

The Bit Commons response to Ofcom's consultation on Directions for Regulatory Financial Reporting – January 2015.

The Bit Commons thanks Ofcom for the opportunity to respond to the consultation on Directions for Regulatory Financial Reporting. The Bit Commons congratulates Ofcom on the quality of its work. The Bit Commons is also grateful for the earlier interjection to secure quarterly reporting of state aid by BT. The Q2 state aid cash receipts of some £96m reported by BT do exceed the guidance provided to analysts of £300-£400m spent annually during the peak of the commercial roll out of FTTC. With even the minimum of transparency, it means decision making can be improved on aid intensity and amendments made to how state aid measures are enforced.

The Bit Commons is responding in two capacities. The first is of general interest arising from working with SME's who are not yet benefitting from the NGA roll out. The second motivation is as a provider of written evidence to the NAO (National Audit Office), Public Accounts Committee (PAC), and the EFRA (Environmental, Food and Rural Affairs) Select Committee, who have each expressed concerns about the lack of transparency with regards to the high levels of state funding in the rural broadband programme. These sentiments were at least endorsed by Dame Patricia Hodgson, Chairman of Ofcom who stated in evidence to the Communications Select Committee (HOC) on Dec 4th, 2014 that it was 'a legitimate concern' that public monies directly or indirectly could be moved from network investment to other projects. The adjustments being recommended in this response are aimed at improving that transparency while respecting BT's need for commercial confidentiality.

Comments are restricted to VULA reporting, question 5, and these are in the form of proposed four recommendations to be included in the existing proposals where the public interest can be served without impinging on the need to respect commercial confidentiality.

Consultation Question

5.1 Do you think the proposed revisions to the scope, form and content of the Regulatory Finance Statements fairly reflected the decisions of the Fixed Line market review and are necessary to ensure that we have the information which we need to carry out our functions?

In any normal circumstance the Ofcom proposals look perfectly adequate. Ofcom have also attempted to deal with the exceptional circumstances of state aid investment of some £1.7bn in rural broadband in section 5.17 '*where in a third private schedule, the report will outline how BT has allocated the government grants*'.

The following recommendations, while issues of substance are not substantive changes but I hope are constructive but necessary modifications, given what are exceptional circumstances.

Separate reports for FTTP and FTTC

Recommendation 1. An important but minor point, Ofcom should consider a report for FTTC and other copper dependent variants and a separate report for FTTP. This information will inform Ofcom of the costs and thus incentives needed should more FTTP become a priority. It is likely a significant number of premises will benefit from FTTP from the initial Phase 1 BDUK contracts totalling £1.2bn should counties complete full cost reconciliation activity against the original milestone payments and spend the monies extending NGA coverage.

BDUK phase 1 funding is already delivering 4-5% of premises FTTP in Surrey. The availability of FTTP is likely to grow in most counties as funds are recovered through cost reconciliation activity, the surrendering of Universal Service Commitment premiums and revenue from clawback clauses once the 20% take up threshold is passed.

This minor change should also begin the process of informing Ofcom of the relative actual costs of operating all fibre networks compared to legacy PST networks.

From Allocation to impact analysis of State Aid investment.

With reference to the private report outlined section 5.17. Should this be an 'allocation' by BT or should the report show the full impact of £1.7bn of public investment on the VULA wholesale price? There would appear to be a benefit to BT, Ofcom and the Government that such an impact is made clear. The more efficient BT uses the available public investment the less the impact on future VULA prices in the FLAMR 2017. The state aid is supposed to be gap funding not replacement funding. It is made clear in the State Aid Measure 33671 approving the UK scheme that Ofcom would assist BDUK in securing value for money. This reporting mechanism ought to be used to make clear the intensity of state aid. The more state aid used the greater the possible impact on VULA pricing in the future.

This proposed report should make the impact of state aid on VULA pricing very clear to all stakeholders. The private report should also be available to the NAO office acting on behalf of all Government agencies. It should also be available to European Commission when reviewing the state aid measure SA.33671.

Recommendation 2 – The private schedule should include the impact of state aid on VULA wholesale prices, specifically the increase in price should BT have invested 100% of their own capital or indeed the reduction in VULA as a consequence of the state aid investment.

Recommendation 3 – The final Ofcom decision when published should include an illustrative example of the impact of the £1.7bn state aid on VULA pricing and how the efficient use of state can reduce that impact. Ofcom should use this measure in support of ensuring BT do not game or graze on state aid funds, or use the Superfast Extension Project (SEP) to reduce their commercial footprint. The latter is occurring on all SEPs so far announced.

Creating a Reliable Public record of NGA investment.

The cost of NGA upgrades have been the subject of many studies. The BSG/Analysis Mason study in 2009 forecasted FTTC costs to be circa £5-6bn, while full FTTP would be close to £30bn.

It is likely the overall cost for FTTC will be significantly lower than originally forecast, e.g £3.5bn (see below) versus £5-6bn. If this can be confirmed then this will inform public policy on the levels of incentives and the timing of these incentives for full fibre access networks. There is a public interest to know how far the state investment can be stretched so future incentives can be designed and their impact understood. This can be done without impinging on BT's need for commercial confidentiality on the detail cost of their components. However there is a public interest to protect not just relating how state aid is accounted for but the need to secure the full potential economic impact from what is an ongoing revolution in being connected and online to the global internet.

Given the concerns expressed by the NAO, three PAC hearings, two EFRA hearings and more than 300 parliamentary questions on the subject of rural connectivity The Bit Commons would propose that a key facts sheet is created to verify and provide a trusted public record of the basic parameters. This would enhance and support Ofcom's VULA reporting objectives, while providing the institutions of Government a public record that could be relied upon. The primary objective is to provide confidence in the basic numbers being regularly used by Ofcom guidance to stakeholders, Government and Parliament.

The fact sheet or table would set the record straight on the following matters ;

- 1.) Reconcile BT's often quoted £2.5bn NGA private investment, with the guidance given to BT Analysts. The £2.5bn has been used widely to inform public opinion and public policy. How much of this money is capital, how much is incremental to the existing Openreach capital envelope? How much is operational costs, and how many years operational costs are counted.
- 2.) BT made public their promise of an additional £1bn capital to match the investment by Government in rural broadband, but the NAO could only find reference to about £350m capital in their 2013 report.
- 3.) Ofcom have referenced in their documentation £530m BDUK programme but not the full £1.7bn public investment in state aid once the Superfast extension projects are let.
- 4.) The NAO reports relying on inputs from BT and BDUK showed that 20% of the £1.2bn state aid contracts was for future proofing. There is no white paper describing the nature of that future proofing or a public record of the nature of the publicly funded future proofed assets.
- 5.) Some note should be provided on the state investment will impact the cost of fibre services to mobile operators, in locations benefitting from the state aid investment in rural areas.
- 6.) Account should be taken of the reduction in commercial NGA footprint where SEP are being approved.

It would seem appropriate that the basis upon which Ofcom is beginning VULA reporting should be documented so there is a public record that can then be relied upon.

Recommendation 4 The following draft table could be completed and audited and published. It is a suggestion and the format can be modified to meet the needs of all stakeholders. It addresses point 1 to 5.

Year	Openreach Capital	BT NGA (capital) Estimate* within BT capital budget	BT operational costs- No estimate available.	Public funding of NGA estimate	Accumulated premises served from a Cabinet	Accumulated premises capable of receiving superfast broadband	Accum. premises That can order FTTP
2009/10	£907m	£300m					
2010/11	£1078m	£300m			4m		
2011/12	£1075m	£350m			10m		
2012/13	£1144m	£350m		£100m	15m		
2013/14	£1049m	£350m		£200m	19m		
2014/15		£80m*		£400m			
2015/16		£80m*		£400m			
2016/17		£80m*		£400m			
2017/18		£80m*		£200m			
Totals		£1.9bn		£1.7bn			

Notes in the 2010/11 annual report BT reported an accumulated spend of £600m from the £2.5bn to pass 4m premises, so I have split it £300m for 09/10 and £300m for 10/11. It would suggest that the £300m would have included operational costs.

The £350m is the halfway point between £300-£400m provided by BT as guidance to analysts.

The £80m per annum is a Bit Commons estimate dividing the c£350m identified by the NAO in its Rural Broadband report and showing a crude distribution for illustrative purposes. Note the unexplained operational costs are excluded from this analysis.

The £1.9bn total from BT is current Bit Commons estimate for what was a combined capital commitment of £2.5bn for the commercial rollout and a further £1bn of matched capital offered to support rural. This is an opinion, not fact, based on the data that is available in the public domain.

I have ignored operational costs as they tend to be used inconsistently and there is means of verifying what they contain and the number of years of operational costs that might be included in the any calculation. They tend to be used to bridge any anomaly in the numbers.

The £1.7bn is total to be contracted by BDUK. It includes the superfast extension project.

The combined sums of £3.6bn will include the provision of some 90,000 VDSL cabinets and further 8-10% premises equipped to order FTTP.

Implications

The implications I hope are self evident. The rollout of FTTC is an immense engineering achievement. It was cheaper and faster than anyone predicted which is profoundly unusual. This creates its own challenges.

I hope I have shown enough here to at least prove that the task needs to be reported and numbers calculated professionally.

Stakeholders should be given the opportunity to appreciate the impact of the cheaper, faster rollout with significant Government support. The impact of £1.7bn state aid on VULA pricing going forward should be at least shown illustratively.

It is possible to show that by extending fibre from the AGN nodes that FTTP to manifolds on a Distribution Point that FTTP would cost substantially less than that estimates completed in 2009.

I hope Ofcom can consider these recommendations and use them. This paper has not been subject to peer review so I hope the recommendations could be refined by other stakeholders before the process is concluded.

The other points raised on future proofing and the implications for supporting mobile services needs to be picked up in other Ofcom consultations and I will endeavour to do that.

I believe if these recommendations are followed they can make a meaningful contribution to reduce the temptation offered BT to use the imposition of commercial confidentiality agreements on Local Authorities to extract more and to contribute less funds to the rural broadband programme.

End.

Contact: Mikekiely01@btconnect.com