity is to be assessed in a case of this nature? For cases to have to be treated alike, is it sufficient that the occupiers of two different hereditaments are both providers of electronic communications services?; or must there also be similarity in the characteristics of the hereditaments? The Appellant’s case is that it suffices that it and BT are both electronic communications providers and that a component part of BT’s hereditament is the same as or similar to Vtesse’s hereditament.

190. It seems to us that, even if one accepts the applicability of the principles of non-discrimination, on the basis that EU law would regard the NDR levied on BT and Vtesse as a tax on the provision of services, the necessary next step when addressing comparability and equal treatment is to recognise the nature and purpose of the fiscal measure. NDR are a tax triggered by the occupation of business property where the amount of the tax depends on the value of the property:

“The comparability of the situations must be determined and assessed in particular in the light of the subject matter and purposes of the measure in question. The principles and the objectives of the field to which the act relates must also be taken into account ...”  
(Case C-112/16 *Persidera SpA* EU:C:2017:597 at [46])

The criterion of difference or similarity that is fundamental to NDR is the identity and characteristics of the property itself, not the occupier, even though specialist property may only be occupied by certain types of business. In other words, in the context of NDR, it cannot be sufficient - for EU law purposes - to use as the criterion of similarity or difference the fact that the rateable occupiers are competitors in the electronic communications market. Nor is it sufficient to identify the extent to which their businesses overlap. Even Vtesse accepts that its liability should be derived from the value of part of BT’s hereditament, not the value of BT’s business or its own business. Its argument is that the same value of a component of BT’s hereditament must be applied to its hereditament as is applied to BT’s.

191. However, the basis of valuation is the same for all business property: it is specified by para 2 of Schedule 6 to the Local Government Finance Act 1988. It is the rent that would be agreed on the open market between a hypothetical landlord and a hypothetical tenant for the hereditament on the basis of a tenancy from year to year with a reasonable prospect of



continuance. The amount of the value depends on the characteristics of the occupied property itself and the market for such property at the valuation date. As explained in paras 67 and 68 above, the right valuation method to use in any given case depends on the characteristics of the property and any market for such property at the valuation date. The requirement to treat different cases differently and similar cases alike therefore has to be assessed against the characteristics of the property itself, not just the business of the occupier.

192. We have explained in paras 67-69 above the different methods that are used to value property and why they should arrive at the same result for a given hereditament. Which method to use depends on the nature of the property and the judgment of the valuer, but the choice of method should not affect the value. BT's hereditament, being an enormous collection of disparate property associated with its particular business, cannot be valued on the basis of comparable properties because there are no comparables and there is no market for such a vast collection of property. Vtesse's network is much smaller and there is an active market for such property and a large number of transactions or settlements that establish a general tone of value. Vtesse's hereditament could be valued using an R&E method (though Vtesse has not pursued a valuation of its own hereditament using that method – it says that a value derived from BT's valuation should be applied to its hereditament) but the better approach – because more reliable given the amount of market evidence – is the comparative method. If two hereditaments were very similar, then on general valuation principles and (if it applies) under EU law principles of equal treatment it might be unjustifiable to value them using a different method. But that conclusion cannot apply if the properties to be valued are entirely different in character and extent. For reasons that we have explained when reaching our conclusions of fact, Vtesse's hereditament and BT's single cumulo hereditament are simply not comparable.

193. In any event, Vtesse's case is not simply (as it might have been) that its hereditament should also be valued using an R&E method. It is that a value attached to a component part of BT's hereditament, by a process of disaggregation or attribution, should be extracted and applied to its own hereditament to value it. That approach is nothing to do with non-discrimination; it is just an invalid approach to valuation, as we explained in para [178] above.

194. Accordingly, if we were to refer the first question to the CJEU and Vtesse succeeded in persuading that court that the answer to the question is that, for EU law purposes, the NDR are to be classified as a tax on the provision of electronic communication services, the answer seems to us to get Vtesse nowhere. It simply imports into the process of valuing Vtesse's long distance twin-fibre network principles of equal treatment that are already inherent in the valuation approach and in domestic law, as the Court of Appeal explained in its judgment on Vtesse's appeal over 10 years ago: see para [46] above.

195. The answer to the third question that Vtesse wishes to refer is, plainly, that a different method of reaching the annual letting value of a different hereditament is permitted (indeed required) under both domestic and EU law if the hereditament is so different in character and extent that the same method of valuation cannot, or cannot sensibly and reliably, be applied. The fact that BT's hereditament is wholly different in scale and character from Vtesse's hereditament means that it would be wrong to treat them alike, in selecting the best method of valuation. Even if they were valued using the same method, the same unit value would not apply to both since the

much larger hereditament for which there is no market will inevitably attract a sizeable quantum discount. However, importantly, the two hereditaments *are* treated alike so far as the basis of valuation is concerned: para 2 of Schedule 6 to the 1988 Act applies to all non-domestic hereditaments for rating purposes. It is only the selected method of valuation that differs.

196. So far as the second question is concerned, this is irrelevant to a decision on the annual letting value of the Vtesse hereditament on the AVD. There is no appeal against liability of the Vtesse hereditament to NDR. The only issue on appeal is value. The answer to this question therefore is unnecessary to enable the tribunal to give judgment on this appeal and so no reference to the CJEU can properly be made under the terms of article 267 TFEU.

197. The fourth question is conceptually interesting but, again, it does not arise on this appeal. Vtesse seeks to have a rate per kilometre of fibre applied to calculate the rateable value of its hereditament on the AVD. That rate is £20, which Mr Paul explains he derived from an attempt to disaggregate the BT valuation. Vtesse puts forward no other basis of valuation: it has declined the tribunal's invitation to put forward its own R&E valuation. In any event, the use of a rate per kilometre is fully justified by the market evidence. It is how electronic communications providers (including Vtesse itself) negotiate leases of long distance twin fibre. It is therefore the best evidence of how rental value is established in accordance with the statutory basis of valuation.

198. The fifth question is whether the valuation of Vtesse's fixed assets and buildings, as part of its hereditament, also has to be compatible with EU law. The argument is that the plant connected to the fibre and the buildings associated with the plant are as inextricably linked with the provision of electronic communications services as the fibre is. Assuming that is so, and the VOA was obliged to treat BT and Vtesse equally in valuing their plant and real estate, does that support Vtesse's argument that the open market value of its buildings – which is otherwise agreed – should be halved, to bring it into line with what is said to be the values attributed to BT's buildings?

199. This raises exactly the same issues as the third question and our answer is the same. BT's enormous range of operational buildings and plant have to be valued (together with the rest of its hereditament) as a single unit, and the comparable method of valuation is not an available method for such a hereditament. Vtesse's real estate is vanishingly smaller and not comparable in any way to BT's estate. There is therefore no legal duty to treat them as if they were alike and use the same method of valuation. The comparable method based on market evidence is self-evidently the appropriate method of valuation in Vtesse's case.

200. In any event, we found no support whatever in Mr Paul's analysis of BT's valuation for halving the otherwise agreed values of Vtesse's properties, as we have already explained. The appeal therefore fails on the facts, even if Vtesse's EU law premise is sound.

201. For the reasons that we have given, although we accept that the first question is a question of EU law, it is unnecessary to answer it in order to give judgment on this appeal. We can assume in Vtesse's favour (without deciding) that it is right on the first question, and that EU

law principles of equal treatment and non-discrimination are thereby imported into the NDR valuation process. They add nothing to the analysis, however, because what are being valued are two wholly different hereditaments, not two comparable businesses. So under EU law just as much as in valuation principle and under domestic rating law, it would be wrong to treat the different hereditaments in the same way, by using the same method of valuing in accordance with the statutory hypothesis if the facts justify or require the use of a different method.

202. On any view, the contention that EU law requires the VOA to undertake a disaggregation of the value of a different mixed hereditament, when this cannot be done accurately, or to conduct an exercise of attribution of costs of a different business, when this is inexact and not a valuation process at all, in order to value Vtesse's hereditament using a derived unit rate when there is ample market evidence that is directly applicable, cannot be right. On the facts of this case, as we have found them, the answer is clear.

203. We therefore decline to refer any question to the CJEU and dismiss Vtesse's appeal.

204. This decision is final on all matters other than the costs of the appeal. The parties may now make submissions on such costs and a letter giving directions for the exchange and service of submissions accompanies this decision.

Dated 22 April 2020



The Honourable Mr Justice Fancourt  
Chamber President



A J Trott FRICS  
Member