



Melanie Dawes
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Dear Melanie

Thank you for your time over the last couple of weeks – both our meeting and our subsequent telephone calls have been extremely constructive and helpful. I also really appreciate all your efforts to plot a path forward for the regulation of the UK fixed telecoms market at this very important time, including your comments at the FTTH Council Europe conference last week. With the final outcome of your WFTMR firmly in sight, I am preparing to go back to BT's shareholders and Board to provide the reassurance needed to underpin BT's commitment to pass 20 million premises with FTTP by the mid to late 2020s, including 3.2 million premises in the harder to reach Area 3 (the 'FTTP scale case').

When the BT Board agreed to announce our FTTP scale case earlier this year, it did so explicitly on the basis of specific expectations about the regulatory regime. These 'enablers' included: indexation of legacy copper prices, a reasonable premium for the fibre anchor price, fibre pricing flexibility above the anchor, support for stopping selling copper where a reasonable fibre build out level has been achieved, price regulation that enables the recovery of (efficiently incurred) cost and – crucially – a 'fair bet' on returns.

I appreciate the progress that has been made on most of these enablers, especially knowing the opposition Ofcom has faced from some stakeholders. However, the fact is that we still do not have what we need from Ofcom on cost recovery and the fair bet, topics that you and I have discussed a number of times. BT remains the only company that has set out plans to invest at real scale and pace and over the long term. Regrettably, the evidence both from BT's share price and direct feedback from investors is that these plans are unattractive to the market. This is driven largely by the current lack of clarity from Ofcom on cost recovery and returns, reflecting the fact that BT, unlike other telecoms network providers, faces asymmetric regulatory risk, a dynamic which is fully understood by our investors. For these reasons, I am inviting you to consider whether Ofcom can go further to help provide the reassurance our investors need.

We discussed the steps that Ofcom can take to address this, in particular by giving BT, its Board and its shareholders the basis on which to evaluate upfront the prospective returns on the investment of at least £12bn that we will be committing to build a nationwide FTTP network. I appreciate your willingness to go as far as you can in providing the detail we need and ask that you contemplate the following questions:

1. Can you address the remaining ambiguity about how long a **period of regulatory forbearance** Ofcom will provide? Setting out your expectation of no further regulation of fibre prices until *at least* 2031 in your speech was helpful. However, it still exposes BT to the risk of further fibre price regulation within the payback period on our investment. We are, therefore, seeking a statement that Ofcom would expect no further regulation of fibre prices before at least 2036, i.e. three control periods. This would send a signal that Ofcom does not expect to intervene before the payback period on the investment, which would be reassuring to investors.
2. Can you be definitive on the **'triggers' that Ofcom will use to assess whether to impose regulatory price caps on FTTP and how any such cap would work?** As you know, we seek clarity from Ofcom that it will not set price caps in a way that limit our internal rate of return (IRR) on the FTTP scale case at below 15%.
 - This could be expressed simply as a cap on our IRR. If Ofcom instead prefers to use a more traditional RAB-based price cap, we can reconcile this back to our FTTP scale case as required to explain to our investors that it still represents a good return on their investment. In order to do so, we need clarity *now* on how Ofcom would operationalise such a price cap.
 - In either approach we need to know the WACC (and how this will track back to our project-specific WACC), the costs that Ofcom would take into account (and how they relate to the Regulatory Financial Statement), and how Ofcom would approach depreciation.
 - At the decision point on whether to cap fibre prices, this would mean looking backwards at returns made, and also looking at forecast returns over the remainder of the lifetime of the investment. To reiterate, we are *not* asking Ofcom to guarantee BT a return of 15%. We simply want to be allowed upfront to shoot for 15%, leaving sufficient upside in play that we could expect our risk adjusted return to be at least equal to our [X].
3. Can you be more specific about how Ofcom will approach and manage any **distinction between Area 2 and Area 3?** It is reassuring to know that Ofcom expects Area 3 to be regulated in the same way as Area 2 until at least 2031 in terms of outcome (although for different reasons – based on the scope for competitive build and the ongoing public procurement process). However, we remain concerned that the distinction between Area 2 and Area 3 relied upon by Ofcom for potentially different underlying regulatory approaches beyond 2031 is not supported by the evidence. As we understand it, Ofcom's current approach could result in different wholesale prices in different parts of the country (which will flow through to retail prices), which we consider will be politically unacceptable. This is why we have consistently advocated that Ofcom should regulate in the same way across the UK, which would have the added benefit of giving competition the best chance of emerging wherever possible.

4. Can you set out explicitly how Ofcom will approach **regulation of legacy copper prices** beyond 2031 (including indexation of legacy copper prices, support for switch-over and copper stop sell, and service levels in respect of legacy copper which will drive ongoing cost)? Setting a clear expectation – as in your speech – that your new regulatory framework, including regulation of legacy copper prices, will endure for the next decade is helpful. Our investment case covers more than 20 years, however, so clarity about the period beyond 2031 matters. This will allow us to calculate the viability of the FTTP scale case investment on a ‘brownfield’ basis (i.e. taking into account the impact on our legacy copper business), which better reflects the impact on BT’s business overall.

I believed we had clarity on much of this – including, crucially, Ofcom’s approach to returns and the fair bet – when I secured support from the BT Board to announce our FTTP scale case in May 2020. This was not wishful thinking on my part; my belief was informed by Sharon White’s letter to me of 1 May 2019, which reassured me that Ofcom would be content with BT earning returns of up to 15% on our FTTP investment. This was reinforced by Jonathan Oxley’s letter to me of 25 February 2020, in which, after Sharon’s departure, he reiterated Ofcom’s support for her letter. He also stated clearly that Ofcom would adopt the same regulatory approach in Area 3 as in Area 2 if we were to make an acceptable commitment to invest in these harder to reach locations. This was explicitly the basis on which we committed BT shareholders’ cash, at risk, to passing 3.2 million premises in Area 3, as Clive Selley set out in his letter to you of 26 June 2020.

If you are able to make clearer and more detailed statements on the items I have set out above, we will be able to work together to secure the confidence of BT’s shareholders and Board in the FTTP scale case, and with it the investment that the UK needs for the digital transformation of our economy and society. As we have discussed, in the event that investors lose confidence in BT there may be wider consequences for our position as a UK national champion, and on our willingness and ability to lean in on issues of national importance.

Our latest discussions, your recent speech and your engagement with investors have all been much appreciated and I do not doubt your personal commitment to getting the right outcome for the UK. I therefore remain hopeful that we can work through and address the points I have listed in this letter. As always, my team stands ready to work with yours to take this forward.

Yours sincerely



PHILIP JANSEN