

# Compensating Providers Delivering Universal Services Consultation Response

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## 1. Executive Summary

**BT is on a mission to help UK families, businesses and communities to access digital services. BT is ready to do its part to ensure universal connectivity. But it must be a joint industry effort, with the costs of serving the most remote areas shared fairly.**

- 1.1 BT has played a pivotal role in connecting the vast majority of UK households with broadband services, and helping to transform some of the most remote communities in the UK. Superfast broadband (speeds of 24 Mbps or more) is now available to over 96% of all households and this is set to rise further as investment continues.
- 1.2 In the future, gigabit-capable connections – principally via fibre to the premise (FTTP or 'full fibre'), and 5G, will be vital to future-proof the UK's digital infrastructure. Full fibre build is accelerating in the UK – over 10% of premises have access to FTTP, and 5G is available in 19 cities and over 30 towns with more to follow. This is a national priority, but significant investment, alongside policy and regulatory change and joint work and support by the whole of the industry, is needed to ensure they are available across the country in a timely way.
- 1.3 BDUK funding has been vital to improving household connectivity in remote and higher cost areas. For example, with the assistance of various government funds, Openreach has delivered 5 million Superfast capable premises across the UK. Over the next 12 months the extension of existing state aid projects is likely to address another 80,000 premises. Further, BT have been awarded preferred bidder status for all three of the new state aid funded R100 broadband programme tranches in Scotland.
- 1.4 As well as getting Superfast and Ultrafast to as many premises as we can as quickly as possible, we want to ensure as many people as possible have access to decent broadband. The broadband USO helps reach premises that have proven to be uneconomic (typically due to the infrastructure required per household) even with the help of government funding to date. BT is committed to providing the skills and resources to deliver services to such households.
- 1.5 The financial burden of building the infrastructure necessary to make these services available on a universal basis cannot be for BT alone. The broadband USO is a policy choice, and without further government support, the net costs of delivering this essential infrastructure must be fairly shared by all industry participants. This is especially important where the funded infrastructure creates retail opportunities for all industry participants who choose to use it, not just BT. To do otherwise would unfairly preclude some CPs from becoming Universal Service Providers (USPs) in the future, and be fundamentally unfair to current USPs.

**We welcome Ofcom's proposal for a framework for all USO obligations which establishes the underlying principles for cost recovery now and in the future**

- 1.6 We welcome Ofcom's decision to have a single framework of rules and processes that USPs should follow to make a claim for any unfair cost burden involved in providing all USOs.
- 1.7 Any supplier required to undertake uneconomic activities at the request of the regulator for wider societal benefit (where not met via direct state aid funds) ought to be able to recover its efficiently incurred costs in a timely manner. These are costs which cannot be reasonably recovered from customers who benefit from the scheme. Any proposed framework and arrangements must also be able to evolve over time – in the event of future changes to a USO.
- 1.8 Given this is the first time Ofcom is consulting on cost recovery for all future USOs, it is critical that we get the underpinning principles right. In addition to existing regulatory principles of transparency, proportionality, no undue discrimination and least market distortion, any framework also needs to be light touch, flexible, timely, efficient, simple and easy to administer.

### **The costs of USOs are significant, and providers should be able to recover them in a timely way**

- 1.9 We are concerned that Ofcom's proposals are overly complex and administratively cumbersome. A simpler, more efficient framework would mean USPs would be better able to recover efficiently incurred costs. In particular:
- Ofcom should consult and notify all five steps of the cost recovery process together (validating a claim, establishing the existence of net cost, unfair burden, whether an industry fund is required, and who contributes). To do these separately needlessly lengthens the process and undermines the principle that USPs are compensated for any unfair net cost burden in a timely manner.
  - It would be reasonable for Ofcom to complete its review of a USP cost claim within a 9 month timeframe of receiving it (including the five steps above).
  - Ofcom should clarify that when considering the impact of public funding programmes in a claim, it intends to only consider clear government commitments of central funds (such as in Treasury statements and committed through government procurements).
  - Ofcom should use information it already has for calculating contributions to the industry fund, for example, the same approach that is used for the administrative levy. For the broadband USO, this would allow Ofcom to identify now which CPs will contribute what proportion under the existing ECN/ECS definition.<sup>1</sup>
  - Ofcom should make clear at the outset what it considers to be a reasonable minimum threshold for individual claims, above which Ofcom would consider it worthwhile to trigger a review of the claim.
- 1.10 Ofcom's criteria for assessing net cost burden is reasonable overall. However, we think Ofcom's approach could be clearer, simpler and less resource intensive, to minimise uncertainty. Uncertainty could, for example, create the need to provision for costs – a potentially unnecessary cost in itself. Specifically:
- BT has concerns about Ofcom considering the administrative cost burden of establishing an industry fund when assessing if a claim represents an unfair burden. Given Ofcom is proposing a complex and administratively intense process, we worry the costs of setting up and running the industry fund could be considerable, and the threshold for proceeding with a claim very high. We urge Ofcom to apply the principles set out in section 6 to ensure the process is efficient and the costs of administering the industry fund are minimised.
  - Ofcom should confirm that it will recognise the time value of money (i.e. interest) for the period between BT incurring costs and repayments being made from the fund.
  - On the finality principle, we agree that reopening past claim calculations should be limited to exceptional circumstances. Nonetheless, Ofcom should clarify that USPs can include previously rejected costs in subsequent claims, for example, where Ofcom has rejected the claim as insufficiently large to justify setting up an industry fund.

### **We broadly support Ofcom's net costs calculation and suggest improvements where it does not reflect how costs are incurred or recorded in practice**

- 1.11 We agree calculating net costs using a Net Present Value (NPV) framework is more appropriate than using depreciation and return on assets for the broadband USO. We have recommended changes to Ofcom's templates on Openreach network build costs in section 9, including:
- improving the way capital costs are reported to better reflect how networks are built in practice, and
  - simplifying the reporting of ancillary costs such as the use of vehicles.

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<sup>1</sup> As defined in the European Electronic Communications Code (EECC).

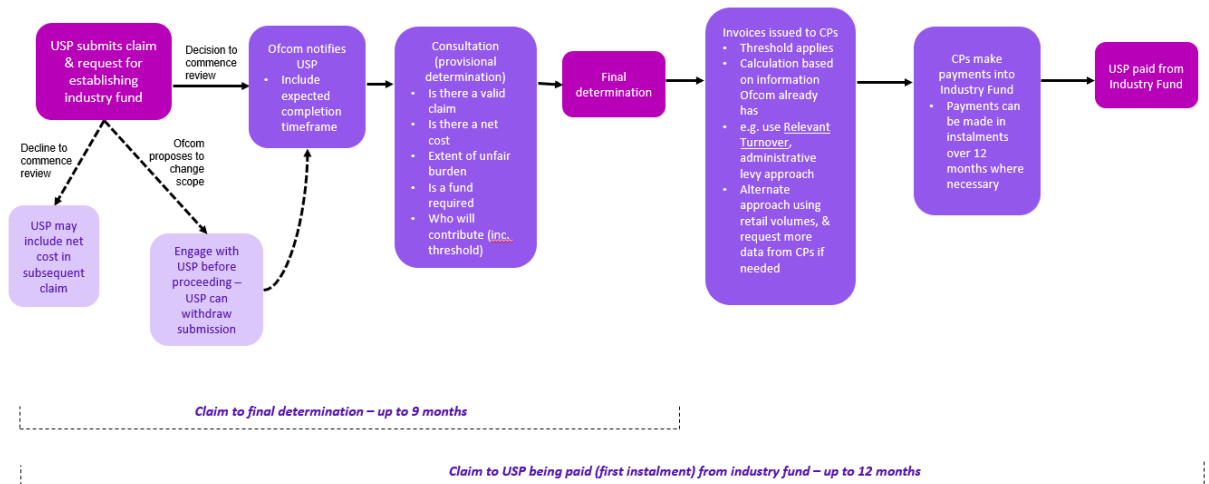
## 2. Introduction

- 2.1 BT welcomes Ofcom's Consultation on 'Compensating providers delivering universal services' ('the Consultation') published on 5 November 2019. It is essential that industry has clarity over the mechanisms and expectations around cost recovery for universal service obligations.
- 2.2 Where USO costs are not met through direct state aid or government procurement the cost burden must be fairly shared by all CPs. We support Ofcom's work to put in place a framework of rules and processes USPs should follow to make a claim for any unfair cost burden involved in providing universal services.
- 2.3 Furthermore, the proposed framework and arrangements must be flexible enough to adapt to potential future changes to any current USO.
- 2.4 Section 3 deals with the end to end process and arrangements, and the remainder of our response follows the layout of the Consultation, with the following annexes:
  - Annex 1 – Proposed amendments to the Draft Funding Regulations
  - Annex 2 – Updated NPV template & model, including BT's proposed changes
  - Annex 3 – BT Revenue assumptions

## 3. End to end process and arrangements

- 3.1 In our view the process proposed in the Consultation, while comprehensive, is complex and unnecessarily drawn out. We support its aims, but it has the potential to create opportunities to game the system and appeal decisions, and could result in a significant delay in USPs being compensated for their efficiently incurred costs.
- 3.2 We need a timely process so that it is clearer at an earlier stage which costs will be recovered, and what the ask will be for contributors – particularly as CPs may need to make provisions for a future contribution to the fund.
- 3.3 Delay is costly because we incur a financing cost associated with funding the USO as well as a delay in being compensated. This means we incur the financing cost for longer than is strictly necessary in order to deliver the USO policy objective, and this unnecessary delay could render the mechanism for delivering the USO policy objective disproportionate.
- 3.4 A streamlined process would also avoid unnecessary delays caused by multiple appeals of various Ofcom determinations. Given these considerations, we recommend the following timeframes to processing claims:
  - Ofcom should come to a final determination within 9 months of receiving a claim, and
  - the USP submitting its claim should receive compensation within 12 months of Ofcom receiving the claim.
- 3.5 We propose a few changes, which would shorten the process, and make it more efficient and less resource intensive for the USP, Ofcom, and the rest of industry. We set out our proposed process in Figure 1 below.

Figure 1 – Suggested end to end process



3.6 The key changes we suggest to Ofcom's proposed process are:

1. The USP should be able to submit its claim and request to establish an industry fund, along with any other information required, in the same initial submission.
2. Ofcom should engage with the USP if Ofcom wishes to change the scope of the review, so the USP can withdraw or alter the submission if they wish to.
3. Ofcom should carry out the consultations and notification of its determinations for all matters of the review at the same time (validating a claim, establishing the existence of net cost, unfair burden, whether an industry fund is required, and who contributes). This would result in a more efficient and less resource intensive process for Ofcom and CPs, and would be in line with the principle of proportionate regulation. For broadband USO, Ofcom should clarify in the final statement its intention to do this.
4. Ofcom should follow the existing process for the administrative levy in setting up the fund, invoicing CPs for payments into and out of the fund. Where additional information may be necessary, Ofcom should use information already available to it, or request specific additional information from individual CPs.

## 4. Requests for review and determining a net cost

- 4.1 The assessment framework should be simple and efficient with Ofcom consulting and deciding on matters of the review together.
- 4.2 The Universal Service Directive (USD) and Communications Act leave the significant detail of the process to Ofcom's discretion. We consider that some aspects of the proposed process are unnecessarily complex and burdensome, as set out below.

### Question 1

"Do you agree with our proposed procedures for commencing a review of a net cost of complying with universal service conditions?"

### The procedures for commencing a review of a net cost claim should be simpler and more timely

- 4.3 We agree that in deciding whether to start a review Ofcom needs to be sure that the USP has provided enough information to be able to calculate and verify a net cost effectively.

- 4.4 When USPs compile a net cost claim it would be useful to know roughly how big a claim needs to be to trigger establishing a fund. It would also be helpful for CPs to have a reasonable understanding as to whether they are likely to be a contributor or not, e.g. if they are already a contributor to Ofcom's administrative charges.
- 4.5 As part of this exercise Ofcom also proposes to consider 'whether the potential size of the net cost is proportionate to the work involved in assessing the application and, potentially, setting up an industry fund' (paragraph 4.5(b)). This provides a further reason why it is important to ensure that a fund is set up in the most efficient way – otherwise, a paradox is created whereby an inefficient (overly costly) fund itself becomes a reason why USPs may not be permitted to recover the costs of providing the USO.
- 4.6 In addition, it would be helpful for USPs to have more detail and certainty on the following areas in order to make an informed decision about when to submit a claim:
- efficiency and reasonableness in the establishment of the fund
  - the expected approximate cost of establishing the fund
  - an estimate of the amount of net cost below which it would be unlikely to meet the criteria for fund set-up, and
  - minimum threshold to identify CPs that may have to pay into a fund.
- 4.7 Without this information, USPs may need to estimate the size of a net cost claim and be incentivised to delay claims until they are sufficiently large. This would not provide timely compensation and would in itself create costs.
- 4.8 Although we regard it as implicit in the terms of the regulations, in line with the regulatory principle of proportionality, we propose the following amendment to regulation 5(2)(d):
- 'the likely *efficiently incurred* costs to OFCOM and others associated with establishing and administering a fund under these Regulations; and;' (see Annex 1)
- 4.9 We agree with the position in paragraph 4.3 that it is a matter of discretion for the USP as to when and how frequently it submits claims in relation to a USO. We anticipate this will be determined by the size of the USO, and in some cases BT may submit more than one claim per year for a USO.

### Question 2

"Do you agree with our proposed procedure for making an application requesting compensation for an unfair burden?"

### The application process for requesting compensation for an unfair burden should be streamlined

- 4.10 We agree with Ofcom's proposed procedure for making an application request for compensation, subject to confirmation that it is sufficiently flexible to allow for USPs to submit the net cost claim together with the request to establish an industry fund.

### Question 3

"Do you agree with our proposed procedures when making determinations when assessing a net cost claim, including our proposed approach to finality?"

### The processes set out by Ofcom will lead to unnecessary delays in reimbursement

- 4.11 As set out in section 3 above, Ofcom's proposed process is unnecessarily long and complex. In our view proportionality requires that it should be streamlined to cover several steps together to

avoid the need for a series of determinations. A single consultation and determination should cover:

- calculating and verifying a net cost
- determining the extent of any unfair burden
- establishing an industry fund, and
- setting out contributors and contributions (where possible).

### Approach to finality

- 4.12 Ofcom proposes that it 'will not reassess the scope of any net cost that is materially covered by an existing determination except in exceptional circumstances' (paragraph 4.23(d)) i.e. if unforeseen and of such scale as to be outside of normal commercial risks.
- 4.13 We support Ofcom's desire to limit the re-assessment of claims to exceptional circumstances, given the already lengthy process, and other routes available for claiming overpayment and appealing Ofcom's determinations.
- 4.14 Nonetheless, the principle of finality should not prevent USPs from including previously rejected costs in subsequent claims, in particular where Ofcom has previously decided that such costs were not sufficiently large to justify assessing the application and/or setting up an industry fund.
- 4.15 In paragraph 6.10 of the Consultation, Ofcom refers to taking into account the 'outcome of any previous determinations of the net costs' in assessing claims. We propose an amendment to regulation 5(2) of the Funding Regulations to make this explicit, either by adding a new sub-paragraph (f), 'any previous Ofcom determinations rejecting the universal service provider's claims'; or by amending sub-paragraph (e) as follows: 'any other matters identified as appropriate by OFCOM having regard to the facts and circumstances pertaining to the case, including any previous Ofcom's determinations rejecting the universal service provider's claims' (see Annex 1).

## 5. Calculating and verifying a net cost

### Question 4

"Do you agree with our proposal on the information the Universal Service Provider should provide alongside an application to review a net cost?"

### **BT can provide the information required alongside the net cost claim, but aspects of the requirements are too broad**

- 5.1 The information Ofcom requires USPs to provide in support of their application to review a net cost is broadly reasonable – where it is focused on the actual costs of providing the USO.
- 5.2 However, paragraph 5.7(g) requires 'any other information identified as appropriate by Ofcom'. We would welcome additional guidance on the types of further information Ofcom could require, and a clarification that the USP can also submit additional information it considers relevant for Ofcom to make an informed decision on the claim (for example, under regulations 3(3) and 5(3)).



**Question 5**

“Do you agree with our proposed approach to calculating, verifying and auditing a net cost?”

**BT agrees there would be no intangible benefits and recommends Ofcom uses information already available to it**

- 5.3 We agree with the proposed approach to calculating, verifying and auditing a net cost (incurred costs less a deduction for earned incremental revenues), but there are some elements of verification and auditing which are impractical and need amending. We have laid these out in further detail under the headings below and in the cost template (Annex 2).
- 5.4 We are also keen that data collection, verification and auditing are proportional to the size of the scheme. We welcome Ofcom's indication that a process could be adopted based on that for BDUK contracts, without every small cost line being explicitly recorded (e.g. fuel and fleet costs) when data is available from other sources which can be used for the calculation.

**Revenues**

- 5.5 The revenues need to be considered at both wholesale and retail levels, and projected ahead over the assessment period. BT accepts that this will need to be a forecast, but our view is that some pragmatic assumptions can be used to provide the required data (set out in more detail in Annex 3).
- 5.6 It is impractical to report revenues by premises for two main reasons. Firstly, the unique premise code (UPRN) which identifies the premises that Openreach has built out to relates to equipment inventory but cannot be linked to an account number identifying the customer paying for the service.
- 5.7 Secondly, we cannot identify all customers in scope of the USO who do not exceed the threshold to obtain service unless they had identified themselves, for example by calling the USO call centre. This means we need to use either proxies or assumptions to calculate revenues. We also need to make assumptions on direct revenue benefits beyond any charge control period.
- 5.8 While Openreach will always benefit from the wholesale revenues generated by its network underlying the broadband USO service, at the retail level there will be competition, and customers will be supplied by a range of retail service providers. Therefore, after the minimum contractual period of 2 years, the net cost calculation will have to make assumptions of BT's retail share of these customers over the period of the NPV calculation. For example, by using BT's average national market share at the retail level. If there was to be a fundamental change in market circumstances or demand we would need to reconsider our assumptions.
- 5.9 It should only be the incremental revenue (between the factual and counterfactual scenarios), net of any associated retail costs, that should be taken into account. We provide more detail on our assumptions for calculating and forecasting future revenues in Annex 3.

**Costs**

- 5.10 It is important that USO costs for the BT Consumer Customer Facing Unit (CFU) are taken into account, including: costs of raising awareness with eligible customers (e.g. mailshots, drafting customer templates), setup costs for the USO Helpdesk (e.g. process design and systems), agents in the USO Helpdesk, and related support function costs. We will include these Consumer setup and operating costs as part an Alternative Schedule in the cost template at the time of submission (Annex 2).
- 5.11 This activity needs to be undertaken for the scheme to achieve its policy objective, and so the provision of a timely, efficient cost recovery mechanism will help to ensure the right incentives are in place to ensure the scheme's success.

### Intangible benefits

- 5.12 Ofcom does not expect intangible benefits (e.g. related to enhanced brand recognition, the benefits of increased ubiquity of the service, and lifecycle benefits) to be significant in the context of the broadband USO specifically, 'given the expected small size of the broadband USO and in light of the fact that BT and KCOM are already designated as Universal Service Providers for the telephony USO' (paragraph 9.24 Consultation).
- 5.13 We agree with Ofcom and expect no intangible benefits of providing broadband USO. The broadband USO will have no positive impact on BT's brand, and the increase in the ubiquity of service (even were this to be shown to be a source of benefit) will be limited as the extra number of customers will be very small in proportion to BT's existing base.
- 5.14 We are concerned that the requirement to provide an estimate in monetary terms of insignificant (if any) intangible benefits would therefore be disproportionate in the context of the broadband USO.
- 5.15 In any event, if we were asked to provide an estimate of intangible benefits, we would want to ensure these were net of any potential disbenefit associated with being the USP. This could be the case, for example, if societal expectations around what the USO should provide (and how quickly) do not match the reality of the USP obligations and the constraints of practical implementation and delivery.
- 5.16 We therefore ask Ofcom to clarify in its final statement that given the unlikelihood of intangible benefits for the broadband USO, USPs will not be required to submit any further evidence and that those will be assumed to be zero. This would be consistent with the proportionality principle.

## 6. Determining the extent of any unfair burden

### Question 6

"Do you agree with the proposed factors we will consider when assessing an unfair burden?"

### More guidance needed on assessing unfair burden

- 6.1 We broadly agree that the factors set out in the Consultation are appropriate for assessing an unfair burden, and in line with principles of transparency, proportionality, no undue discrimination, and least market distortion.
- 6.2 However, we note the following in relation to this assessment:
- additional principles should apply (see below)
  - only efficiently incurred cost (by Ofcom and industry) of setting up and maintaining an industry fund should be considered, and
  - more clarity is needed on how an unfair burden will be assessed.

### Additional principles to apply

- 6.3 In our view the following principles should also apply to processes and procedures for reviewing claims, assessing unfair burden, and establishing an industry fund:
- light touch and not unduly resource intensive
  - flexible and timely
  - efficient, and
  - simple and easy to administer.

- 6.4 These principles will also facilitate the ability to flex the cost of establishing the industry fund dependent on the size of the claim. This cost will reduce as the process progresses, and experience and learnings are applied to avoid replicating efforts.
- 6.5 In paragraph 6.12, Ofcom refers to 'relevant characteristics of the USP' as one of its considerations in assessing unfair burden. We would ask that Ofcom set out the types of characteristics it would consider – beyond the characteristics already described in section 6 of the Consultation. We also seek clarity on Ofcom's understanding of assessing 'quality of its equipment' (3.15).
- 6.6 More generally, we expect Ofcom to consider all relevant circumstances prevailing at the time of its assessment of a claim, including other expected costs and USO obligations, so that its assessment is not unfairly limited.

### **Administrative and cost burden of establishing an industry fund**

- 6.7 In paragraphs 6.7 and 6.13(d), Ofcom proposes to include consideration of the administrative and cost burden of establishing an industry fund in its assessment of unfair burden.
- 6.8 We are concerned about how Ofcom will assess the costs of establishing and administering the industry fund, and how it will balance those with BT's costs. The overall costs of setting up and running the industry fund could be considerable, depending on how complex it is and how efficiently it is set up, and as a result the threshold for proceeding with a claim could be very high. It is important to ensure that the fund is set up in the most efficient way possible, in order that the costs associated with it do not themselves inhibit legitimate cost claims.
- 6.9 Consideration should also be given to possible future changes to USOs in the establishment of any industry fund. Arrangements for an industry fund should have scope to evolve to reflect potential future changes – e.g. in the scale or scope of a USO.
- 6.10 The extent to which the establishment of any industry fund would be unduly costly or administratively burdensome is primarily within Ofcom's control and responsibility, and this depends on the mechanisms and processes involved for reviewing cost and establishing a fund. The objective should be a light touch, efficient, timely process – to ensure the establishment of a fund is not unduly burdensome or costly.
- 6.11 The processes that have been proposed would result in unnecessary increased costs of administering the fund and, thus, in the more likely (unfair) rejection of a USP's claims as disproportionate in relation to such costs (Consultation paragraph 6.13(d)).
- 6.12 In our view, it would provide guidance, and benefit industry and Ofcom, if Ofcom could set a minimum claim threshold above which the potential size of the net cost is likely to be proportionate to the work involved in assessing the application and, potentially, setting up an industry fund (paragraph 4.5).
- 6.13 A threshold would give the USP and CPs some certainty as to whether a claim is likely to fail on the basis of disproportionate administrative and cost burden. It would also help to streamline the process and reduce the administrative burden of preparing claims that will likely fail. Claims below this threshold should be assessed on a case-by-case basis. We would welcome discussions with Ofcom on what an appropriate threshold would be.
- 6.14 In the interests of efficiency and simplicity, we ask that the Funding Regulations require that Ofcom only considers costs related to an industry fund which are efficiently incurred by it or industry. See proposed amendment to draft regulation 5(2)(d) in Annex 1.

### **More certainty required**

- 6.15 It is important that the Funding Regulations are consistent with the proposals in the Consultation. For example, paragraph 6.10 refers to taking into account 'the outcome of any previous determinations of the net costs... i.e. because it was not previously deemed unfair for

the USP to bear those costs' – although this is absent from the corresponding sections of the Funding Regulations. We propose to include this in the regulations (see proposed amendment to draft regulation 5(2) in Annex 1).

- 6.16 In paragraph 6.8(a) of the Consultation Ofcom refers to the degree to which the USP is 'exposed to competition', and in 6.13(a), the 'extent to which the USP is subject to competition in relevant markets'. Ofcom should clarify in its final statement whether these references are specific to broadband services, or more general. The limited competition for broadband services in the premises covered by the broadband USO underpins the USO and the designation of BT as the USP. We therefore consider this consideration to be superfluous in the context of compensation for delivering universal broadband services.
- 6.17 In the circumstances, a consideration of the regulation and designation process set out in 6.13(b) and (c), suggests the net cost of providing the broadband USO would be unfair to BT.
- 6.18 Finally, Ofcom should reiterate in the final statement that Articles 12 and 13 of the USD do not prevent the net cost of the universal service obligation from including the reasonable profit of the USP. Indeed, it is now clearly established that the net cost recovered by the USP can include a reasonable profit.<sup>2</sup>

## 7. Establishing an industry fund

### Question 7

"Do you agree with our proposed approach to determining whether an industry fund should be set up?"

### **The proposed approach to determining whether an industry fund should be set up is unnecessarily complex, and should only consider central funding based on a clear government commitment**

- 7.1 We agree that once Ofcom has established an unfair burden exists, the next step is to determine whether an industry fund should be established to share the burden fairly across the industry. However, Ofcom's proposed process of establishing an industry fund, as set out in the Consultation and Funding Regulations, is overly complex and cumbersome.
- 7.2 Ofcom's proposed draft regulation 9(3) would result in indefinite postponement of compensation where there are potential central funds. In our view any consideration by Ofcom of central funds in the context of establishing an industry fund must be limited to (i) firm commitments by government, and (ii) a short discretionary postponement.
- 7.3 In particular, regulation 9(3) should be amended as follows:
- 'Where it ~~appears~~ is clear to OFCOM that central funds ~~may~~ are to be committed to compensating the whole or part of the financial burden of complying with one or more of the relevant universal service conditions, OFCOM ~~must~~ may postpone the calculation of the amount to be collected until such time as the part of the amount to be compensated from central funds is known, *provided such delay is reasonable in the circumstances.*'*
- 7.4 Our proposed amendments will ensure that:
- Any postponement may only be triggered by a firm government commitment of funds (rather than where it appears such funds may be committed),
  - Ofcom will have discretion (rather than be obliged) to postpone,

<sup>2</sup> ECJ caselaw, cases C-508/14, C-280/00 and C-508/14.

- Any postponement is more limited in time (rather than open-ended 'until such time as the part of the amount to be compensated from central funds is known').
- 7.5 See Annex 1 for suggested changes to draft regulation 9(3) of the Funding Regulations.
- 7.6 Ofcom should confirm in its final statement that there has been no clear commitment for central funds from Government in relation to broadband USO, by the date of publication of the final statement. We note that for the broadband USO the question of public funding is also considered as part of the assessment of whether premises are eligible for the USO under the USO Conditions.
- 7.7 Finally, Ofcom should clarify in the final statement that its proposal in regulation 10(2) to 'open a separate fund to compensate each amount to be collected which is greater than zero' is intended to separate the administering of various claims, and will not incur additional cost or burden.

### Question 8

"Do you agree with our proposed approach to determining which providers will contribute to any industry fund?"

### Ofcom already has relevant information to estimate and indicate which CPs will contribute what proportion under the existing ECN/ECS definition

- 7.8 We agree with the proposal to apply a minimum relevant turnover threshold to rule out smaller players and instead focus on potential contributors. However, Ofcom should provide a preliminary indication on the threshold that will determine contributors from the outset. It can then develop a list of contributors based on this threshold which would provide greater clarity and certainty to affected industry participants.

### Contributors to the industry fund

- 7.9 Ofcom notes the requirement for a wider pool of contributors to avoid a distortion of user demand (7.28). BT supports widening the pool of contributors to spread the burden of net cost. This would be a fairer distribution of the burden and non-distortionary, as the USO will also result in more premises being available for all CPs to serve over the longer term – not just the USP.
- 7.10 In line with Article 13 of the USD, Ofcom proposes that contributors to the funds would be providers of ECN and ECS as defined in section 32 of the Act, or a sub-set of those providers. Ofcom proposes that if the definition in the Act is amended following the transposition of the European Electronic Communications Code (EECC) in the UK (expected in December 2020), it will determine appropriate providers in light of the definitions in force at the time of a request for compensation.
- 7.11 BT agrees with this proposal regarding adopting changes based on the EECC, and notes the recent ECJ case law on the status of VoIP providers.<sup>3</sup>
- 7.12 However, it is important that changes in definitions (or other changes, e.g. in scope) do not result in unnecessary delays in the process. If timing of changes in legislation interferes with the efficient process we suggest that any compensation process or payments should not be delayed – even if there is initially a smaller pool of contributors. Legislative changes that could cause delay should instead be taken into account in the assessment of subsequent claims.

<sup>3</sup> C-142/18 Skype Communications Sarl v IBPT.

**Question 9**

“Do you agree with our proposed approach on calculating contributions from fund contributors?”

**BT proposes that Ofcom uses information already available to it to calculate contributions from fund participants, to reduce burden and complexity, and in line with the proportionality principle**

- 7.13 Ofcom must have regard to the principles of transparency, least market distortion, no undue discrimination and proportionality. The application of these principles may vary depending on the relevant context. However, some general points can be made:
- We agree that similarly situated suppliers should be treated equally by Ofcom.
  - To ensure least market distortion, the pool of contributors should be sufficiently wide to avoid some suppliers having a cost burden which their competitors do not have. A wide pool will also keep down the contributions required of individual suppliers.
  - As Ofcom notes, this will also minimise distortion of consumer demand (7.27 - 7.28) because each provider will have a smaller cost burden to bear.
- 7.14 As a matter of fairness, covering the cost of providing a decent minimum broadband service where it is not commercial for a single operator should be an industry responsibility. It is appropriate and fair that all operators (above the threshold) should play their part, especially as the infrastructure will then be available to whoever wishes to offer communications services to the end customer. CPs should not be able to avoid this responsibility because of an overly complex scheme which they could game.

**Relevant turnover**

- 7.15 Ofcom should use the information it already has to calculate contributions to the industry fund, and to help streamline the process and reduce administrative burden. To do this, we suggest the following approach to determine contributions to the industry fund:
1. Ofcom uses the same approach it already uses for calculating the administrative levy,
  2. Ofcom uses additional information it has, e.g. using retail volumes or revenues (consumer and SMEs) for all relevant ECNs and ECSs, which could be sourced from the Communications Market Report, and/or
  3. Where appropriate, through follow-up requests, Ofcom seeks additional information from relevant parties.
- 7.16 In the Consultation Ofcom proposes to use ‘net relevant turnover’ for calculating contributions, whereas Ofcom uses ‘relevant turnover’ (as included in ‘Turnover Returns’) for calculating administrative levies. We are concerned that using ‘net relevant turnover’ (calculated by subtracting allowable deductions from the relevant turnover figure) is not consistent with the proportionality principle:
- Ofcom already uses the proportion of industry revenue generated by each organisation as the basis for calculating that organisation’s liability to pay Ofcom’s administrative levy. This should be the starting point for calculating that organisation’s contribution to the industry fund. Given that this is familiar to the industry, it would provide welcome clarity on who would be expected to contribute.
  - Adopting two different bases for calculating the administrative levy and a sharing mechanism for the USO would increase the administrative burden on providers, and add complexity and difficulty. For example, issues are likely to arise as suppliers who buy telecommunications services from other CPs for the provision of ECNs and ECSs may not have full records of these purchases to hand.
  - There is additional work and likelihood of errors resulting from multiple submissions on different bases, and this is of concern given the risk of enforcement action being taken against providers submitting incorrect information.

- 7.17 By using information already available to it, and requesting specific information from individual contributors, if and when necessary, our suggested approach would be more proportionate, and would reduce the unnecessary burden and risk on potential contributors.

## 8. Procedures for the collection and distribution of funds

### Question 10

“Do you agree with our proposed approach to collecting contributions to an industry fund?”

#### **USPs incur significant costs in delivering USOs and should be promptly compensated**

- 8.1 For simplicity Ofcom should have a consistent approach between collecting contributions to a USO fund and its own administrative costs. Currently in relation to the administration levy Ofcom receives submissions on turnover nine months after the previous year end and collects fees from debtors on a monthly basis in the financial year following the submission.
- 8.2 We consider payments in instalments into the industry fund to be reasonable so long as USPs are compensated appropriately for any delay in receiving payments. This is not an issue if all net burden costs are repaid within the year, however, this is unlikely given the approach that Ofcom proposes in this Consultation.
- 8.3 We note that Ofcom proposes to set a relevant turnover threshold for contributors to the industry fund, as well as repayment by instalments, so all contributors should be able to pay relevant amounts without causing them cashflow issues.

#### **Bad debt**

- 8.4 Ofcom's proposed timescale for bad debt recovery is too long, and it should not take six months to trigger the bad debt process to recover civil debts. In addition, any process for recovering bad debts should also allow for the recovery of the cost of the debt.
- 8.5 Ofcom's proposal to reallocate bad debt amongst other CPs may lead to further delays. It is important that a framework is in place that encourages CPs to pay in a timely manner and discourages any tactical gaming of the system.

### Question 11

“Do you agree with the proposed process by which we would compensate the Universal Service Provider?”

#### **We have suggested improvements to Ofcom's proposed process for compensating the USP to make it more efficient and light touch**

- 8.6 We agree with Ofcom's proposed payment process for USPs, subject to our comments above on the potential for delays from the approach to recovering bad debts.

### Question 12

“Do you have any comments on the specific provisions of the draft funding regulations?”

#### **The Funding Regulations should align to the Consultation and should be clearer**



- 8.7 We have considered the proposed Funding Regulations and provided suggested amendments in Annex 1.

## 9. Calculation of a net cost for the broadband USO

### Question 13

“Do you agree with our proposed approach to the choice of the counterfactual for the calculation of a net cost of the broadband USO?”

#### BT agrees with the approach to the counterfactual

- 9.1 Yes – the choice of counterfactual is appropriate in terms of the assumption that no alternative providers would have been designated.

### Question 14

“Do you agree with our proposal to use a NPV methodology to calculate a net cost of the broadband USO?”

#### BT agrees to the use of the NPV methodology for calculating net cost

- 9.2 We support Ofcom's proposal to use a NPV methodology as this would avoid the need for multiple calculations over the lifetime of the assets (e.g. up to 40 years in the case of any new duct). For this reason we see it as a simple and more efficient approach to using an alternative model of depreciation and adding a return on assets. This is particularly the case for the broadband USO, which will mainly involve upfront capital costs at the start of the project.
- 9.3 We recognise that an NPV calculation which involves a 20-year forecast (including revenues) presents potential issues. However, we believe these can be addressed by using some pragmatic assumptions such as:
- Service margins (revenues minus opex at the retail/wholesale level as appropriate) and Weighted Average Cost of Capital (WACC), which remain constant.
  - Valuing future benefits based on margin per line, scaled by forecast line volumes.
  - Forecast volumes which recognise that many customers will switch to other suppliers once the minimum contract term expires – by using BT's current market share at the retail level.
  - Recognition of the time between expenditure by the USP and repayment from the fund. The USP would otherwise be disadvantaged because it would need to fund investment for this period (for example, spend in April one year not being compensated until later in the next financial year).

#### NPV cost template

- 9.4 We welcome Ofcom's discretion to agree changes to the NPV cost template. This is because it may become necessary to add tabs or expand on the calculations provided to Ofcom as part of a claim. This is provided for in the Reporting Directions (A6, Part 3, section 3(a)):
- ‘in the form specified in Annex 1 to this Schedule 1 except in so far as Ofcom may consent otherwise in writing; and’
- 9.5 We ask that Ofcom clarify in the final statement that changes can be made to the proposed template (for broadband USO), and other future USO templates, as required, in agreement with BT.
- 9.6 We have included an updated NPV model (Annex 2) showing our suggested changes to the proposed template.



**Question 15**

“Do you agree with our proposed reporting requirements in respect of the broadband USO?”

**The proposed reporting requirements are reasonable**

9.7 We agree that the proposed reporting requirements are reasonable, subject to our comments above.

**Question 16**

“Is there anything else you would like to tell us about the proposals set out in this document?”

**We have nothing further to add**

## 10. Annexes

**Annex 1 – Changes to Draft Funding Regulations**

**Annex 2 – Updated NPV Template**

**Annex 3 – BT Revenue Assumptions**

Comments should be addressed to:  
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