BT response to the BDUK Urban Broadband Fund Consultation on Connection Vouchers

Response from BT

24 July 2013

General points on the objectives of the proposed voucher scheme and its effectiveness in delivering superfast networks in cities

The Government has been clear on its overall objectives for superfast broadband:

"*To achieve the 'Best Superfast Broadband network In Europe by 2015'*,"

and also in the BDUK rural broadband scheme and the recent NAO report of delivering:

"*Superfast to 90% of BDUK areas by May 2015.*"

However, there is not a well-defined objective identified for the Connection Voucher scheme that we are aware of. It is unclear whether the priority for the scheme is to support broader UK economic growth, drive the growth of SMEs and jobs or to extend coverage of the last x%, related to cities. The closest the consultation document comes to setting any objectives appears to be that the scheme is:

"*…**intended** to stimulate the market to **improve** digital connectivity…..**helping** cities to create and attract new jobs…..*"

Without clear objectives it is impossible to define the criteria for the scheme's success and hence whether it will represent value for money.

BT believes that there are very real benefits to the economies of cities through the provision of ubiquitous high-speed broadband services, as in rural areas. However, BT does not consider a voucher scheme aimed at demand-side intervention to be the most appropriate mechanism to deliver these benefits. It will not resolve the issue of next-generation access (NGA) white areas (locations eligible for public subsidy under state aid guidelines) in cities in order to deliver ubiquitous high-speed connectivity and strong customer take-up resulting in economic benefits. These are discussed in a report on city broadband commissioned by BT, which can be found at: http://www.btplc.com/Thegroup/BTUKandWorldwide/BTRegions/England/Factsandfigures/CitiesReportreUltrafastBB-June2013.pdf

The above view is informed by the fact that NGA white areas in cities exist for many of the same reasons as they exist in rural areas, eg, the business case for a wholesale network provider is unclear, very high risk and there is a long pay-back period due to low forecast take-up, high capital cost to build infrastructure, etc. Therefore, we believe that the resolution of this problem in cities will require intervention to the supply side to lower the risk of delivering new network capacity as has been the case in rural areas.

BT therefore believes that the scheme under consultation is unlikely to have a meaningful impact in assisting the Government to achieve its objectives of delivering NGA across the country and its commitment to build the best superfast broadband network in Europe. The best way to deliver these objectives in cities is through effective supply side intervention supported by suitable state-aid clearance at EU level.

However, given that the Government's decision is to proceed instead with the proposed demand-side voucher scheme, BT has focused this response to help ensure that if this scheme becomes the

remedy to address city whitespaces, it can be made as effective as possible despite its obvious challenges.

Specific responses to consultation questions

Question 1: What methods do you consider most useful and practical in the context of stimulating awareness and demand for a broadband connection scheme?

SME end users in cities are typically not aware of the range of potential solutions to their connectivity needs or to the further options that may be possible if their demand was to be aggregated across a range of similar users. Delivery of high-speed connectivity to a building shared by multiple SME users is more cost-effective than a series of individual links. Effective aggregation of demand would enable potentially more effective, higher cost options to become cost-effective or enable the supply side risk of delivery to be suitably offset.

For such a scheme to be effective it is essential that SMEs are made aware of the solutions available. Groups of SMEs that could be served by a common or shared solution should also be identified and encouraged to work together through landlords, managing agents or local business leaders/advisers. The value they place on connectivity (eg, using monthly rental rate as a proxy for value) should also be established.

BDUK/city authorities then need to ensure that there is an effective two-way exchange of information between the SME/user side and the supplier side in any city. This information should be made available to suppliers in that area in a non-discriminatory manner to allow them to assess if they are able to deliver suitable solutions. It is therefore this market-demand information that is important to suppliers delivering solutions to local/bespoke market opportunities; this information needs to be the focus of awareness and demand-side of this scheme.

Question 2: If you are an SME, ISP or network operator: (a) would you be keen to participate in the voucher scheme on the basis that we have set out in this consultation? (b) In addition to the elements described in this consultation document, what further steps, if any, would BDUK need to take to ensure your participation in the scheme (e.g. broadening the categories of eligible end-users)?

BT is willing to participate in a voucher-based scheme given that this currently represents the only intervention in city NGA but we would highlight that the effectiveness of such a scheme to address NGA white areas in cities will be extremely limited.

A key additional feature that we would wish to see in the scheme is the recognition that SMEs' landlords/business park agents, etc. should also be eligible to participate on behalf of their co-located SMEs as long as they meet the SME criteria.

We propose that a separate 'landlord voucher' should also be available that delivers effectively N x 30Mbit/s (or some other high speed level eg, 1Gbit) to N SMEs within a multi-tenant building or business-park location, but that such a landlord voucher should also have a higher maximum value of N x £3000 as well. Such a change would encourage landlords of business units to take part in the scheme and incentivise them to resolve issues such as access to tenanted buildings, internal cabling etc, which are major handicaps to delivery of these services to individual SMEs in such buildings.

Question 3: Does BDUK need to place any conditions or criteria on the vouchers to ensure effective take-up by end-users?

We suggest that keeping the voucher scheme as simple as possible is a key element of ensuring participation. This simplicity principle applies equally to end users/SMEs to use and to ISPs/suppliers to deliver. For example, any deviation from standard products/systems in order to comply with voucher term is likely to decrease participation and take-up. However, it would be beneficial to impose a condition that vouchers must be used within a reasonable time to ensure they are allocated to recipients with a clear intent to utilise them, subject to normal lead time issues associated with any product likely to require such a voucher (see our related point on timescales under Question 11).

Question 4: Which costs do you consider should be eligible for funding by the connection voucher?

The consultation document makes it very clear that this fund is targeted at paying for SMEs' 'initial broadband-connection costs' and that this will need to be 'where there is evidence that demand exists and that connection charges are a genuine barrier to take-up'. Given these objectives, BT sees that that the scheme should therefore apply to three main eligible costs as follows:

- costs of connecting a business to an existing business connectivity network in the area, including the one-off/bespoke excess construction charges for the relevant SME (or SME landlord in accordance with our proposals under Question 2)
- costs of providing the one-off connection and excess construction charges for an FTTP service to the relevant SME (or SME landlord in accordance with our proposals under Question 2)
- costs of enabling the connection of an FTTC-based solution for a group of SMEs/SME landlords connected to an un-served cabinet. In this case the connection charge would be the cost of connecting/enabling that cabinet to provide high-speed services to the relevant group of SMEs on the cabinet. Typically this would be in the region of £20-40K per cabinet and so would be suited to an aggregated demand scenario of a group of SMEs in a particular business area such as a business park. This would deliver high-speed benefits to all users on the cabinet once aggregated demand of circa 8 -15 SME users was assured (or perhaps one or two SME landlords).

Question 5: Do you think the current value range proposed for the connection vouchers (£250 to £3,000) is appropriate?

Whilst BT agrees that the average connection cost could be covered by voucher values in this range, we believe that for some SMEs, with difficult access issues, a value of up to £5,000 per individual would be more appropriate. In addition, and as described in our answer to Question 2, we believe that the scheme should also comprise a 'landlord voucher' that can deliver benefits to multiple SMEs. This voucher should have a maximum value significantly higher than £3000, subject to it delivering benefits to multiple SME users, ie, its value is effectively up to N x £3000 where N is the number of benefitting SMEs.

Question 6: Should a contribution to the connectivity costs be required of end-users or should the scheme support the total costs of connectivity? If you consider a contribution to be appropriate please explain why and confirm which end-user should be required to contribute (e.g. SMEs, residents etc.), and what the minimum contribution should be.

A connection grant of 100% of the value is inappropriate and would fail to recognise that there is value to the SME in securing high speed connectivity. Ideally therefore we believe that the connection grant should be capped at a lower level. The contribution, in addition to the grant amount, would then be made by the end user/SME or the landlord/agent as appropriate to reflect their commitment to the additional value delivered by the enhanced connectivity. In this case we would suggest a contribution from the end user of circa 20% of the connection fee but capped at £500. However, given that voucher scheme is intended to be as simple and attractive as possible for end users during the market test we would not propose including this additional complexity at this stage.

Question 7: Do you agree that a 'portal' (web based interface) providing is the best mechanism to enable end-users to meet potential suppliers? If so, what information do you consider should be provided on the 'portal'?

A portal or similar web-based interface is one of a range of mechanisms that should be deployed to ensure that end users are aware of suppliers' products and capabilities but it should not be the only mechanism or the take-up of the scheme is likely to be sub-optimal. The availability of vouchers and the capabilities of the scheme and product offerings available need to be actively communicated to SMEs/end users via a range of business engagement routes, including local federations and trusted advisers such as banks, accountants and local authority business support teams, amongst others.

We would also propose that 'white label' marketing and promotions schemes run at a local city level and targeted at local SME groups and business leaders and advisers should also be a key part of the scheme to ensure that the availability of the fund and its benefits to the target groups are effectively communicated and understood.

Question 8: Other than the use of a portal, what steps could be taken by BDUK to maximise the effectiveness and efficiency of the scheme for suppliers and end-users?

The availability of vouchers and the capabilities of the scheme and product offerings that are available as a result need to be actively communicated to SMEs/end users via a range of business engagement routes including local federations, trusted advisers such as banks, accountants and local authority business support teams, amongst others.

We would also propose that 'white label' marketing and promotions schemes run at a local city level and targeted at local SME groups and business leaders and advisers should also be a key part of the scheme to ensure that the availability of the fund and its benefits to the target groups are effectively communicated and understood.

Question 9: The measures that BDUK is proposing are designed to stimulate the take-up of high-grade connectivity demanded by SMEs. These measures and the voucher scheme in particular have been formulated to work with the current regulatory framework and State aid rules. Please confirm:

(a) whether and how you consider these measures might result in a distortion to competition and what, if any, adjustments to the scheme might serve to correct for such distortions; and

(b) whether the operation of the proposed scheme is likely to give rise to any regulatory concerns.

The key regulation and state-aid issue associated with this scheme is the liability or otherwise of the vouchers to promote network 'overbuild' and/or funded intervention in access markets that are not subject to identified market failure. In particular, in many/all of these city areas there are multiple existing providers of business connectivity circuits that are capable of delivering high-speed connectivity to SMEs or any user who chooses to buy them.

The reasons the SMEs do not utilise these services are varied but fall largely into three areas as follows:

- lack of knowledge of the range of product options available beyond basic broadband.
- high initial/connection costs.
- high on-going cost.

The proposed voucher scheme as we understand it will seek to address the first of these by promoting awareness of solutions amongst SMEs, landlords and business park managing agents, amongst others, and ensure that demand is effectively communicated to potential suppliers (see our answer to question 1) . It will also seek to address the second of these directly by contributing to the connection cost financially. However, it will not address the third issue at all.

The voucher scheme could lead therefore lead to a distortion of competition (case (a) above) if the voucher was used to pay for the construction of network assets alongside/adjacent to existing network assets already provided by a commercial provider in the area to deliver the same service e.g. new duct/fibre in the street where an existing provider was already present.

The scheme may also give rise to regulatory concerns (case (b) above) if the service delivered resulted in a reduced ability for the end user to take advantage of competition in the market, eg, by restricting access to the range of service providers experienced by other users. (See also our response under question 11 on open vs. closed access).

Question 10: What methods do you consider might be most useful and practical to monitor the Voucher Scheme and evaluate its outcomes?

It is difficult for BT to comment on this without greater clarity on the objectives of the scheme and the expected outcomes (see our general comments at the start of this response.) However, given that this scheme is seeking to distribute some £90M of public money (nearly 20% of the total amount allocated by central Government to date for delivering the best superfast broadband network in Europe) coupled with the very real and proper focus on value for money from any Government spend, we would expect the scheme to have clear target deliverables and outcomes, each of which would need to have clear values of benefits and number of beneficiaries associated with them and costs of delivering those benefits. This would enable a clear assessment of the benefits of the scheme to be made and demonstrated to the taxpayer. As an illustration however London has some 3.3 million premises and we understand is expected to receive approximately

£20M of the £90M total, more than a fifth of the total pot. However, an average voucher value of £2000 per SME this would be sufficient to resolve 10,000 premises or 0.3% of the total.

Question 11: Are there any other aspects that directly relate to BDUK's proposed demand-side measures that you would like to raise?

BT has a number of comments about the proposed demand-side measures and the design of the voucher scheme that we would wish to see addressed if it is to work effectively and not to involve significant unnecessary cost, complexity or delay to potential suppliers or end users in gaining the benefits of high speed connectivity. In particular we would make the following points:

Need for multiple quotes:

The current proposed process requires an end user to obtain "at least two" quotes from suppliers in order to apply for a voucher; this process risks ignoring the impact of quotes on underlying wholesale providers. For example, in order to provide a quote a retail provider may need to obtain quotes from a wholesale provider, for example, for Excess Construction Charges (ECC) for Ethernet connectivity. If the two retail quotes rely on the same wholesale provider, or if retail providers proactively target end users and initiate quotes to inform those discussions to secure business then this could lead to a significant rise in the need for wholesale level quotes. Many of these quotes will involve the assessment of network connection/ECCs and associated surveys. Most wholesale providers will have designed systems and pricing structures for products on the basis of an assumed level of quote/survey activity. The voucher scheme, particularly with its insistence on two quotes could significantly impact this and the costs of surveys, including the potential for multiple surveys of the same site. Whilst there are actions that can be taken by suppliers to try and identify multiple requests for the same site and thus try to avoid repetitive work on surveys, we believe that the insistence on two quotes per voucher request is unnecessary and unduly burdensome.

Timescales of the Market Test and product delivery

We note that the planned market test stage of this process is expected to be of the order of two calendar months. However, many/most of the product options that could be deployed to meet any resultant demand for vouchers issued through this scheme are liable to have relatively long lead times. For example an Ethernet connection is typically delivered in 60-90 days, similarly an FTTP end user connection is circa 60 days, and a cabinet enablement to connect a group of business users could be of the order of six to nine months to deliver. The only products that are likely to be capable of delivery within the timescales of the market test are existing standard broadband products from existing suppliers, by definition in NGA Black (one which has two competing fixed line infrastructures) or Grey (where there is only a single physical infrastructure but it supports a wholesale marketplace) areas and the connection costs of these products is typically well below the £250 threshold for the voucher.

It therefore appears to BT that within the current planned timescales of the market test it will only be possible to test if a quote for a product can be obtained and a request made and assessed to allocate a voucher. The ability to claim against a voucher, process it through supplier and SME systems and actually deliver a connection is highly unlikely to be tested within these timescales. BDUK therefore needs to seriously consider if this is sufficient information to adequately test this

approach before committing significant Government funds to such a scheme and whether further time is required to enable actual delivery of connections via a voucher scheme.

The very short timescales of the market-test stage also mean that any new/innovative approach to solutions will be unlikely to be available and thus the market test will need to rely on standard market offers.

Open vs. closed access schemes.

The UK market for high-speed connectivity is characterised by high levels of competition at the retail level with a large number of competing service providers underpinned by equivalent access products offered at the wholesale level. As a result an end user can typically take a service from one retailer and, at the end of their contract, easily change to another service provider without needing to change the underlying infrastructure or arrange complex and expensive 'handover' from one circuit provider to another. This is a feature of 'active' layer access products at a wholesale level.

The voucher-based scheme, targeted as it is at retail level ISPs and the likely use of bespoke business connectivity circuits, could well lead to a situation where the benefits of such open-access systems are lost as retail providers will seek to deliver their own vertically integrated closed-access systems using the voucher to provide a dedicated access link into the SME building. Therefore, when the contract ends and the SME wishes to change provider they may be faced with a completely new access cost to provide another dedicated link to their building, effectively presenting the service provider with a local monopoly that was, at least in part, funded by the Government voucher. BT does not consider this to be an effective or value for money outcome and therefore the design of the scheme should seek to avoid, wherever possible, the provision of a closed-access solution to end users.

Two stage payment proposal to the supplier

The consultation proposes that the payment of the voucher will be made on behalf of the end user from DCMS direct to the supplier and that this payment will be made excluding VAT. This approach leads to a number of potential complexities in the billing process for suppliers. In effect, the supplier will issue an invoice to the end user (including VAT for non VAT registered SMEs) once the service is delivered, and then accept a payment from DCMS for the voucher amount less VAT and a separate amount for the balance from the end user (plus any VAT due on the voucher element not paid by DCMS). Such an approach requires a non-standard payment mechanism to be instigated by suppliers wishing to accept vouchers and thus compromises the principle of simplicity highlighted in our response to question 3 and that BT and others suppliers have consistently highlighted through the market-engagement phase of this project.

This two-stage payment process could seriously impact the ability of suppliers to take part in the scheme and would definitely increase the cost to the supplier to take part resulting in wasted money and decreased benefits from the scheme. We would therefore propose that DCMS instead makes the payment direct to the SME following settlement of the supplier invoice.

We would be happy to discuss these issues further. Further enquiries can be directed to
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