Implementing a Landline Duty

HM Treasury, HMRC, BIS

Consultation Document

Response from BT – 12 February 2010

Implementing a Landline duty: consultation on draft legislation and impacts - BT response

General

1. BT believes that investment in Superfast broadband is vital to the future of a Digital Britain, enabling UK businesses to successfully compete globally using the latest technology and consumers to access an exciting new range of high-speed applications in the home. In particular, widespread NGA availability will provide a major spur to UK creative industries and protect and create jobs. Hence, we see investment in NGA infrastructure as potentially forming a major plank of the UK economic recovery plan and why we have committed to investing £1.5bn in rolling out NGA to 10 million homes. If the policy objective of the UK Government is to see fibre investment go further and faster than is commercially viable then BT believes that some kind of Government stimulus would be helpful. No country in the world has managed to get widespread fibre investment without Government action of some sort.

2. BT therefore supports the policy principle behind the proposed Landline Duty of raising additional investment in this important area but recognises also that there could be other ways to fund the gap between commercial viability and policy objectives – for example, using the money raised by spectrum auctions.

3. BT understands that it is not intended that costs to industry of collecting the duty will be reimbursed from duty funds. Therefore, as the purpose of raising the duty is to increase the level of resources available to industry for investment in NGA, it would be counter-productive to adopt a complex process for collection of the proposed duty requiring significant changes to systems and associated investment costs. BT, therefore, welcomes the generally straightforward process envisaged by the consultation proposals. A more complex process, for example to include other business services such as leased lines, would add considerably to the burden of implementing this duty at network owner level and potentially seriously impact the timescales for implementing the changes. Businesses will already be contributing significantly to the duty under the existing proposals as drafted, through their use of PSTN and ISDN 2 and 30 lines supporting voice, broadband and ancillary services on private networks. Further detail on this particular aspect of the impact of the duty is included at Annex 1.

4. BT, therefore, welcomes the opportunity to comment on this important legislation and the opportunity to minimise operational impact and costs and thus ensure maximum "flow through" to the fund.

Consultation Questions

<u>Question 1</u> : The first tax return will cover the period from 1 October 2010 to 31 March 2011. Does this cause line owners any problems?

5. The introduction of the proposed Landline Duty will require changes to the systems and processes of network operators (and potentially wholesale and retail Communications Providers who consume the network operator's products). We understand that the resultant change and ongoing costs of the duty collection systems will also need to be covered by the operators themselves. As such it is important that the system changes are kept as simple and straightforward as possible commensurate with that required to collect the duty.

6. BT understands that the specific legislation to introduce the Landline Duty will be contained within the finance bill due to be presented to Parliament in March. The proposed lead time for the first tax return period of approximately six months is considered sensible and should not lead to significant problems. Our assumption is that the duty is to be applied at the Openreach network level on PSTN lines in accordance with the definition at clause 1 (5) of the proposed schedule in Annex B. Systems exist within BT that can be enabled to perform this tracking at Openreach level and subsequently the pass through to Openreach's customers, with some system modification. If the scope of the duty were to be extended beyond that foreseen in the consultation, for example to include access tails of VPN networks or leased lines for corporate networks, the system implementation consequences would become significantly more onerous. This would involve higher cost and longer lead time to implement.

7. Other factors that would impact the ability of BT to implement these changes within the proposed timescales include changes to the proposed application of VAT from that in the consultation i.e. the current plan to include VAT in addition to the duty itself allows existing VAT based billing systems to be utilised at retail level if required. Changes to this approach could cause additional complexity.

<u>Question 2:</u> Are there any reasons why line owners will not be able to deliver a return and payment to HMRC on or before 30 April 2011?

8. Similar to our answer to question 1 regarding the scope of the duty and the simplicity of the tracking approach, collection of this duty over the initial period from 1st October 2010 to 30th April 2011 should be possible. However, if the scope of the duty were to be extended beyond that foreseen in the consultation, for example to include access tails of VPN networks or leased lines for corporate networks etc., the system implementation issues would become significantly more onerous. This would imply significantly higher cost and consequently longer lead time to implement, potentially jeopardising the timescales envisaged in this consultation.

<u>Question 3:</u> Are there any problems caused for line owners if the accounting period for the duty is annual? Would owners find it helpful to have any other accounting schemes available?

9. In keeping with the general principle of ensuring the duty collection mechanism is simple and straightforward to implement, run and maintain, BT sees a number of benefits in having an annual accounting period for the duty. The need to produce

reports only on an annual basis with a simple return at the end of the period minimises the impact of both the initial set up of the process and its ongoing maintenance and collection. Given that the implementation and ongoing costs are expected to be borne by the network owners and that such increased costs have the potential to impact all downstream users at both retail and wholesale level, BT believes it is in everyone's interest to make such systems as simple and efficient as possible.

10. Openreach bills its wholesale customers typically on a quarterly or monthly basis according to their contract and as such we understand that some respondents may be concerned about the potential for Openreach to benefit from the "mismatch" between collection and payment terms inherent in the proposals in the consultation, i.e. that Openreach would effectively collect the duty on its lines throughout the billing period but only submit the duty funds to the Government at the end of the relevant period. However Openreach, and other network owners, will need to modify systems and processes to collect this duty and incur the associated costs in advance of any collection and it is our understanding of these proposals that these costs will need to be absorbed by the Network Owner, as well as associated bad debt risks, and are not refunded from the duty amounts. As such BT considers the proposed annual accounting period to be the best compromise position in terms of ensuring that the system is kept as simple and low cost as possible to the Network Owner commensurate with the system operating as intended. Any shorter accounting period would lead to additional complexity and cost.

Other issues for BT

11. BT notes that the definition of "Physical circuit" in Clause 1 (6) of the proposed schedule refers to "copper" circuits. We would highlight that although the majority of the Openreach access network utilises copper lines, there are also instances where other metallic cables are utilised e.g. aluminium. It would, therefore, be more accurate to utilise the term "metallic" rather than "copper" in the definition for these circuits.

Annex 1

NGA Duty collection on Business lines - Issues and impact

Summary

1. Businesses will already be making a significant contribution to the NGA duty under current proposals, because of their existing lines used for PSTN and ISDN2 and 30 services, including broadband access to the internet.

2. Extending the duty to other business services such as leased lines and access to Virtual Private Networks (VPNs) would require detailed drafting amendments to what the Government is currently proposing, and introduce a number of complexities around collection, as set out below.

3. The system costs of tracking these additional lines to BT would be significant, expected to be at least £1m, and would be significantly more than the additional revenue raised in the first year.

The issue

4. The original DBR report specifically focussed the NGA duty on traditional telephone lines and excluded corporate networks. We suspect this was primarily because of the difficulties in identifying and collecting such a duty from these networks.

5. Simply extending the duty to all private circuits and other corporate network circuit ends presents a number of problems as follows:-

6. A typical corporate data network , whether provided by BT Retail, BT Global Services or any other communications provider who procures wholesale services from BT, is made up of a range of different product access inputs that might include some or all of:-

   - Ethernet circuits provided by Openreach
   - Analogue private circuits provided by BT Wholesale
   - Partial private circuits provided by BT Wholesale
   - Private optical fibre network components from a non SMP network provider
   - Ordinary PSTN and ISDN lines for, voice, broadband access, back up, fax, ISDN lines monitoring of fibre circuits etc. provided by Openreach

7. All of these components are combined together to provide a network solution to the end user, and typically a solution price is levied, not a per circuit price. There is, therefore, no direct correlation between the circuit components BT Wholesale or Openreach provide to their customers and the "customer end circuits" sold by those Communications Providers to their end customers and in particular the network components from the non SMP provider would typically not be based on any end user circuit but part of an aggregated network solution e.g. component optical fibre. The typical network though would include a large number of normal PSTN type circuits (often significantly more, in pure number of local ends terms, than fibre pipes and these would attract the duty under the PSTN definition) through their use as monitoring lines for fibre pipes, ISDN lines, emergency lines etc. A typical corporate network would therefore incur a bill based on the PSTN definition for the duty without the additional complexity of including leased lines in the definition.

Issues associated with including leased lines

8. The market structure for leased lines and other data services used for corporate networks presents a number of issues if it is necessary to track the number of corporate network local ends:-

   - BT Openreach and BT Wholesale have no means currently of knowing if the circuit components they sell are ultimately used to deliver a retail customer end or part of a wider network solution.

   - Network providers other than BT typically do not sell individual circuit components nor do they publish prices for such products. Therefore, any per circuit charge at the BT Wholesale level is likely to impose a competitive disadvantage to BT, as there is no effective equivalent product from other operators, and no means of ensuring it is applied in a competitively neutral manner. Note also that BT Retail and BT Global Services do not "self provide" their network components and thus would be disproportionately disadvantaged if such a duty was not applied equivalently across all network providers.

   - To implement such a system would require a major exchange of information about the use of wholesale circuits from the retailer/end network solution provider back to BT Wholesale or Openreach before a system to distinguish between end user circuits and network components could even be constructed. It is impossible to cost this solution without a commitment to exchange this information but a typical system change to wholesale or retail billing system to enable this would cost in the region of £1million.

   - Since most network providers sell network solutions not circuits it is unlikely that they will have any means currently of tracking any equivalent product internally and thus no means of raising an equivalent charge.

9. As stated above, a typical private network will consist of a mixture of fibre private circuit tails, and PSTN type lines. The lines will be used for various ancillary services such as emergency back up lines (no need for emergency battery power as exchange powered), as well as ISDN lines and fax lines, etc. In addition, large fibre pipes will typically have a PSTN type line associated with them for monitoring purposes in the event of circuit failure, etc. As a result a duty charged on PSTN lines only, and therefore based on Openreach SMPF and MPF lines as envisaged by the original duty definition, would result in charges to large corporate networks for these various copper lines that are part of their mix of circuits. Typically these PSTN type lines would be significantly more numerous, in terms of simple volume of lines, than the small number of high capacity fibre tails in the network. Therefore, adding leased lines to an NGA duty definition may increase the number of lines in a corporate network that attract a bill for the duty slightly (probably by less than 10%) but it will incur significant additional complexity and cost to implement and will not add significantly to the existing level of duty that corporate networks will pay through their current and ongoing use of the various ancillary services essential to a corporate network that PSTN type lines provide.

10. Because of the lack of systems for tracking business local ends it is not possible to give accurate numbers for the scale of the additional duty from including leased line access tails but the market review figures that Ofcom have produced based on submissions from each operator provide an indication. These are based on estimates of customer "circuit ends" from each of the market participants and information submitted to Ofcom as part of the review process. They are estimates

primarily because private networks are not built or sold as discrete circuits, as discussed above. These figures would imply a value of such a business duty of approximately £80,000 per month or about 0.5% of the proposed PSTN type line duty. The bill to business from the duty on their associated copper lines for the ancillary services is expected to be substantially more than this figure i.e. businesses are expected to incur the duty without this change. Additional changes to a wholesale or retail level billing system to track these access tails would incur costs in addition to any costs associated with the current proposed Openreach copper line duty.

11. BT understands that it is not intended that costs to industry of collecting the duty will be reimbursed from duty funds. However as the purpose of raising the duty is to increase the level of resources available to industry for investment in NGA, it would clearly be counter-productive to adopt a complex amendment, as would be necessary to include business/leased lines, when businesses will already be contributing significantly to the duty under the existing proposals as drafted.