



16th September 2016

CWU and Prospect Submission to Ofcom's consultation on Strengthening Openreach's strategic and operational independence

Introduction

This is a joint submission from the Communications Workers Union (CWU) and Prospect. Between the two unions we represent the vast majority of BT employees, including all of the company's Team Members (non-managers) and the company's reward framework workforce. We are the only unions in the UK with formal recognition in BT and the only unions with membership in BT.

Each union has already made submissions to Ofcom's Digital Communications Review and, jointly, the CWU and Prospect have written to Ofcom on a number of occasions and have had a number of meetings with Ofcom's representatives. We are grateful to Ofcom for making the time to meet us regularly, and for the fact that Ofcom has clearly taken account of our views in a number of respects in formulating its proposals.

In this submission, we concentrate on a small number of key issues, as these issues relate specifically to the job security, pensions and terms and conditions of our members, as well as to the ability of BT to fund, invest in, and improve the customer experience of, the UK's telecoms networks and services.

Whilst this submission will concentrate on these key issues, it is important for us to point out that, on Ofcom's own statistics, the UK actually has one of the most comprehensive broadband networks anywhere in the world. Whilst we would wholeheartedly accept that no change is not an option, it is important in our view to recognise that the UK has enjoyed a genuine revolution in broadband coverage over the last decade and a half – and that this has been achieved largely by BT alone. Moreover, BT embarked on its massive investment in transforming broadband through Fibre in the teeth of a worldwide recession towards the end of the first decade of the 21st century. No other provider did so. Not a single other provider, for example, has significantly embraced the BDUK programme. As far as we are aware, not a single other provider has sought to describe itself as willing to contribute to the provision of a Universal Service Obligation (USO) for 10Mb broadband. That is more or less bound to fall entirely on BT to provide and we have supported this investment as being vital for the future security of our members in BT – this remains the case today.

BT is – and will always be – at the heart of the UK’s telecoms infrastructure. Whilst some of BT’s competitors would like to give the impression that they contribute too, the reality is that, with the limited exception of Virgin Media, they do not and have no intention of contributing and the Fix Britain’s Internet campaign is a chimera. What happens to BT and Openreach as a result of the DCR will almost entirely determine what will happen to broadband provision over the next decade and more. We are inevitably, and rightly, concerned about the occupational interests of our members. We also want BT to succeed as that is self-evidently in our members’ long-term interests and what is good for BT is generally often good for our members. But we also want broadband to be ubiquitous and genuinely great in the UK as a matter of social policy. We are as committed as Ofcom to the right outcomes for the UK from the DCR. For both unions, this goes beyond the narrow employment-related interests of our members.

The Latest Proposals – strengthening Openreach’s strategic and operational independence

Certain aspects of the current proposals from Ofcom, as they stand, are deeply troubling. We believe that, should they be implemented, they will damage ‘UK plc’ by undermining the development of the UK’s telecoms infrastructure and also BT’s ability to provide decent customer service. They could also bring a series of challenges and problems for BT employees – particularly for Openreach employees but potentially for all employees.

We have seven principal areas of concern about the current proposals:

1. The proposal that there should be a transfer of assets from BT to Openreach.
2. The proposal for the separate legal incorporation of Openreach.
3. The proposal that BT’s Openreach employees TUPE transfer to Openreach.
4. The potential for the current proposals to cause significant collateral damage to the BT Pension Scheme covenant, and the potential for the proposals to deny our Openreach members the ability to remain in the BTPS in respect of future service.
5. The proposal that Openreach should undertake its own R&D.
6. The proposals for ongoing review of BT as set out in Section 6 of the latest report.
7. The proposals for a separate independent board for Openreach.

What follows concentrates on each of these specific issues.

1. The proposal that there should be a transfer of assets from BT to Openreach.

We want to deal with this first as we believe this aspect of the proposals goes to the heart of this latest Ofcom report, in terms that would impact on our members directly. By seeking a transfer of assets, Ofcom would potentially create an environment in which the unified nature of the telecoms network would be seriously undermined; in which it could become impossible to avoid the need for a complex, expensive and very difficult TUPE transfer of members between BT and Openreach; in which there could be real damage done to the BT Pension Scheme covenant; and which would in any

event be an extremely difficult, time-consuming, expensive and an ultimately largely arbitrary process.

Openreach inevitably has a presence in every exchange building in the UK, as the local loop needs to physically inter-connect with the back-haul network. The existence of a separate 'local loop' (the part of the network Openreach is responsible for), whilst important in terms of providing equivalence, is essentially a regulatory construct. It is self-evident that the local loop, on its own, is unable to provide any telecoms and data inter-connectivity. It is only through its attachment to a back-haul network (operated by BT TSO, or indeed to a third-party provider) that it is actually able to provide any services at all. Likewise, of course, the back-haul network, on its own, cannot provide any customers (other than wholesale re-sellers) with any products and services. The *engineering* reality is that BT has a unified network in the UK which it owns and operates, whilst there is a purely *regulatory* separation of the local and back-haul portions of this network.

- Who would own these shared exchange buildings?
- Which - TSO or Openreach (or indeed other Lines of Business: many buildings are occupied by employees from every BT Division) – would pay for their upkeep?
- What about the exchange equipment itself?
- How would BT partition the capital and running costs of this unified network?
- How would corporate overheads be partitioned between Openreach and BT?
- What about IT systems, which as an issue is potentially extremely significant? BT reports that it spent £1 billion on creating separate IT systems and processes (and, an even more complex exercise, migrating existing data and processes to them) as a result of the 2005 Undertakings. That separation exercise – which, eleven years after the Undertakings were signed, still has some residual elements ongoing due to its immense complexity – in the main 'only' covered systems holding customer data. However, BT has many hundreds of "enterprise management" IT systems covering finance, HR, legal, resource management, procurement, supply chain, fleet management, internal communications, investor relations, etc. These are BT Group-wide systems, so do we have to go through a similar and extremely expensive exercise to that which was undertaken for systems holding customer data? Also, under the Undertakings BT is permitted, with appropriate safeguards, to host Openreach and Rest of BT systems in a single set of data centres. Would Openreach systems need to be moved to their own data centres? All of these things would introduce large extra cost for BT and divert money and people from other activities which directly benefit customers and the industry.

This proposal to transfer assets would in itself have a potentially harmful impact on the pension scheme covenant. Would it also be envisaged that the past pension liabilities as between Openreach and BT be partitioned? (We don't think this could be done since as far as we know, the records of previous employment by Line of Business simply do not exist or go back far enough to enable it to be done). What about future service liabilities? Would they too be partitioned? If so, the impact on the covenant would be immediate and significant – in essence it would become two separate covenants, potentially with different strengths. Even if that were not to be the case, even if it were possible to maintain a singular approach to future service liabilities (which seems unlikely to us), it is obvious

that a division of assets must have an impact on the covenant, and in our view, it must be to weaken that covenant through the Balkanisation and dilution of BT's existing assets.

The partitioning of assets could mean that a TUPE transfer of BT employees to Openreach would become legally unavoidable, no matter how unpalatable and unwise such a move would be (see Section 3 below). The Acquired Rights Directive could leave BT and the unions with no choice but to go down the TUPE road.

Any attempt at partitioning BT's assets would ultimately be largely arbitrary. It is simply not possible to determine what belongs where with any underpinning accuracy. This proposal is therefore ultimately also theoretical, rather than practical, as well as harmful and massively expensive.

2. The proposal for the separate legal incorporation of Openreach.

As well as the TUPE issue below we are concerned with this as it could well leave the BT Board and the proposed Board of Openreach without the necessary clarity about their respective functional responsibilities and accountabilities. This lack of clarity could well result in a reluctance to invest. We do of course appreciate that it could be argued that separate articles of association for BT and Openreach could in theory be drafted to enable such clarity to exist. But we would want to be convinced that this could be done and where is the evidence for this? Are there any successful examples of this structure, involving an extremely large operating division with functions central to the firm's core purpose and business model, which Ofcom can point us to? We are not aware of any.

We also believe that this proposal is inconsistent with Ofcom's acceptance that ultimately it must be BT plc's Board that makes the decisions as to how much will be invested in Openreach. We agree with Ofcom about this – it is clear that Openreach on its own doesn't have a clear source of capital to invest, that the network is anyway a single entity except in regulatory terms, and that Openreach would be far less able than BT as a whole to raise capital - but we believe that this sensible view is potentially fatally undermined by separate legal incorporation.

Again, we believe that separate legal incorporation could well have a negative impact on the BTPS covenant, as the Trustee would be obliged to consider the impact on the sponsoring employer's (or employers'?) ability and willingness to stand behind the past and future pension liabilities of two separate legal entities. Who exactly would 'own' this split covenant?

Separate legal incorporation could also drive BT legally to having to embrace a TUPE transfer, whether it wanted or needed to or not.

3. The proposal that BT's Openreach employees TUPE transfer to Openreach.

We are deeply concerned at the suggestion that all Openreach employees would need to TUPE transfer to Openreach. This would be, we believe, the largest TUPE of all time. It would be extremely complex, costly and difficult to do and would take significant time and resource to get right.

It would create inflexibility in a way that would potentially seriously undermine our members' job security, in Openreach and indeed throughout the company. BT plc has always applied a voluntary

redundancy approach. This is of utmost importance to both unions. In order to manage this, there are well tested long-term agreements in place to enable surplus staff to be redeployed between BT's various operating divisions. Over the last ten years, some 20,000 BT employees have been through the redeployment process and Openreach has been an importer of talented engineers in particular from areas where there has been surplus. Had these arrangements not been in place it arguably would not have been possible for BT to avoid compulsory redundancy. Openreach employs some 32,000 BT employees – prior to the purchase of EE that represented some 40% of BT's UK workforce. TUPE could well effectively remove Openreach from the BT redeployment process, with very serious consequences for job security across the whole of BT. Such a change would simply not be acceptable to our members. To be clear this does not mean that we have people moving out of Openreach en masse into other areas – Openreach has grown and it has been able to import people due to growth and demographic attrition, which we would expect to see continue so Openreach has been able to ensure we could provide new roles.

A TUPE could well create major employee and industrial relations challenges, with the potential need to establish new and separate recognition and collective bargaining arrangements, different terms and conditions and different industrial relations processes. None of that would be at all easy to do and could create a very unnecessary, difficult and febrile environment for both the unions and for BT. It is hard to see how any of this would add to Openreach's, or BT's, ability to deliver improved customer service. In fact we think it would do the opposite – it would be at best a massive and expensive distraction and, at worst, could cause a major industrial relations crisis driven, we would stress, by this decision, not the actions of BT or the unions.

As we say above, this would be the largest TUPE transfer of all time, and would be exceptionally challenging for employees, creating a huge level of uncertainty and anxiety for Openreach's 30,000 plus employees. As trade unions we have dealt with hundreds of TUPE transfers over the year and even small transactions can give rise to complex and difficult issues and take significant time and resource to manage. This one would be almost off the scale in terms of complexity and sheer size it could force BT down the road of two separate sets of HR process, systems and policies, and two major sets of HR and finance overheads. Having to cater for two sets of HR approaches, covering respectively some 30,000 employees in Openreach and some 55,000 employees in the rest of BT would add massively to BT's total overheads. And for what? In what sense would this improve customer service? In our view, the exact opposite would result. First, it would cause a massive distraction. Second, it would create open-ended, on-going deep issues and concerns for our members whilst also severely undermining their job security.

Ofcom has also suggested that, rather than using TUPE, BT could in some way second employees to Openreach on a service contract basis. We appreciate the intentions behind this proposal – one which is designed to signal that if a way can be found of avoiding a TUPE, then that would have Ofcom's blessing. However, as we say above, we fear that the transfer of assets from BT to Openreach and separate legal incorporation between them may make a TUPE unavoidable. We also fear that such a service contract model would pose some very awkward issues around contractual and other labour law rights for those seconded. We do not think, as far as we can tell, that this would be a practical measure to take.

We also wonder if Ofcom is perhaps underestimating the degree to which Openreach already does have quite a separate culture to the rest of BT. Although it has been the case over the last decade that Openreach has received a substantial number of redeployees from other parts of BT (notably from TSO), it has been much less the case that Openreach employees have been redeployed to the rest of BT. That's largely a reflection of the fact that employment in Openreach has been growing whilst in the rest of BT the opposite has generally been the case. Most Openreach employees have been continuously employed in Openreach (and its predecessors), often for decades. That is perhaps mainly because of the relatively specialist nature of Openreach roles for the vast majority of Openreach employees. Their jobs are simply not to be found in the rest of BT. In the past few years, Openreach has taken on thousands of employees completely new to BT. None of these individuals have in fact worked anywhere in BT other than Openreach, and that will most likely indefinitely remain the case for the vast majority of them – again, essentially because the roles they undertake are simply not found elsewhere in BT. In short, whilst we can appreciate that Ofcom would want to avoid any situation where an employee is in Openreach today and elsewhere in BT tomorrow, the reality is that this is not an everyday occurrence.

To demonstrate what we mean, we have drawn numbers from our own membership records, about the movement of employees between Openreach and the rest of BT. We estimate that less than 10% of Openreach's workforce has moved out to work anywhere else in BT since the creation of Openreach, over ten years ago. That is a very low number and demonstrates the sheer stability and insularity of Openreach's workforce. In any single year, our figures suggest that less than 1% of Openreach's workforce moves to another Line of Business. (There has been more movement into Openreach from elsewhere in BT as – see above – Openreach has been a source of redeployment opportunities for our displaced members elsewhere – particularly from TSO.) These figures are taken from our own membership systems and may not reflect the situation fully – but we would assume BT would have comprehensive statistics on the matter. It might be instructive for Ofcom to approach BT on this topic.

Notwithstanding that it may be that Ofcom currently underestimates the degree to which Openreach employees already do have a separate culture and an 'Openreach-centric' view of the world, we can accept it could be useful that this is extended to step change customer service. We recognise – and have done for some time – that there is a need for a step-change in quality of service (something we positively want to see happen) and we have worked with BT to try and achieve this. We positively want to ensure that there is an environment in which this can continue to happen. Our concern is that a TUPE and/or a worsening of the pension scheme covenant (see section 4 below) would make that environment impossible. In fact the environment would in our firm view be poisoned.

We confirm a clear and unambiguous offer that both unions will commit to accelerate discussions with BT designed to further enhance a new, different and better culture and approach in Openreach, dedicated to ensuring a better customer experience. This must be predicated on an outcome that there is no TUPE or damage to the BT covenant. We would be willing to discuss with you, when we meet, what this could entail.

4. The potential for the current proposals to cause significant collateral damage to the BT Pension Scheme covenant, and the potential for the proposals to deny our Openreach members the ability to remain in the BTPS in respect of future service.

We believe Ofcom's proposals could well have serious negative implications for the covenant which would trigger a very predictable and damaging series of events. In the current environment, any weakening of the covenant would be very likely to result in higher repair payments from BT, possibly over a shorter period. This, in turn, would inevitably reduce the amount available for investment in the UK telecoms infrastructure, including of course in Openreach, and as such would be totally self-defeating in relation to Ofcom's own stated objectives for the Digital Communications Review.

We urge Ofcom to understand how significant this could be. We are not in a position to put numbers round the impact on the covenant, therefore we cannot ourselves give a numerical estimate of the impact this aspect of Ofcom's proposals could have on BT's ability to invest in the network, as opposed to making deficit repair payments. However, we assume that the BTPS Trustee could do so and we would urge Ofcom – if necessary in confidence – to seek such evidence from the Trustee. What we can however say with certainty is that we believe the impact on the pension scheme covenant is highly likely to prove utterly disproportionate.

We are also very concerned about whether or not our members in Openreach – if it becomes a separately incorporated body (albeit wholly owned by BT) - would even be able to continue in active membership of the BTPS. Any attempt to cease active membership of the BTPS for Openreach employees would be highly likely to create irresistible pressure for a major industrial dispute (which in itself would have significant implications for the covenant as well as for customer service). We believe that Ofcom recognises this distinct possibility as it has repeatedly stressed to us in our meetings with Ofcom that they do not want to create a 'breakdown in labour relations'. Nevertheless, as things currently stand, we cannot be certain about the ability of Openreach employees to remain active members of the BTPS, whilst we can be certain that any inability to do so would cause an industrial relations crisis.

There could be serious and complex implications for the Crown Guarantee arising from Ofcom's proposals. It is not clear to us that this guarantee could any longer stand behind Openreach members of the BTPS if Openreach were to be separately incorporated. Ofcom has told us that the Treasury has been approached over this issue and believe it can be relatively simply resolved. We are far less sanguine. Given the huge amount of time merely legally clarifying the Crown Guarantee took, we are concerned that this issue could result in protracted, expensive and complex legal issues again. Moreover, since we know that the Treasury has always sought to minimise the extent of the Crown Guarantee, we are also concerned that any formal approach on this issue to the Treasury could well open a Pandora's Box, raising serious questions about the long-term security of our members' pensions.

Overall, we view the combined potential impact of a TUPE transfer and the collateral damage to pensions as, between them, creating huge potential problems. We know Ofcom is committed to

bringing about a fundamental improvement in customer service. We share that ambition. We know that bringing it about is likely to involve some very hard issues for the unions and for our members. How would we convince our members about the need for change against the background of a massive, complex and difficult TUPE and potential damage to the pension scheme and to their continued membership of it? The answer is clear – it would be impossible. Hence we believe that these proposals would directly and fatally undermine the key objectives of the DCR – that customers should get a better quality of service and that the UK should enjoy better connectivity.

5. The proposal that Openreach should undertake its own R&D

Whilst on the face of it, the proposal that Openreach should have the capacity to undertake its own research seems relatively innocuous and uncontroversial, we believe this would be extremely expensive to set up and also perhaps misunderstands the nature of network research and development. As we say above (Section 1), the existence of a separate ‘local loop’ is essentially a regulatory construct. The local loop, on its own, is unable to provide any telecoms and data inter-connectivity. It is only through its attachment to the back-haul network (operated by TSO) that it is actually able to provide any services at all. The back-haul network, on its own, cannot provide any customers (other than wholesale re-sellers) with any products and services. The *engineering* reality is that there is a unified network in the UK owned and operated by BT whilst there is a purely *regulatory* separation of the local and back-haul portions of this network.

It therefore follows that the sharp division between BT and Openreach which we fear would flow from Ofcom’s current proposals could result in reluctance on the part of BT to continue with its very substantial commitment to network R&D, with serious consequences for UK network development. That would self-evidently be bad for both ‘UK plc’ and for the thousands of our members who work in BT’s research and development centres.

6. The proposals for ongoing review of BT as set out in Section 6 of the latest report

A worrying feature of Ofcom’s proposals is that BT and Openreach would be subject to virtually continuous review, with at first six-monthly and then yearly reports from Ofcom about the new approach. This would generate serious regulatory uncertainty in our view, which is the opposite of conducive to an environment in which BT (or other Service Providers) would invest in the UK’s telecoms infrastructure. BT could not be certain from one year to the next that it will even continue to own and operate Openreach. As such we believe this proposal is disproportionate. The level of on-going uncertainty it would bring for our members is unnecessary and would be unacceptable for the unions – this ‘sword of Damocles’ would be counter to getting the best from BT people and the best service for BT customers. Consequently, we do not support this proposal and can see no evidence to justify it.

We also believe that this proposal, as currently presented, would provide BT’s competitors with both the invitation and the means to ‘game’ the review process. The Fix Britain’s Internet campaign is the clearest possible indication of the intentions of BT’s major competitors to keep campaigning to break BT up, because that’s in what they perceive to be in their best commercial interest. It is therefore obvious – they are giving clear notice of this – that they will seek to intervene in this proposed

review process. They will have the means – and they are giving notice of the intention – to ensure that these reviews will take place on the grounds of their choosing. As such, the likelihood is that these reviews will become a major opportunity to re-run the Ofcom DCR on an annual basis – with dire consequences for the industry as a whole in terms of regulatory stasis. That on its own would be likely to leave BT's Board wondering at the wisdom of committing substantial investment resource to a part of BT (Openreach) that at any point it could cease to own.

7. The proposals for a separate board for Openreach.

In Section 4 (and in particular 4.15 and following) Ofcom proposes a separate Board for Openreach. Notwithstanding our opposition to separate legal incorporation, we can see merit in Openreach having an independent Board, and for this Board to consist of a majority of members who are independent of BT (and of Openreach). We also believe there would be considerable benefits for there to be worker representation on this board. We propose to discuss this with BT after discussing it with Ofcom. Openreach has a very highly unionised workforce. It is not always a happy ship. There is real merit in seeking to build a new culture and a new approach to employee relations, and one way to contribute to that could well be to adopt an idea that we note has been floated by the UK Prime Minister – worker representation on the board. We believe this would increase engagement and commitment in the Openreach workforce.

Conclusions

In this brief submission we have sought to concentrate on what we believe to be the key and critical issues raised by the 26 July 2016 report. We look forward to meeting with Ofcom to discuss its content.

16th September 2016