Regulatory Financial Statements

for the year ended 31 March 2023

Contents of the Regulatory Financial Statements

Introduction to the Regulatory Financial Statements

KCOM Limited (“KCOM”), has been classified by Ofcom as a communications provider with Significant Market Power ("SMP") in certain communications markets in the Hull area represented by the geographic area of KCOM’s original licensed area ("OLA" or the “Hull Area”).

In accordance with Ofcom’s conditions and directions relating to its SMP findings, KCOM is required to prepare financial statements (the Regulatory Financial Statements or “RFS”) setting out its financial performance in certain markets which KCOM has been found to have SMP.

In October 2021 Ofcom published its *Hull Area Wholesale Fixed Telecoms Market Review 2021-26* ("Hull FTMR") which removed its SMP findings relating to KCOM in the following markets:

- Wholesale Broadband Access
- Wholesale Low Bandwidth Traditional Interface Symmetric Broadband Origination (TISB0) <8Mbit/s
- Wholesale Contemporary Interface Symmetric Broadband Origination ('CISBO')
- Wholesale Fixed Analogue Exchange Lines
- Wholesale ISDN 30 Exchange Line Services
- Wholesale ISDN 2 Exchange Line Services
- Wholesale Call Origination on Fixed Narrowband network

The FTMR found that KCOM had SMP in the following markets and accordingly required KCOM to prepare RFS for these markets:
- Wholesale Local Access
- Wholesale Leased Lines Access Services

The RFS comprise individual and consolidated reports for each of the markets where cost accounting and accounting separation obligations apply. The RFS are based on the consolidated results of KCOM Group Limited. Reconciliations to the KCOM Group Limited annual report are included in the RFS.

The respective wholesale markets contain fully allocated costs, revenues, assets and liabilities relating to services provided to other licensed telecommunications operators or similar services provided to KCOM’s retail business units. Network charges to other operators and KCOM’s own retail business are based on their consumption of bundles of network elements (known as “components”) in network services. The current cost accounting ("CCA") cost of components is based on fully allocated costs of components including a cost of capital.

The accompanying Description of Cost Accounting System (‘DOCAS’) document describes the basis on which the RFS have been prepared.

The form and content of the RFS are based on the reporting obligations set by Ofcom in the following documents:

- *KCOM Regulatory Financial Reporting, Statement on new regulatory financial reporting directions covering all regulated fixed telecoms markets* (6 February 2019)
- *Hull Area Wholesale Fixed Telecoms Market Review 2021-26 (28 October 2021)*

Introduction to the Regulatory Financial Statements

Impact of inflation on Returns

As in FY22, the returns in the FY23 RFS are materially impacted by high levels of inflation.

The RFS are prepared on a current cost accounting basis, which requires fixed assets to be revalued, based on an estimate of the cost to replace them.This is done using the Retail Price Index (RPI). The estimated cost of replacing these assets and the reported mean capital employed will therefore increase each year in line with inflation. This increase, or “holding gain”, is recognised in the income statement for the year and has the effect of reducing reported net costs and increasing reported returns.

In FY22 the increase in RPI was 9% and in FY23 14%.

The impact on inflation on returns in the SMP reported markets is illustrated in the table below which shows the returns in 2023 excluding the holding gains and supplementary depreciation in the year from both the income statement and mean capital employed.

Return on Mean Capital Employed	**FY22 (Restated) As reported**	**FY22 Excluding Holding Gains and Additional Depreciation (Unaudited)**	**FY23 As reported**	**FY23 Excluding Holding Gains and Additional Depreciation (Unaudited)**
Wholesale Local Access	17.2%	10.3%	23.4%	13.0%
Wholesale Leased Lines	17.0%	12.0%	16.2%	12.3%
All reported SMP Markets	**17.2%**	**10.5%**	**22.6%**	**12.9%**

Sale of National Business (Prior Year)

During FY22, KCOM sold its national ICT business (the "National Business"). The revenues and costs of the National Business for the 4 months prior to the sale in FY22 are included in the Retail Residual statements for the prior year.

Restatement of Prior Year Comparatives

Following the disposal of the National Business segment, management undertook a comprehensive review of the fixed asset register during the year to identify any assets which have been replaced or decommissioned. As explained in the Annual Report (page 41), this included assets on the register in FY22, and resulted in a restatement to the prior year comparatives.

Some costs in the cost model used to prepare the RFS are allocated on the basis of gross replacement cost (“GRC”), being the current cost equivalent of gross book value ("GBV"), and so prior year comparatives for FY22 in the RFS have been restated based on amending the cost allocations to reflect the restated GRC (there was no change in the allocation methodology, only the allocation percentages based on GRC’s).

The impact of the restatement on each market is shown in Note 4.

Business Reorganisation

During the year some parts of the business were reorganised, resulting in the creation of new cost centres and mergers of others. The classification of some costs on the face of the profit and loss account depends on the cost centre and as a result, in some cases this has changed from FY22. For example, the procurement team was previously in a separate cost centre and shown as 'Other', but is now in the finance cost centre and shown as 'Finance and Billing' (the RFS Model currently only provides for a single cost classification to be used for each cost centre). This has not affected the allocation methodologies of costs, only the classification of the cost. Accordingly some cost catregories may not be directly comparable with FY22, but are at a total level.

Introduction to the Regulatory Financial Statements

Wholesale Business Review

KCOM has continued to strengthen the capabilities of its Wholesale function through its independent commercial business unit and continued investment in Core IP Network and self-service order portals for wholesale partners which has laid the foundations for future growth while improving the experience of existing customers. The company has also begun testing next generation XGS PON technology which will quadruple bandwidth availability and prove a huge asset going forward.

The Wholesale business has continued to grow solidly with more than 150 reseller partners now providing services over our expanding network, a 60 per cent increase over the previous year. It is continuing to strengthen and onboard new partners. Following a review of its pricing in FY24 the wholesale business reduced its wholesale FTTP prices in Autumn 2023 to attract new wholesale customers and increase fibre take-up.This demonstrates how by working together with resellers positive benefit can be delivered - from KCOM’s partners accessing the Company’s world class infrastructure, to their end customers who receive quality products delivered over one of the best networks in the UK.

Statement of directors' responsibilities in respect of the regulatory financial statements

The directors of KCOM Group Limited are responsible for preparing the regulatory financial statements in accordance with the Description of Cost Accounting System ("DOCAS") dated 20 December 2023. This special reporting framework is specific to these financial statements and does not represent a financial reporting framework established by an authorised or recognised standard setting organisation. The directors must not approve the regulatory financial statements unless they are satisfied that they have been properly prepared, in all material respects, in accordance with the basis of preparation and accounting policies in note 2 to the regulatory financial statements. In preparing the regulatory financial statements, the directors are responsible for:

- selecting suitable accounting policies and then applying them consistently;
- making judgements and accounting estimates that are reasonable and prudent;
- stating the basis of preparation and accounting policies applied; and
- reconciling the regulatory financial statements with the Annual Report and Accounts of KCOM Group Limited and ensuring that reconciliation is demonstrated and explained.

The directors are responsible for safeguarding the assets of the KCOM Group Limited, which may for regulatory purposes be allocated or apportioned to the separate businesses, and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are also responsible for keeping adequate accounting records that are sufficient to show and explain the group's transactions and disclose with reasonable accuracy at any time the financial position of the group.

The directors are also responsible for the maintenance and integrity of the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Tim Shaw
Chief Executive Officer
20 December 2023

Independent auditors' report to the members of KCOM Group Limited and Ofcom

Opinion

In our opinion, KCOM Group Limited's Regulatory Accounts for the year ended 31 March 2023 have been properly prepared, in all material respects, in accordance with the Description of Cost Accounting System ("DOCAS") dated 20 December 2023 and "The regulatory financial reporting obligations of BT and Kingston Communications" published by the Office of Communications ("Ofcom" or the "Regulator") on 22 July 2004 and subsequent amendments, including the most recent directions conferred in "Hull Wholesale Fixed Telecoms Market Review 2021-26" issued October 2021 (the "Obligations") as summarised in the basis of preparation in note 2 and accounting policies in note 2 to the Regulatory Accounts.

We have audited the Regulatory Accounts, which comprise:

- the Consolidated Current Cost Profit and Loss Account, the Consolidated Statement of Current Cost Mean Capital Employed and the Consolidated Network Activity Statement as at 31 March 2023 and for the year then ended;
- the Current Cost Profit and Loss Accounts and the Current Cost Mean Capital Employed Statements for each Regulatory Market (Wholesale Local Access in the Hull Area, and Wholesale Market for Leased Lines within the Hull Area) as at 31 March 2023 and for the year then ended;
- the notes to the Regulatory Accounts, which include a description of the significant accounting policies; and
- the Reconciliation Statement - the Consolidated Profit and Loss Account for the year ended 31 March 2023, and the Reconciliation Statement - the Consolidated Mean Capital Employed for the year then ended.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)"), including ISA (UK) 800, and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the Regulatory Accounts section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We remained independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, as applicable to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Emphasis of matter - Basis of preparation

In forming our opinion on the Regulatory Accounts, which is not modified, we draw attention to note 2 of the Regulatory Accounts which includes a description of the basis of preparation, and in particular, the fact that the accounting policies used and disclosures made are not intended to, and do not, comply with the requirements of international accounting standards in conformity with the requirements of the Companies Act 2006. The Regulatory Accounts are prepared in accordance with a special purpose framework for the directors and Ofcom for the specific purpose as described in the Use of this report paragraph below. As a result, the Regulatory Accounts may not be suitable for another purpose.

In addition, we draw attention to the fact that these Regulatory Accounts have not been prepared under section 394 of the Companies Act 2006 and are not the company's statutory financial statements.

Independent auditors' report to the members of KCOM Group Limited and Ofcom

Conclusions relating to going concern

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the company's ability to continue as a going concern for a period of at least twelve months from the date on which the financial statements are authorised for issue.

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

However, because not all future events or conditions can be predicted, this conclusion is not a guarantee as to the company's ability to continue as a going concern.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

Reporting on other information

The other information comprises all of the information in the Regulatory Financial Statements other than the Regulatory Accounts and our auditors' report thereon, including the Regulatory financial review on page 13. The directors are responsible for the other information. Our opinion on the Regulatory Accounts does not cover the other information and, accordingly, we do not express an audit opinion or any form of assurance thereon.

In connection with our audit of the Regulatory Accounts, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the Regulatory Accounts or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the Regulatory Accounts or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

Responsibilities for the Regulatory Accounts and the audit

Responsibilities of the directors for the Regulatory Accounts

As explained more fully in the Statement of directors' responsibilities in respect of the regulatory financial statments, set out on page 6, the directors are responsible for the preparation of the Regulatory Accounts in accordance with the basis of preparation and accounting policies in note 2 to the Regulatory Accounts and for determining that the basis of preparation and accounting policies are acceptable in the circumstances. The directors are also responsible for such internal control as they determine is necessary to enable the preparation of Regulatory Accounts that are free from material misstatement, whether due to fraud or error.

In preparing the Regulatory Accounts, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditors' responsibilities for the audit of the Regulatory Accounts

Our objectives are to obtain reasonable assurance about whether the Regulatory Accounts as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these Regulatory Accounts.

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud, is detailed below.

Based on our understanding of the company and industry, we identified the principal risks of non-compliance with laws and regulations related to Ofcom regulations, and we considered the extent to which non-compliance might have a material effect on the financial statements. We also considered those laws and regulations that have a direct impact on the financial statements such as the Companies Act 2006. We evaluated management's incentives and opportunities for fraudulent manipulation of the Regulatory Accounts are based upon (including the risk of override of controls), and determined that the principal risks were related to posting journal entries to manipulate financial performances and management bias in determining significant accounting estimates that could influence reported performance. Audit procedures performed included:

- Enquiring with management to understand relevant laws and regulations applicable to the company and their assessment of fraud related risks;
- Identifying and testing journal entries using a risk based targeting approach for unexpected account combinations and users;
- Testing accounting estimates that we deemed to present a risk of material misstatement including assessing the data, methods and assumptions applied to by management in the development of each estimate; and
- Reviewing correspondence with Ofcom to assess compliance with relevant regulations.

There are inherent limitations in the audit procedures described above. We are less likely to become aware of instances of non-compliance with laws and regulations that are not closely related to events and transactions reflected in the Regulatory Accounts. Also, the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

A further description of our responsibilities for the audit of the Regulatory Accounts is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

Use of this report

This report, including the opinion, has been prepared for and only for the company's directors as a body for the purposes of meeting the company's obligations under the Obligations and for Ofcom in accordance with our engagement letter dated 16 August 2023 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person other than the company (or, where the Regulator has signed a Written Notice, the Regulator) to whom this report is shown or into whose hands it may come, including without limitation under any contractual obligations of the company, save where expressly agreed by our prior consent in writing.

Our opinion on the 2023 Regulatory Accounts is separate from our opinions on the statutory financial statements of KCOM Group Limited for the year end 31 March 2023 on which we reported on 22 September 2023, and for the year ended 31 March 2022 on which we reported on 23 November 2022 which are prepared for a different purpose. Our statutory audit work was undertaken so that we might state to KCOM Group Limited's members those matters we are required to state to them in a statutory audit report and for no other purpose. In conducting our subsequent audit of the 2023 Regulatory Accounts, and in providing the opinions above, we have not performed any additional tests of the transactions and balances which are recorded in the general ledgers and other accounting records beyond those already performed for the purpose of the audit of the statutory financial statements of KCOM Group Limited for the years ended 31 March 2022 and 31 March 2023.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants
Leeds
20 December 2023

Consolidated Current Cost Profit and Loss Account
Consolidated Total - For all markets where cost accounting and accounting separation obligations apply

for the year ended 31 March 2023	2023	2022 (Restated) (Note 4.)	£k Change Year on Year	% Change Year on Year
Turnover				
Internal Sales	27,822	24,961	*2,861*	*11%*
External Sales	2,657	2,033	*624*	*31%*
Total Turnover	**30,479**	**26,994**	*3,485*	*13%*
Operating costs				
Operating costs				
- Engineering Support	(4,312)	(3,575)	*(737)*	*21%*
- Finance & Billing	(1,992)	(728)	*(1,264)*	*174%*
- General Management	(1,517)	(2,622)	*1,105*	*(42%)*
- Bad Debts	(10)	(62)	*53*	*(84%)*
- Back Office Support	(2,154)	(294)	*(1,860)*	*633%*
- Other Costs	(2,374)	(5,316)	*2,942*	*(55%)*
Sub total operating expenditure	**(12,359)**	**(12,597)**	***238***	***(2%)***
Depreciation				
- Duct	(136)	(143)	*7*	*(5%)*
- Copper	-	-	-	-
- Fibre	(3,853)	(3,995)	*143*	*(4%)*
- Transmission	(127)	(140)	*13*	*(9%)*
- Exchange	(124)	(216)	*92*	*(43%)*
- Other	(2,545)	(1,348)	*(1,197)*	*89%*
CCA adjustments:				
Holding gain / (loss)	12,820	7,532	*5,289*	*70%*
Supplementary depreciation	(1,770)	(998)	*(772)*	*77%*
Other adjustments	-	-	-	-
Total operating costs	**(8,094)**	**(11,905)**	***3,811***	***(32%)***
Return	**22,385**	**15,088**	***7,296***	***48%***
MCE	**99,062**	**87,659**	***11,403***	***13.0%***

RETURN ON MEAN CAPITAL EMPLOYED

Total Reported Wholesale Markets	2023	2022 (Restated) (Note 4.)
	%	**%**
Return on mean capital employed	**22.6%**	**17.2%**

Consolidated Statement of Current Cost Mean Capital Employed

Consolidated Total - For all markets where cost accounting and accounting separation obligations apply

for the year ended 31 March 2023

	£k 2023	£k 2022 (Restated) (Note 4.)	*£k Change*	*% Change*
Fixed assets				
Tangible assets				
- Land & Buildings	2,187	1,340	847	*63%*
- Duct	4,481	4,442	39	*3%*
- Fibre	70,300	65,157	5,142	*8%*
- Copper	-	-	-	-
- Transmission	2,181	1,776	406	*23%*
- Exchange	331	509	(177)	*(35%)*
- Other	15,935	11,938	3,997	*33%*
Investments	-	-	-	-
Total fixed assets	**95,415**	**85,160**	**10,254**	***12%***
Current assets				
Stocks	2,033	643	1,390	*216%*
Debtors				
- internal	2,287	2,052	235	*11%*
- external	444	503	(59)	*(12%)*
Total current assets	**4,763**	**3,197**	**1,566**	***49%***
Creditors: amounts falling due within one year				
Other creditors				
- internal	-	-	-	-
- external	(1,116)	(699)	(417)	*60%*
Total creditors: amounts falling due within one year	(1,116)	(699)	(417)	*60%*
Net current assets	3,647	2,498	1,149	*46%*
Total assets less current liabilities	99,062	87,659	11,403	*13%*
Provisions for liabilities and charges	-	-	-	-
Closing capital employed	**99,062**	**87,659**	**11,403**	***13%***

Consolidated Network Activity Statement

for the year ended 31 March 2023

Fully Allocated Costs £'000	HCA operating cost	Supplementary Depreciation	Holding gain and other CCA adjustments	Total CCA operating costs	CCA mean capital employed	Applicable rate of return on capital %	Capital costs	Total of operating costs and capital costs relating to current year	Unit of measure (based on network components)	Volume	Average costs per unit on a current cost basis relating to current year
Components											
Net Current Assets	-	-	-	-	3,647	7.8%	285	285	Various	162,122	£1.7579
Electronics	1,063	79	(323)	818	3,081	7.8%	240	1,058	Various	162,122	£6.5279
Field Provision	1,150	23	(45)	1,127	367	7.8%	29	1,156	Various	162,122	£7.1312
Field Maintenance	259	5	(10)	254	83	7.8%	6	260	Various	162,122	£1.6034
Local Loop Infrastructure	11,085	1,273	(11,745)	613	83,822	7.8%	6,538	7,151	Various	162,122	£44.1104
Exchange Concentrator		-	-	-	-	7.8%	-	-	Various	162,122	£0.0000
Exchange to Exchange Transmission link	2,118	281	(487)	1,913	6,451	7.8%	503	2,416	Various	162,122	£14.9017
Back-office Provisioning	3,203	63	(126)	3,140	1,021	7.8%	80	3,220	Various	162,122	£19.8631
Back-office Maintenance	11	0	(0)	10	3	7.8%	-	10	Various	162,122	£0.0639
Sales and Product Management	-	-	-	-	-	7.8%	-	-	Various	162,122	£0.0000
Other	255	47	(84)	218	587	7.8%	46	264	Various	162,122	£1.6258
Totals 2023	**19,144**	**1,770**	**(12,820)**	**8,094**	**99,062**		**7,727**	**15,821**			

for the year ended 31 March 2022 (restated) (Note 4.)

Fully Allocated Costs £'000	HCA operating cost	Supplementary Depreciation	Holding gain and other CCA adjustments	Total CCA operating costs	CCA mean capital employed	Applicable rate of return on capital %	Capital costs	Total of operating costs and capital costs relating to	Unit of measure (based on network components)	Volume	Average costs per unit on a current cost basis relating to current year
Components											
Net Current Assets	-	-	-	-	2,498	7.8%	195	195	Various	151,815	£1.2845
Electronics	1,100	44	(188)	957	2,063	7.8%	261	1,218	Various	151,815	£8.0239
Field Provision	1,718	9	(24)	1,703	250	7.8%	19	1,722	Various	151,815	£11.3441
Field Maintenance	208	1	(3)	206	30	7.8%	2	208	Various	151,815	£1.3686
Local Loop Infrastructure	11,067	638	(6,461)	5,244	73,686	7.8%	5,747	10,991	Various	151,815	£72.3966
Exchange Concentrator	-	-	-	-	-	7.8%	-	-	Various	151,815	£0.0000
Exchange to Exchange Transmission link	2,638	253	(723)	2,168	7,719	7.8%	594	2,762	Various	151,815	£18.1963
Back-office Provisioning	1,102	6	(15)	1,093	160	7.8%	12	1,105	Various	151,815	£7.2791
Back-office Maintenance	42	0	(1)	42	6	7.8%	-	42	Various	151,815	£0.2767
Sales and Product Management	64	-	-	64	-	7.8%	-	64	Various	151,815	£0.4208
Other	500	46	(118)	428	1,247	7.8%	98	526	Various	151,815	£3.4624
Totals 2022 Restated	**18,439**	**998**	**(7,532)**	**11,905**	**87,659**		**6,928**	**18,833**			

Regulatory Financial Review

Rounding of Presented Numbers

These statements incorporate numbers to decimal places which, when presented as whole digits within these statements, may not cast precisely to the totals. In consequence the % variances refer to the underlying figure in £ and may differ from calculations performed using the visible integers.

Ofcom Statement

Under Schedule 4 of Ofcom's Statement: *KCOM Regulatory Financial Reporting* , 6 February 2019, Ofcom is entitled to comment on the data in, the notes to, or the presentation of any of the Financial Statements, in relation to each of the markets. Ofcom has informed KCOM that it does not consider such a statement necessary for the Regulatory Accounts ending 31 March 2023.

Wholesale Local Access in the Hull area

The Wholesale Local Access market comprises fibre access products from a point of aggregation (at an exchange) to a home or business premise in the Hull area. KCOM does not supply any copper-based Wholesale Local Access services and so none are included in this market (all wholesale copper services in the Hull area included in the statements for the Wholesale Residual market). As at 31 March 2023, 100% of premises were passed by KCOM's fibre deployment in the Hull Area. There are a number of residential and business addresses in the Hull Area that are currently without 'bookable' access to our fibre broadband service (i.e. those customers that cannot currently purchase our fibre broadband service due to controllable engineering exceptions but whose premise has been passed with the requisite fibre infrastructure). These 'non-bookable exceptions' arise as a consequence of engineering (e.g. direct buried cables) or administrative (e.g. wayleaves) issues. KCOM has an active programme to address these exceptions. The proportion of consumer broadband customers connected with fibre was 87% at the end of FY23.

Number of circuits

	2020/21 Restated		**2021/22**		**2022/23**	
	Volume	**Annual increase**	**Volume**	**Annual increase**	**Volume**	**Annual increase**
Rental circuit Volume	125,370	N/a	135,610	8%	143,393	6%

Wholesale products in this market have been priced using relevant Reference Offer prices in the period under review.

Revenue has increased by 14% primarily as a result of higher volumes.

The increase in profitability is primarily due to the increase in holding gain (due to higher inflation in the year).

Wholesale Local Access in the Hull area

CURRENT COST PROFIT AND LOSS ACCOUNT
for the year ended 31 March 2023

	£k 2023	£k 2022 (Restated) (Note 4.)	*£k Change Year on Year*	*% Change Year on Year*
Turnover				
Internal Sales	24,413	21,389	*3,024*	*14%*
External Sales	-	-	-	-
Total Turnover	**24,413**	**21,389**	***3,024***	*14%*
Operating costs				
Operating costs				
- Engineering Support	(2,312)	(2,190)	*(121)*	*6%*
- Finance & Billing	(1,619)	(593)	*(1,026)*	*173%*
- General Management	(1,235)	(2,052)	818	*(40%)*
- Bad Debts	(8)	(62)	*55*	*(87%)*
- Back Office Support	(1,600)	(270)	*(1,330)*	*493%*
- Other Costs (1)	(1,928)	(4,192)	*2,264*	*(54%)*
Sub total operating expenditure	**(8,700)**	**(9,359)**	***659***	*(7%)*
Depreciation				
- Duct	(90)	(84)	*(6)*	*7%*
- Copper	-		-	
- Fibre	(3,514)	(3,410)	*(104)*	*3%*
- Transmission	-	-	-	-
- Exchange	(114)	(187)	*73*	*(39%)*
- Other	(2,003)	(1,060)	*(942)*	*89%*
CCA adjustments:				
Holding gain / (loss)	11,876	6,564	*5,311*	*81%*
Supplementary depreciation	(1,334)	(659)	*(674)*	*102%*
Other adjustments	-	-	-	-
Total operating costs	**(3,879)**	**(8,196)**	***4,317***	***(53%)***
Return	**20,534**	**13,193**	***7,341***	***56%***
MCE	**87,602**	**76,481**	***11,121***	***15%***

RETURN ON MEAN CAPITAL EMPLOYED
for the year ended 31 March 2023

	2023	2022
Return on mean capital employed	**23.4%**	**17.2%**

(1) Other Costs includes £0.9m of Hereditament costs (FY22 £0.4m).All 'Other' cost items are below 5% of total operating costs.

Wholesale Local Access in the Hull area

STATEMENT OF CURRENT COST MEAN CAPITAL EMPLOYED
for the year ended 31 March 2023

	£k 2023	£k 2022 (Restated) (Note 4.)	*£k Change*	*% Change*
Fixed assets				
Tangible assets				
- Land & Buildings	1,661	927	*734*	*79%*
- Duct	2,979	2,618	*361*	*14%*
- Fibre	67,273	60,866	*6,406*	*11%*
- Copper	-	-	-	-
- Transmission	-	-	-	-
- Exchange	270	407	*(137)*	*(34%)*
- Other	12,668	9,949	*2,719*	*27%*
Total fixed assets	**84,851**	**74,767**	**10,083**	***13%***
			-	-
Current assets				
Stocks	1,652	523	*1,129*	*216%*
Debtors				
- internal	2,007	1,758	*249*	*14%*
- external	-	-	-	-
Total current assets	**3,658**	**2,281**	**1,378**	***60%***
Creditors: amounts falling due within one year				
Other creditors				
- internal	-	-	-	-
- external	(907)	(567)	*(340)*	*60%*
Total creditors: amounts falling due within one year	(907)	(567)	*(340)*	*60%*
Net current assets	2,752	1,714	*1,038*	*61%*
Total assets less current liabilities	87,602	76,481	*11,121*	*15%*
Provisions for liabilities and charges	-	-	-	-
Closing capital employed	**87,602**	**76,481**	***11,121***	*15%*

Regulatory Financial Review (KCOM)

Wholesale Market for Leased Lines within the Hull Area

The Leased Lines market includes 2Mbit/s to 100Gbit/s ethernet services. Customers include businesses, mobile infrastructure operators and Communications Providers servicing their national clients.

Number of Circuits

	2020/21 Restated		2021/22		2022/23	
	Volume	Annual increase	Volume	Annual Increase	Volume	Annual Increase
Circuit Nos	1,616	n/a	1,913	18%	1,893	-1%

Overall, revenue has increased by 8% reflecting higher average prices per circuit offset by lower sales volumes. Total costs increased by 14% with a resulting reduction in ROCE of 0.8%.

Wholesale Market for Leased Lines within the Hull Area

CURRENT COST PROFIT AND LOSS ACCOUNT
for the year ended 31 March 2023

	£k 2023	£k 2022 (Restated) (Note 4.)	£k Change Year on Year	% Change Year on Year
Turnover				
Internal Sales	3,408	3,572	*(164)*	*(5%)*
External Sales	2,657	2,033	*624*	*31%*
Total Turnover	**6,065**	**5,605**	***461***	***8%***
Operating costs				
Operating costs				
- Engineering Support	(2,000)	(1,384)	*(616)*	*45%*
- Finance & Billing	(374)	(136)	*(238)*	*175%*
- General Management	(283)	(570)	*287*	*(50%)*
- Bad Debts	(2)	-	*(2)*	*0%*
- Back Office Support	(555)	(24)	*(530)*	*2173%*
- Other Costs (1)	(446)	(1,124)	*678*	*(60%)*
Sub total operating expenditure	**(3,659)**	**(3,238)**	***(422)***	***13%***
Depreciation				
- Duct	(46)	(59)	*13*	*(23%)*
- Copper	-	-	-	-
- Fibre	(339)	(586)	*247*	*(42%)*
- Transmission	(127)	(140)	*13*	*(9%)*
- Exchange	(10)	(28)	*19*	*(67%)*
- Other	(542)	(288)	*(255)*	*89%*
CCA adjustments:				
Holding gain / (loss)	945	967	*(23)*	*(2%)*
Supplementary depreciation	(437)	(339)	*(98)*	*29%*
Other adjustments				
Total operating costs	**(4,214)**	**(3,709)**	**(505)**	*14%*
Return	**1,851**	**1,896**	**(45)**	*(2%)*
MCE	**11,460**	**11,177**	***282***	*3%*

RETURN ON MEAN CAPITAL EMPLOYED
for the year ended 31 March 2023

	2023 %	(Restated) %
Return on mean capital employed	**16.2%**	**17.0%**

(1) Other Costs includes £0.2m of Hereditament costs (FY22 £0.3m). All 'Other' cost items are below 5% of total operating costs.

Wholesale Market for Leased Lines within the Hull Area

STATEMENT OF CURRENT COST MEAN CAPITAL EMPLOYED

for the year ended 31 March 2023

	£k 2023	£k 2022 (Restated) (Note 4.)	*£'k Change*	*% Change*
Fixed assets				
Tangible assets				
- Land & Buildings	527	413	*113*	*27%*
- Duct	1,502	1,823	*(322)*	*(18%)*
- Fibre	3,027	4,291	*(1,264)*	*(29%)*
- Copper	-	-	-	-
- Transmission	2,181	1,776	*406*	*23%*
- Exchange	61	101	*(40)*	*(40%)*
- Other	3,267	1,988	*1,278*	*64%*
	`			
Total fixed assets	**10,564**	**10,393**	**171**	***2%***
Current assets				
Stocks	381	120	*261*	*218%*
Debtors	-	-		
- internal	280	294	*(13)*	*(5%)*
- external	444	503	*(59)*	*(12%)*
Total current assets	**1,105**	**916**	**188**	***21%***
Creditors: amounts falling due within one year				
Other creditors				
- internal	-	-	-	-
- external	(209)	(132)	*(77)*	*58%*
Total creditors: amounts falling due within one year	(209)	(132)	*(77)*	*58%*
Net current assets	895	784	*111*	*14%*
Total assets less current liabilities	11,460	11,177	*282*	*3%*
Provisions for liabilities and charges	-	-	-	-
Closing capital employed	**11,460**	**11,177**	***282***	***3%***

Notes to the Regulatory Financial Statements including accounting policies

1. STATUTORY FINANCIAL STATEMENTS
These Financial Statements, which are not statutory accounts within the meaning of the Companies Act 2006, have been prepared on the basis described in the Description of Cost Accounting System (DOCAS) dated 20 December 2023. The statutory financial statements for KCOM Group Limited, for the year ended 31 March 2023 have been prepared, on which the auditors issued an unqualified report.

2. ACCOUNTING POLICIES
Summarised below are the principal accounting policies which have been consistently applied throughout the current and prior financial year.

Basis of preparation

These financial statements have been prepared on the basis described in the Description of Cost Accounting System dated 20 December 2023 and as required under Ofcom's regulatory financial reporting requirements as set out in the documents listed on Page 3. This special reporting framework is specific to these financial statements and does not represent a financial reporting framework established by an authorised or recognised standard setting organisation.

Current cost profit is derived firstly by arriving at historical cost profit/(loss) in each of the businesses. Then an adjustment is made for current cost depreciation, to result in current cost retained profit/(loss). Finally, unrealised holding gains/(losses) and realised holding gains/(losses) are calculated to result in holding gains/(losses) on fixed assets. This calculation is added onto current cost retained profit/(loss), to result in amount retained.

In the current cost balance sheet, each Business's assets are restated at their value to the Business, using their net current replacement cost.

Wholesale services used internally and externally are costed using the same network components and allocated using the same usage factors.

The reconciliation (on page 29) between profts in the RFS and the Annual Report reconciles the Profit as shown in the RFS to the operating profit before tax in KCOM Annual Report excluding 'profit from discontinued operation'.

Similarly, in the reconciliation (on page 31) between mean capital employed in the RFS and the Annual Report, the adjustments to Shareholder Funds, made to exclude items not relevant to the regulatory financial statements, are based on the amounts shown in the Annual Report presented net of 'Liabilities directly associated with assets classified as held for sale' and 'Assets held for sale'. As a result, the RFS include an allocation of certain items, (including deferred tax assets and lease liabilities) to the retail residual activity which would previously have been excluded from the RFS as reconciling items.

Turnover

The Group's product and service offerings include service only contracts, product only contracts and contracts which combine the provision of equipment and services as described in more detail below. Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services supplied, stated net of discounts, returns and value-added taxes. All intra-Group transactions, balances, income and expenses are eliminated on consolidation.

Standalone service offerings
The Group offers a range of fixed telephone, internet access and hosting services. Service revenue is recognised as the service is provided, based on usage (e.g. minutes of traffic or bytes of data used) or the period (e.g. monthly service costs). Service obligations which are substantially the same and have the same pattern of transfer to the customer are treated as a single performance obligation.

Service only offerings may include an initial service connection fee. In general, this is not deemed to be a separate performance obligation and thus the connection fee is deferred as a contract liability and recognised over the enforceable term of the contract.

Standalone product sales

Equipment sales may be separate from, or bundled with, a service offer. When equipment sales are separate to a service offer, the amount invoiced is recognised in revenue upon delivery of the equipment, at the point that control is deemed to transfer to the customerBundled equipment and service offerings

Equipment revenue is recognised separately if the two components are deemed to be distinct (i.e. the customer can benefit from each component of the contract separately). Where one of the components is provided at a reduced selling price, revenue is allocated to each component in proportion to their individual selling prices.

Notes to the Regulatory Financial Statements including accounting policies (continued)

Standalone product sales
Equipment sales may be separate from, or bundled with, a service offer. When equipment sales are separate to a service offer, the amount invoiced is recognised in revenue upon delivery of the equipment, at the point that control is deemed to transfer to the customer.

Bundled equipment and service offerings
The Group often enters into contracts with customers which comprise equipment (e.g. a router) and services (e.g. an internet access contract). Equipment revenue is recognised separately if the two components are deemed to be distinct (i.e. the customer can benefit from each component of the contract separately). Where one of the components is provided at a reduced selling price, revenue is allocated to each component in proportion to their individual selling prices.

Tangible fixed assets

Tangible fixed assets are recorded at current cost. Depreciation is provided so as to write off the current cost of assets to residual values on a straight-line basis over the assets' useful estimated lives as follows:

- Freehold buildings - 40 years
- Leasehold buildings and improvements - Period of lease
- Exchange equipment - 10 years
- External plant - 10 to 40 years
- Vehicles, other apparatus and equipment - 3 to 10 years
- Freehold land is not depreciated

Depreciation of network infrastructure and related equipment is provided for from the date the network comes into operation.
Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets, or where shorter, over the term of the relevant lease. As the RFS are prepared on a current cost accounting (CCA) basis, KCOM revalues its assets based on an estimate of what it would cost to replace them. KCOM bases its estimate of replacement cost on the RPI index.

The residual value of the asset, if significant, is reassessed annually.

Current Cost Accounting

As set out in Ofcom's directions, asset values are stated on a Current Cost Accounting ("CCA") basis. This requires KCOM to revalue its assets based on an estimate of what it would cost to replace them. KCOM bases its estimate of replacement cost on the RPI index.

The estimated cost of replacing these assets, and therefore the reported mean capital employed, will increase each year, in line with inflation. This increase in value, or holding gain, is recognised in the income statement for the year and has the effect of reducing reported net costs. A supplementary CCA depreciation cost on the income statement is also calculated to reflect the higher depreciation costs associated with the increased asset value.

Stocks

Stocks, stores and work-in-progress are valued at the lower of cost or net realisable value. Cost is determined using the weighted average method. Cost includes raw materials and, where appropriate, direct overhead expenses. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution. Provision is made for obsolete, slow moving or defective items where appropriate.

Foreign currencies

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction or at the contracted rate if the transaction is covered by a forward exchange contract. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange ruling at the balance sheet date or, if appropriate, at the forward contract rate. The exchange difference arising on the retranslation of opening net assets is taken directly to reserves. All other translation differences are taken to the profit and loss account with the exception of differences on foreign currency borrowings to the extent that they are used to finance or provide a hedge against Group equity investments in foreign enterprises, which are taken directly to reserves together with the exchange difference on the net investment in these enterprises.

Notes to the Regulatory Financial Statements including accounting policies (continued)

Leases

On inception of a new lease, a 'lease liability' is recognised in the balance sheet. The lease liability is measured at the present value of minimum lease payments, discounted using the Company's incremental borrowing rate. A 'right of use asset' is also recognised, typically at an amount equal to the lease liabilty.

The right of use asset is depreciated over the life of the lease and interest is recognised based on the incremental borrowing rate. This replaces the straight line expense typically seen for operating leases.

All Right of Use assets and associated liabilities are associated with the part of the KCOM business outside of the regulated Hull area and are therefore excluded from the RFS statements for those markets.

Pensions

During the year the Company operated three primary pension schemes covering the pension arrangements of eligible employees. One of these schemes operates on the defined contribution (money purchase) principle and for this scheme the pension cost charged represents the contributions payable. The other schemes provide members with defined benefits based on final pensionable salary. The overall long term costs of providing pensions for employees who are members of this scheme are charged against profits evenly over the expected working lives of the members. The contributions are assessed in accordance with the advice of a qualified actuary based on actuarial valuations normally conducted every three years. The relevant benefits promises are funded in advance and the assets of the schemes are held in separate trustee administered funds.

Sale of National Business

During FY22, KCOM sold its national ICT business (the "National Business"). The revenues and costs of the National Business for the 4 months prior to the sale in FY22 are included in the Retail Residual statements.

3. INTER BUSINESS BALANCES

The Balance Sheet statements for the Businesses include balances relating to the charges from the Wholesale business to the Retail business assuming a 30 day payment cycle.

Charges by the Wholesale Business to the Retail Business and Other Licenced Operators (OLO's) are made on the basis of Refrerence Offer prices for the relevant products where available.

4. RESTATEMENT OF PRIOR YEAR COMPARATIVES

Following the disposal of the National Business segment, management undertook a comprehensive review of the fixed asset register during the year to identify any assets which have been replaced or decommissioned. As explained in the Annual Report (page 41), this included assets on the register in FY22, and resulted in a restatement to the prior year comparatives.

Some costs in the cost model used to prepare the RFS are allocated on the basis of gross replacement cost ("GRC"), being the current cost equivalent of gross book value ("GBV"), and so prior year comparatives for FY22 in the RFS have been restated based on amending the cost allocations to reflect the restated GRC (there was no change in the allocation methodology, only the allocation percentages based on GRC's).

The impact of removing the GRC in each of the market is as follows

	Wholesale Local Access in the Hull area		Wholesale Market for Leased Lines within the Hull Area	
	FY22 Previously Reported	FY22 Restated	FY22 Previously Reported	FY22 Restated
Revenues	21,389	21,389	5,605	5,605
Total Operating Costs	(8,004)	(8,196)	(4,506)	(3,709)
Return	13,385	13,193	1,099	1,896
MCE	76,217	76,481	12,336	11,177
ROCE	17.6%	17.2%	8.9%	17.0%

Annex 12

Reconciliation Statement

Consolidated profit and loss account

for the year ended 31 March 2023

	Turnover	Operating Costs	HCA Return or Profit before taxation	Holding gain/(loss) and other Adjustments	Supplementary depreciation	CCA Return or Profit Before Taxation
	£k	£k	£k	£k	£k	£k
Market/Area						
Wholesale SMP Markets	30,479	(19,144)	11,335	12,820	(1,770)	22,385
Residual activities						
- Wholesale residual activities	74,172	(52,273)	21,898	5,723	(2,243)	25,379
- Retail residual activities	90,866	(110,738)	(19,872)	15,218	(1,523)	(6,176)
Total	**195,516**	**(182,154)**	**13,362**			
Adjustments (as necessary)						
Elimination of Inter Business turnover and costs	(94,303)	94,303	-			
Other operating income			-			
Goodwill			-			
Group’s share of profits of associates and joint ventures			-			
Profit on sale of fixed asset investments			-			
Profit on sale of Group undertakings			-			
Amounts written off investments			-			
Profit on sale of property fixed assets before exceptional items			-			
Profit on sale of property fixed assets			-			
Net short term interest payable			-			
Finance income			1,451			
Finance costs			(9,183)			
Long term interest payable			-			
Rounding differences						
Finance Costs attributed to discontinued operations						
Discontinued Operations			-			
As per the KCOM Group Limited Annual Report (page 23)	**101,213**	**(87,851)**	**5,629**			

Reconciliation Statement

Consolidated profit and loss account
for the year ended 31 March 2022 (restated) (Note 4.)

	Turnover	Operating Costs	HCA Return or Profit before taxation	gain/(loss) and other Adjustments	Supplementary depreciation	CCA Return or Profit Before Taxation
	£k	£k	£k	£k	£k	£k
Market/Area						
Wholesale SMP Markets	26,994	(18,439)	8,555	7,532	(998)	15,088
Residual activities						
- Wholesale residual activities	65,196	(50,680)	14,516	5,100	(1,413)	18,203
- Retail residual activities	137,047	(139,457)	(2,410)	9,800	(1,449)	5,941
Total	**229,236**	**(208,575)**	**20,661**			
Adjustments (as necessary)						
Elimination of Inter Business turnover and costs	(83,837)	83,837	-			
Other operating income			-			
Goodwill			-			
Group's share of profits of associates and joint ventures			-			
Profit on sale of fixed asset investments			-			
Profit on sale of Group undertakings			-			
Amounts written off investments			-			
Profit on sale of property fixed assets before exceptional items			-			
Profit on sale of property fixed assets			-			
Net short term interest payable			-			
Finance income			931			
Finance costs			(8,309)			
Long term interest payable			-			
Rounding differences			(5)			
Finance Costs attributed to discontinued operations						
Discontinued Operations	(44,658)	31,128	(13,530)			
As per the KCOM Group Limited Annual Report (page 23)	**100,741**	**(93,611)**	**(253)**			

Reconciliation Statement

Consolidated mean capital employed	2023	2022 (Restated) (Note 4.)
for the year ended 31 March 2023	£k	
Consolidated mean capital employed		
Shareholders' funds as per the KCOM Group Limited Annual Report (page 24)	35,294	54,988
CCA Adjustments	80,086	52,762
Adjustments		
Investments	(46)	(81)
Retirement benefit asset	(7,522)	(40,543)
Deferred tax assets	(5,208)	(4,149)
Finance leases	4,662	8,759
Provisions for other liabilities and charges (short)	1,397	303
Bank loans	-	-
Loans from related parties	165,500	151,664
Retirement benefit obligation	-	-
Deferred tax liabilities	15,412	24,763
Finance leases long term	6,725	12,344
Provisions for other liabilities and charges	1,795	3,682
Finance lease receivable ST	(3,578)	(7,290)
Finance lease receivable LT	(5,646)	(10,490)
Other differences		(6)
Closing CCA capital employed at 31 March	**288,871**	**246,706**
Opening CCA capital employed as 1 April	246,706	265,978
Adjustment to opening CCA Capital employed at 1 April	(1,072)	(185)
Revised Opening CCA Capital Employed at 1 April	245,634	265,793
Average CCA Capital employed	**267,252**	**256,249**
Mean Capital employed of SMP Markets		
Wholesale Local Access	87,602	76,481
Wholesale Broadband Access	11,460	11,177
Sub total markets	**99,062**	**87,659**
<u>Residual activities</u>		
- Wholesale residual activity	69,429	63,822
- Retail residual activity	98,762	104,768
Total CCA Mean capital employed	**267,252**	**256,249**