Cover sheet for response to an Ofcom consultation

BASIC DETAILS

Consultation title: Changes to BT and KCOM's regulatory and financial reporting 2012/13 update

To (Ofcom contact): David Brown

Name of respondent: Mike Kiely

Representing (self or organisation/s): The Bit Commons Limited

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Please tick below what part of your response you consider is confidential, giving your reasons why

Nothing	X	Name/contact details/job title	
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Name Mike Kiely Signed (if hard copy)

The Bit Commons

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12-2-2013.

Dear Mr Brown,

Thanks for the opportunity to reply to the consultation on changes to BT regulatory and financial reporting.

The particular change I wish to request arises from the likelihood that BT will in the next few years benefit from some £1.4bn in state aid to upgrade rural NGA networks, and may benefit even more if additional funds become available or are requested for a fibre transition activity. The latter could begin with some of the current £150m urban broadband fund and the £300m set aside from the TV licence fund in 2015-2017.

The current BT Undertakings and associated regulatory reporting do not cater for the eventuality of very large cash subsidies by the state and the need for the state to achieve value for money. Indeed BT's discretion in how it recovers its costs are, it could be argued being used by BT in the rural NGA programme to act as barrier to providing an adequate level of transparency so value for money can be established.

Ofcom will accept BT has an enduring monopoly in the local access network, hence the BT Undertakings. Ofcom through the current and the 2010 market review for WLA/WBA will confirm that the lack of demand for investing in infrastructure has meant passive infrastructure access (PIA) products are not as developed as they might be. This is understandable as verifiable demand for PIA did not emerge in the 2010 market review process. Thus resources and energies were not fully applied to PIA development and Ofcom's conclusions based on the evidence available were reasonable. This has led to a near exclusive reliance by Ofcom and the BDUK programme on BT's FTTC/FTTP VULA based NGA solutions for the rural NGA programme.

It is no surprise therefore that BT has come to dominate the BDUK competitive dialogue process and subsequent Local Government call off process. Neither should it be a surprise that given the discretion BT has in recovering costs it remains challenging to secure value for money. The evidence given by the Minister Vaizey to the EFRA committee examining on November 28th confirmed that the search for Value for Money was a work in progress. He should be congratulated for his candidness.

The press releases announcing the BDUK supported projects are suggesting a public subsidy in excess of £200 per premise <u>passed</u> for a largely FTTC based solution. This contrasts with circa £70 public subsidy per premise passed for a near same solution for the BT Northern Ireland NGA project.

My concern was enhanced on December 16th, when on a BBC Radio 4 broadcast a representative of Openreach stated a VDSL Cabinet/Path costs £100,000 each and every BT exchange would cost millions of pounds each to upgrade. I cannot find any publicly available data to suggest the costs are anything like the numbers used in the broadcast. In line with BT 21C announcements, possibly only one in five exchanges in rural areas will act as handover points requiring a fibre rack and layer Ethernet switch will be installed. These data transport facilities have a bill of materials a fraction of £1m let alone millions. In terms of VDSL cabinet costs, fully equipped single cabinets can be purchased for circa £15,000 before industry discounts. If there is the remotest chance that BT's cost recovery for NGA rural is informed by the numbers in the BBC broadcast or significant fractions of those numbers , and the press announcements for the Local Authority projects suggest this is a possibility, then Ofcom given their statutory duties need to act.

It should be noted that in evidence to the House of Lords in the summer of 2012, Rory Stewart MP provided evidence of a per path and VDSL cabinet costs of £90k for three or £30,000 each for three very rural communities in Cumbria. This provided a very useful upper cost bound for a single community served by a cabinet in late 2011 early 2012, Since then BT estimates appeared to have accelerated upwards as Fujitsu's interest began to fade. It is the disappearance of a sensible upper bound on a cost per fibre path/cabinet and the lack of verifiable rate card for the kit and labour that makes it difficult of not impossible to establish value for money. Yet all of these costs are readily available to BT from their commercial roll and the public funded rollouts in Northern Ireland and Cornwall.

Temporary changes in the regulatory accounts aimed at highlighting the key incremental costs would provide a quick and easy way to create the correct level of transparency so value for money can be secured. This would permit Government if it wishes, to apply additional resources to assist in a fibre transition plan. The current lack of cost transparency and BT's reliance on pernicious confidentiality agreements to prevent these costs being revealed will act as a deterrent to future public investment in the UK's communications market.

The measures aimed at achieving value for money outlined in the state aid approval SJ33671, over rely on benchmarking one BT project against another, and on clawback. Given the four year case on Ethernet pricing, and the exhaustive work Ofcom has done on this case which is still likely to be challenged by BT, then it is unlikely clawback will prove a useful measure in containing BT cost allocations.

In the light of the above, I have a drafted and attached a simple spreadsheet which I am proposing BT should complete as a part of its legal responsibilities in generating its regulatory accounts. It is meant to clearly identify incremental costs, BT's 'up to £1bn investment (be it cash, capitalised labour, SGA, depreciation) in rural and the proportion paid by the combined public funding pots. The draft is not complete and will need peer review. It is primarily produced as reference point to begin a discussion.

This does not replace any of the BDUK Framework, which is essential to a rapid roll-out but seeks to ensure the Framework contracts are reconciled on actual incremental costs consistent with what state aid is intended to achieve. This action will allow NGA solutions to be delivered well into the final 10% and indeed 5% of most rural areas, while creating the conditions for more public investment in a critical national resource should that be deemed necessary. Clawback and the benchmarking proposed in SJ33671 are insufficient measures to secure value for money given the cost escalations identified above, BT's discretion in allocating costs; BT's lack of transparency and it's use of confidentiality agreements for what is publicly subsidised work suggest BT is treating this as a wholly commercial negotiation rather than the receipt of a possible £1.4bn subsidy on assets with BT will manage and own.

I do hope Ofcom recognise the need to protect the needs of rural users and assist BDUK and local authorities in securing value for money. A competitive dialogue with a monopoly access provider and a framework constructed to comply with state aid approval cannot of themselves assure value for money.

Given this is a matter of public interest and the BDUK funding is the first major public investment in networking since BT's privatisation, I will also include this request in consultations on Ofcom's annual action plan while copying to EFRA and PAC in the House of Commons in the hope the matter can be addressed between you.

Yours sincerely

Mike Kiely,

Founder, The Bit Commons.

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