Contents

Section 1

Summary

1.1 Universal Service ensures that basic fixed line services are available at an affordable price to all citizen-customers across the UK.

1.2 The scope of the Universal Service Obligations (USO) is defined by the EC Universal Services Directive ('USD'). The Secretary of State for Trade and Industry specifies the services which must be provided throughout the UK in the Universal Service Order (the Order). The Order has been implemented by Ofcom through specific conditions on BT and Kingston Communications (in the Hull area) and general conditions on all providers. USO services include the following: special tariff schemes for low income customers; a connection to the fixed network, which includes functional internet access; reasonable geographic access to public call boxes; and a range of services for customers with disabilities including the text relay service.

USO Review and Ofcom's Strategic Review of Telecommunications

1.3 Ofcom is reviewing BT and Kingston's USO to ensure it continues to meet the needs of consumers. The review is focussed on delivering the current Universal Service arrangements and is being carried out alongside Ofcom's Strategic Review of Telecommunications ('the Strategic Review') which looks at longer term Universal Service issues. The Strategic Review's conclusions on USO are set out in this document. The Strategic Review, published in November 2004, emphasised the importance of USO as the 'safety net' for vulnerable consumers but noted that the mechanisms for funding and provision of universal service may need to change if and when the provision of USO becomes an undue burden. At that point, it would be necessary to design new funding and provision mechanisms, for example a Universal Service fund. In future, it may also be appropriate to alter the overall scope of USO. Though we do not believe at this point that there is a case for extending universal services to include broadband, the Strategic Review considers how the scope of USO might evolve over time.

Affordability

1.4 As Universal Service Providers (USPs), BT and Kingston have to ensure that customers can afford to obtain and retain telephone service. This is achieved through special tariff schemes that target customers on low incomes. BT's existing schemes use a proxy of low use in order to attract low income customers. Ofcom's research suggests that this works reasonably well: around 60 per cent of users are claiming a state benefit to assist with their income. BT has proposed an alternative scheme targeted at households with annual household income below £10,400. Ofcom is inviting views on both the existing and the proposed new schemes.

1.5 Ofcom considers that disconnections policy is another indicator of affordability. BT disconnects around 5 per cent of residential customers (1 million) a year for non-payment of bills. Ofcom research suggests that BT could promote its schemes more effectively and that this would assist customers who might otherwise be disconnected.

Public Call Boxes

1.6 Public Call Boxes (PCBs) provide a service that is valued and needed by many people without a phone or those away from home, who cannot, for whatever reason, use their mobile. Many disadvantaged and vulnerable consumers still rely on PCBs.

1.7 BT and Kingston are each required to ensure adequate coverage of PCBs. Ofcom considers that adequate coverage is best determined at a local level through consultation with local public bodies. The last PCB cannot be removed from a site if those bodies object – 'the local veto'. As revenues from PCBs have fallen in recent years, BT argues that the local veto is unduly restrictive. Ofcom proposes that the local veto should remain but with new measures to make the process more transparent, accountable and consistent. Ofcom is proposing to issue guidance on requests for PCB removal, to improve the consultation process and to establish an appeal process.

1.8 Ofcom is also inviting views on the definition of a 'site'; this determines which PCBs are subject to the local veto. Ofcom is also reviewing which public bodies represent the most appropriate level of local government to have the local veto.

Services for customers with disabilities

1.9 Universal Service measures provide access to, and affordability of, a range of essential services for customers with disabilities. A key service is the text relay, which is highly valued by customers. However, it needs to evolve as demand and technology changes. To improve transparency and accountability, views are sought on the establishment of a Stakeholder Advisory Panel for the relay service plus the publication of an annual plan and report on the operation of the service. A study into a video relay service is also proposed.

Provision of a connection capable of functional internet access

1.10 BT and Kingston are required to provide a connection upon reasonable request and at uniform prices, irrespective of geographical location. This requirement is particularly valuable to customers in remote rural areas whom the market might otherwise not serve. Where installation of a new line costs £3400 or less, BT sets a standard charge. Where installation will cost over £3400, BT requires the customer to pay the excess costs (plus its standard connection charge). Ofcom consider the use of a 'threshold' to be a sensible approach; Ofcom is seeking further data to help it decide the level of that threshold. In addition, Ofcom intends to publish guidance on the issues to be taken into account in considering whether a request is reasonable.

1.11 The obligation on BT and Kingston to provide a connection upon reasonable request encompasses the provision of a narrowband connection capable of 'functional internet access' (FIA). Guidelines on FIA were issued in 2003 which said that users should be able to expect connection speeds of at least 28.8 kbit/s. It also set out measures that universal service providers should take in response to complaints about data speeds. The Guidelines have been beneficial and no significant changes are proposed at this time. In particular, it is considered that the benchmark minimum speed should remain at 28.8 kbit/s for the time being.

Costs and benefits of providing USO

1.12 USO is currently funded by BT and Kingston as the obligations have not previously been considered to represent an unfair burden on them. Ofcom has considered how the costs and benefits to BT of providing USO might have changed in recent years. Ofcom's indicative estimates suggest that since 2001 the costs of serving uneconomic customers have fallen significantly while the costs of providing uneconomic payphones have risen sharply by a similar amount. Benefits from providing universal services arise primarily from brand image and advertising on public call boxes. Ofcom's indicative estimates of the benefits suggest they have remained broadly stable. Ofcom's indicative estimate of the current costs of USO for BT suggests they are around £50-70m and the benefits are around £60m. Ofcom believes therefore that there is unlikely to be an undue financial burden on BT as a result of USO that would justify conducting a full cost benefit analysis and setting in place new USO funding arrangements. The Strategic Review is considering the medium to long term issues around universal service funding.

Section 2

Introduction

Universal Service – what it is and why it is important

2.1 In the modern world we all rely upon a variety of telephony services. Most people have access to both a fixed line and a mobile telephone. Many of us use email, text (SMS) and instant messaging. More than half of households have internet access and an increasing number have broadband. These services keep us in constant touch with our friends and family. With the continued fall in prices, telephony services have become ever more affordable. These positive developments have not been shared by everyone; Universal Service aims to make the benefits available to all sectors of our society. USO provides a safety net that ensures basic fixed line services are available at an affordable price to all citizen-customers across the UK.

2.2 There are both social equity and economic grounds for USO. It provides services to help vulnerable customers and customers in remote and rural areas, whom the market might not otherwise choose to serve, allowing them to take their full part in the economy and society. In addition, all citizens benefit by having a larger telephone network; they can contact and be contacted by more people. Cheap communication also enhances economic growth. The balance between these rationales has changed over time. In 1984 when the proportion of customers with fixed telephones was around 77 per cent, the focus was on increasing the size of the network. Today, when 99 per cent of people have access to fixed telephony services, USO is more focused on bringing benefits to those with low incomes who have difficulty affording telephony service, customers with disabilities who need particular services or facilities and customers in rural areas for whom the actual cost of service might otherwise be prohibitively expensive.

2.3 The provision of USO is of course not cost free. If services are to be made available to those who might not otherwise be able to afford them (or consumers who live in rural areas the market might not serve), this requires a subsidy from other users of the telephone network. While there are social and economic arguments in favour of these cross subsidies, it is also essential that they are targeted effectively. If, for example, there are to be special schemes at lower prices, this involves cross subsides and should be focussed on low income consumers. To achieve this objective without means testing is not easy. While Ofcom endeavours at all times to operate in accordance with the regulatory principle of a bias against intervention, in this area there may be a need for slightly more detailed regulation in order to ensure the effective targeting of limited resources.

The legal framework

2.4 The scope of the USO is defined by the USD. Under the Communications Act 2003 (“the Act”) it is the duty of the Secretary of State for Trade and Industry to make an order setting out the general requirements which must be provided as Universal Services in the UK. It is Ofcom’s responsibility to carry out the Order and ensure these services are provided. Ofcom imposes certain conditions on all providers, such as requirements in relation to disconnection. In addition, using objective, transparent and non discriminatory criteria, Ofcom has designated BT and Kingston to provide the following specific further services, all of which have to be offered at uniform prices across the UK:

- A connection to the public telephone network at a fixed location, following a reasonable request, which includes functional internet access;
- At least one schemes for consumers with special social needs who have difficulty affording telephone services;
- public call box services; and
- A range of services for customers with disabilities.

2.5 BT and Kingston are also obliged to make sure that charges for USO services do not entail payment for unnecessary additional services, to provide free itemised billing and to ensure that USO services meet defined quality thresholds. In addition, BT has to provide a relay service for textphone users and keep an up-to-date database and provide directories as well as the contents of the database to other providers.

2.6 The Order was laid in 2003. Ofcom is now reviewing USO to ensure that it meets the needs of customers as demand and technology changes and in accordance with its legal duties under the Communications Act. Ofcom's principle duty is to further the interests of citizen-consumers. In performing this duty it is also to have specific regard to the elderly, the disabled, those on low income and the different interests of persons living in rural and urban areas; the needs of these people are very relevant to the USO.

USO and the Strategic Review of Telecommunications

2.7 This review is about the current scope of USO as permitted by the framework of the USD. It focuses on the shorter term issues of what more can and should be done now. Alongside this USO review, Ofcom is carrying out the Strategic Review, phase two of which was published recently. The Strategic Review looks at the medium to longer term and broader policy issues around universal service, such as extending USO to broadband, the use of mobile to fulfil USO requirements and the provision and funding of USO in an effectively competitive market. The output of the Strategic Review will help inform the medium term development of USO, in particular Ofcom's input to the 2005/6 European review of USO. The Strategic Review's conclusions are summarised in the next chapter.

2.8 This review recognises and takes account of these broader developments in the market. Although mobile services are not part of USO (nor could they be as the Directive and therefore the Order relate only to fixed services) Ofcom recognises that mobiles meet the needs of some low income customers for access to telephony services.

International context

2.9 Universal Service is, as explained above, an EU wide objective. All the Member States have obligations that ensure access to affordable fixed line telephony services. Universal Service is however not simply a European phenomenon. Many countries, including Australia and the USA, have similar requirements. This review has examined the practical interpretation given to USO across Europe and in Australia and the USA. Each chapter has a section that describes the international context to each of the elements of USO.

A two stage consultation

2.10 This consultation is the first of two stages. This document explains how each of the core elements of USO is delivered, provides evidence, including research, as to their effectiveness and then sets out a series of options for the future, with Regulatory Impact Assessments being provided, where appropriate, in Annex K. Questions are set out both in the relevant sections and policy annexes and are listed together in Annex C.

2.11 At this time, Ofcom is not consulting formally on any changes to USO; it is seeking views on the policy options outlined in this document. If any changes to USO are required as a result of this consultation, these will be subject to a formal consultation that will be included in the Statement with Ofcom's conclusions.

Section 3

Universal Service and the Strategic Review of Telecommunications

Universal Service – an evolving concept

3.1 Universal Service is not a fixed concept. The services that were deemed fundamental to social inclusion in 2004 are not the same as those that were deemed essential in 1984 when BT was privatised. The world has moved on a great deal since then and so has technology. Twenty years ago no one had mobile telephones and there was no world wide web. Today functional Internet access is a Universal Service requirement and although USO cannot yet be delivered via mobile telephony, it certainly impacts upon the availability of affordable telephony services.

Universal Service today

3.2 USO has adapted as society and technology has changed. Universal Service is not however, at the forefront of these changes; it follows, and comes into play when the lack of an affordable service represents a serious obstacle to full participation in society.

3.3 This review focuses on the here and now. What should happen to the payphone at the end of your street? Is the Light User Scheme still the best means of delivering an affordable basic telephony service? Are changes needed to the text relay service? Is the provision of a fixed line connection in remote/rural areas that are costly to serve a significant issue that needs more attention? There are important, higher level and strategic issues associated with USO: the impact of mobile telephony and broadband; the operation of USO in a competitive market? These issues are addressed in the context of the Strategic Review.

USO and the Strategic Review

3.4 The extent of USO has been defined and prescribed until at least 2005/6 by the EU and by the Government (via the USD). This review seeks to ensure that the measures taken to implement that obligation deliver the best possible outcome for the UK's most disadvantaged and vulnerable consumers within the framework of the USD. The focus is the short to medium term. Ofcom recognises that this focus needs to be supplemented and complemented by a more detailed and strategic examination of what should happen to USO in the medium to longer term. These questions could have been included within this review. However, they are connected to even wider policy issues such as future market developments and Ofcom's overall strategy. As such, it was considered that the best place to examine them was in the Strategic Review. The options set out in the Strategic Review are summarised below and the questions posed by that review are repeated. The conclusions on the longer term issues will be set out in the stage 3 Strategic Review Statement and in a targeted work programme following that Statement.

Provision and funding of universal service arrangements

3.5 Increasing competition in telecoms raises issues about the funding of USO. Historically, BT and Kingston have funded any net cost from profits they make on higher margin services, as discussed in Section 9. As competitors enter the market, these more profitable services are targeted. For example, international calls used to be very profitable, and competition developed rapidly in this market. As competition erodes high margins, at some point providing USO may become an 'undue burden'. When this occurs, it will be necessary to consider alternative mechanisms for funding and allocating USO. Such a fund could be implemented in several means:

- A direct levy on all consumers of certain communications services (for example, a fixed amount that appears directly on the bill);
- An indirect levy on consumers via a levy on communications providers (such a model is used in the USA and France); and
- Direct Government funding.

3.6 Ofcom has not considered the exact details of such a fund but direct government support via taxation is likely to be one of the most difficult to implement. A levy that appears on their telephone bill could create arbitrage at the margins of what is defined as a communications service. Once a fund has been established, it might be appropriate to consider whether other carriers could deliver universal services, at least in some areas. One possibility would be to auction off the right to deliver USO, on the basis of the level of subsidy required. This auction could be of the whole or just parts of the USO for example the provision of special schemes or PCBs.

Q1 What should be the arrangements for funding USO in future?

Q2 How could competition for the delivery of USO be organised in future?

Scope of universal service arrangements

3.7 USO can be justified on the basis that it promotes economic efficiency through increased access to the network or on equity grounds in that it ensures that desirable social policy goals are met. The current USO and the demands for the extension of USO to new areas such as broadband can be analysed in this way. Overall we believe the current range of Universal Service can be justified on these criteria. As explained above, the ability to change USO is constrained in the short term. The Secretary of State, not Ofcom, decides its scope. The USD requires that extension of the scope of USO will only be permissible if its extension does not disproportionately increase the financial burden on service providers. Nonetheless, it may be appropriate for the Government and European Commission to consider a number of reasons why the scope of USO might need to change as the Commission begins its review of current USO in 2006. These are:

- **use of mobile**. Mobile may be able to meet many of the requirements of USO, and it may be a much cheaper technology to deliver services to some remote locations which are within mobile coverage. It may be appropriate to make USO service-specific rather than technology-specific (it currently specifies a fixed connection). This does not mean that a separate mobile universal service obligation should be imposed alongside the obligation to provide a fixed service, but that a universal service obligation defined in terms of access to voice services could be delivered via a mobile connection; and

- **broadband obligations**. Ofcom believes that the case for extending the universal service obligation to broadband is not currently strong either on the basis of economic efficiency, or on the basis of equity. It is simply too early in the development of the market for the necessary conditions to be met. We note that the combination of BT's further roll-out of DSL, and its adoption of extended reach DSL, means that BT and market dynamics will make DSL available to 99.4 per cent of the population by mid 2005. The very limited remaining shortfall may best be addressed through public sector infrastructure schemes.

Q3 Should mobile technologies be used to help address the existing USO?

Section 4

Special tariff schemes and disconnections

Summary

- One of the key strands of USO is the requirement on BT and Kingston to ensure that all customers can afford to obtain and retain telephone service.
- To achieve this goal, BT and Kingston provide special tariff schemes that target customers with low incomes. BT currently offers the Light User Scheme (LUS) and In Contact; Kingston offers Basic Call and Basic Contact.
- BT's existing schemes are not means tested and use a proxy of low use in order to attract low income customers. Ofcom research suggests that this works well but not perfectly: around 60 per cent of current LUS and IC members are from low-income households. 20 per cent of users have an annual household income above £17,500.
- A more targeted scheme would have benefits. BT has proposed an alternative to LUS and IC focussed on households with annual household income below £10,400.
- Ofcom is inviting views on both the existing and the proposed new scheme.
- In order to ensure that customers stay connected, disconnections policy is an interlinked and vital aspect of USO.
- The number of residential customers that BT disconnects has remained constant at around 5 per cent - 1 million – a year for several years.
- Ofcom research suggests that BT is not promoting its schemes and services effectively to customers experiencing debt management problems. Ofcom believes that the levels of disconnections could be reduced and more customers would remain connected if BT's debt management and disconnection process were made more effective.

Schemes: Background

4.1 The ability to obtain a telephone service and to retain that service is an integral aspect of Universal Service. One way this is achieved is through special tariff schemes aimed at customers who are on low incomes or have special social needs that would not be provided under normal commercial conditions.

4.2 The ability for USPs to provide special tariff schemes is implemented through a Universal Service Condition on BT and Kingston, requiring them to make available one or more schemes the effect of which is to assist consumers who have difficulty affording telephone services. Each scheme must comply with any direction which Ofcom may from time to time make which may specify, amongst other things: the requirements to be met by a scheme; the criteria to be applied by BT or Kingston in deciding which of its consumers are entitled to the benefits of a scheme; and/or the date of the introduction of a scheme. To-date no direction in relation to special schemes has been issued by Ofcom. Ofcom is now seeking views on the current scheme and a scheme proposed by BT which it would provide to comply with its USO.

International Context

4.3 The provision of special tariffs for vulnerable customers varies across Europe. The UK approach is fairly pro-active in comparison with other Member States many of which have no measures. Some countries apply reductions to the line rental for low income customers, for example in France where customers in receipt of certain benefits are eligible for a reduced rental.

4.4 Australia and the US have special schemes that are more generous than the UK. In Australia, Telstra offers a range of discounted tariffs for pensioners and benefits recipients. Telstra's Pensioner Concession Scheme provides a monthly rebate on calls and reduced connection charges. Provision in the United States varies between states but most offer reductions to between 10-20 per cent of households (a higher proportion than the UK). For example, in Texas customers receive a discount of up to $12 off their monthly telephone bill if they participate in state programs such as Medicaid and Public Housing Assistance and if their income is at or below 125 per cent of Federal poverty guidelines.

Current schemes

4.5 BT provides two special tariff schemes: the *Light User Scheme* and *In Contact.*

Light User Scheme (LUS)

4.6 LUS was launched in 1993 and currently has around 1.1m customers. Use of the scheme has fallen from around 2.5m in 1999; the introduction of IA/CPS barring explains in part the fall in customers using LUS. Normal line rental charge and installation costs apply but users receive a rental rebate if call charges are less than £15.07 per quarter. The tariff is complex: where the quarterly call bill is at or below £10.90, the rebate is 11.56 pence for every 10 pence that call charges fall below £16.75. Where the quarterly call bill is above £10.90, but at or below £15.07, the rebate is be £6.77. Where the quarterly call bill is above £15.07, there will be no rebate for that quarter. If call charges exceed joining threshold on three consecutive bills, the customer is removed from the scheme.

4.7 LUS was created to ensure that customers on low incomes and other disadvantaged customers (who might be without service in the absence of such a scheme) could be connected to the network at an affordable price. LUS involves a discounted line rental and it is important that this discount is directed as effectively as possible. For instance, LUS is not intended to enable customers who make calls using other providers' networks to obtain a subsidised line rental. BT customers who use Indirect Access (IA) or Carrier Pre-Selection (CPS) and who make regular use of mobiles are therefore not eligible for membership of LUS.

BT's In Contact (IC) scheme

4.8 *In Contact* is a low cost service that combines post- and pre-pay. The connection charge and line rental are billed for and are post-paid; calls are pre-paid using cards purchased at selected outlets. Customers use an access code and a PIN to make calls which are charged at a flat rate of 10p per minute. Without the use of the pre-pay facility, customers can receive incoming calls and make outgoing calls to freephone, operator and emergency services. The joining fee is £9.99 and the quarterly rental is £9.25. The scheme was launched in April 1999. It currently has around 63 000 customers; around 100 000 customers have used the scheme since its launch in April 1999. About 50 per cent of those leaving the scheme have moved on to the full BT service.

Kingston

4.9 Kingston has 2 schemes, *Basic Contact*, an incoming calls only scheme (with the exception of emergency calls and fault repairs) and *Basic Call* which allows for outgoing calls by purchasing a prepaid card. The schemes are used as an alternative to disconnection and for customers who cannot afford a security deposit. Take up of both schemes has been small (112 and 3 respectively).

Scheme: Research findings

4.10 Ofcom carried out research amongst current users of LUS and IC during 2004. This research examined the profile of scheme users and their views of the schemes. Details of the research are set out in Annex D. The research reveals some differences between the user profiles of LUS and IC. LUS customers are predominantly older (6 in 10 are aged 65+) and half rely a state pension. IC customers are on average much younger (with just 8 per cent aged over 65+), more likely to have children and be in low income households. Half are non-working, unemployed or retired and hence many are in social group E.

4.11 The vast majority (94 per cent IC and 96 per cent LUS) of scheme users were satisfied with the scheme overall – even among former scheme users, satisfaction stood at 95 and 85 per cent for LUS and IC respectively. Reasons given by former scheme users for no longer using the scheme were mainly due to a desire to make more calls. The research showed that many users of LUS make few phone calls. This is supported by data supplied by BT which shows the majority of users of LUS make less than £6 of calls a quarter. In addition, the research showed that providing a control on costs was another important factor. For IC users, being able to control costs and affordability issues were the main reasons for becoming scheme users.

4.12 Although the schemes are for low income customers, between a quarter and a third of customers appear to have annual household incomes over £11,500 and around a fifth have an income over £17,500.

Affordability

4.13 To provide an indication of the affordability of LUS for low income customers, the table below sets out the proportion of income, after housing costs, customers in lowest three income deciles would have to spend if they were on LUS and made no calls; on LUS and had the average call profile; on BT's Option 1 package and had the average call profile for BT customers.

Figure 4.1

Usage level	No use	Low use	Average Use
		Average LUS User	(Median bottom 80 per cent by spend)
BT tariff	LUS	LUS	Option 1
% average 1st decile	1.1%	2.8%	4.7%
% average 2nd decile	0.7%	1.7%	2.9%
% average 3rd decile	0.5%	1.4%	2.3%

Source: Family Resources Survey, BT

4.14 These figures are lower than those for water (5.3 per cent for the average 1st decile of household income) and electricity (4.9 per cent) and suggest the schemes succeed in their aim of making telephony services affordable, at least for low users. (Source: Food and Expenditure Survey). The proportion of income that the average user of LUS pays for this service is equivalent to that for a colour TV licence Ofcom believes both can be considered household necessities and that this is a reasonable tariff level for such a scheme.

Pre-consultation issues

4.15 Discussions with stakeholders prior to the issue of this consultation document have highlighted concerns about the existing schemes:

- the complex nature of LUS' tariff structure was felt to be a deterrent to making calls or even to uptake of the service;
- the exclusion of mobile users was considered to be disproportionate by some consumer stakeholders given the high penetration rate of mobiles;
- the availability of the scheme to higher income users was raised as a concern in particular given the objective is to help those on low income customers.

4.16 In order to see whether it would be possible to establish a scheme that dealt with these concerns, Ofcom invited BT to develop proposals for a new scheme. Issues that Ofcom asked BT to consider included: tariff levels, eligibility, how eligibility is assessed and marketing. The main features of the Scheme are eligibility linked to low household income and receipt of benefits, an inclusive call allowance of £1, easy to understand prices at 10p per minute and extra savings for use of Direct Debit. BT's proposals are set out below:

Figure 4.2

BT proposals for new special tariff scheme

Tariff

Connection: Standard £74.99 connection charges for customers taking new service with BT. For customers wishing to pay in instalments this charge could be spread across 5 payments.
Line rental: £14.50 a quarter, reduced to £11.50 if the customer pays by direct debit or has a Monthly Payment Plan. Customers would receive a £1 per quarter Inclusive Call Allowance.
Call charges: 10p per minute for UK geographic national and local calls. All other calls charged at standard BT Together Option 1 rates.

Bill payment options including monthly direct debit or monthly payment plan (MPP) which allows telephony costs to be spread payments over 12 months would be available. For customers requiring additional budgetary control, it would also be possible to pre-pay for calls.

BT proposals for new special tariff scheme

Eligibility

This scheme is focussed on customers with low income. As a result, customers would only be eligible for the scheme if they fall within the Government's standard definition of poverty (60 per cent median income). This would mean that eligible base would comprise customer who have an annual household income of less than £10,400 and who are in receipt of a significant means tested state benefit, such as pension credit, would be eligible for the scheme.

In line with arrangements for the existing BT social telephony products (Light User Scheme and In Contact Plus) the following exclusions would apply :

- customers who use Indirect Access (IA) and Carrier PreSelection (CPS)
- customers with more than one line whether at a single or multiple locations;
- customers with lines used exclusively for burglar alarms (not 'lifeline' alarms).
- customers with payphone, ASDL, ISDN or business lines and
- mobile phone users.

Assessing eligibility

Customers would be asked to self-declare that they are eligible. To ensure that the scheme remained targeted at the agreed target audience, BT proposes use of a status-checking agency to identify any applicant customers with a high-income profile. BT will seek further clarification from applicants suspected of false declaration.

Communicating about the scheme to eligible customers

Low-income customers are difficult to identify. BT argues that government agencies, the voluntary sector and other consumer groups are essential in any communication strategy for these audiences. In addition, BT will advise BT customers currently benefiting from a social telephony product about the new scheme and invite them to transfer, if eligible. BT will also communicate with its wider customer base about the social telephony scheme using channels such as individual customer billing, and other literature such as its consumer Code of Practice.

Assessing BT proposals – Ofcom's response

Tariffs

4.17 The table below compares BT's proposed tariffs with the existing schemes. Annex E shows a comparison between BT's Option 1 tariff, LUS and the new scheme.

Figure 4.3

	Connection inc VAT	Line Rental per quarter inc VAT		Calls inc VAT
			With Direct Debit/ Monthly Payment Plan discount	National and local
BT proposal	£74.99	£14.50	£11.50	10 pence per minute (ppm) + a £1 per quarter calls allowance
LUS	£74.99	£34.50. Discount to line rental for call bills below £15.07. Rental of £11.75 if no calls are made.	Not available	Basic call rates (see Annex E)
IC	£9.99	£9.25 (under review)	n/a	10ppm
BT Option 1	£74.99	£34.50	£31.50	Varies

4.18 The simpler tariff structure of the proposed scheme, compared with LUS, is advantageous and might encourage customers to more calls and increase take up. However, the scheme's reliance on direct debit (DD) monthly payment plan (MPP) to provide significant benefits is of concern. The diagram in Annex E shows that customers using LUS who transfer to the proposed scheme and who did not pay by DD or MPP would, without exception, be worse off. BT cites research that 85 per cent of low income households have bank accounts but consumer stakeholders argue that there is reluctance amongst such customers to use DD as it can hinder the ability to budget.

Eligibility

4.19 Ofcom recognises the need for the scheme to be targeted appropriately. The proposed criteria for eligibility that customers should fall within the Government's standard definition of poverty (60 per cent median income) **and** receive a significant means tested benefit seem sensible as this allows the scheme to be appropriately targeted. Around 2.4M households fall within the definition of poverty but not all will receive mean-tested benefits. The continued exclusion of customers who use IA/CPS also seems reasonable because the scheme involves a balance between rental and call charges and is not intended to provide a subsidised line rental to customers who make calls using other providers' networks.

4.20 Ofcom does not consider that the exclusion of mobile users is appropriate. Exclusion from LUS was acceptable in the early stages of mobile use because it served as a proxy for higher income. However, the eligibility criteria should ensure that the scheme is focused on low income households. Ofcom considers that access to a pre-pay mobile should not mean a low income consumer cannot have access to an affordable fixed line service: calls to and from mobiles are more expensive than calls to fixed phones and there are issues over coverage and reliability. In addition, as set out in the Strategic Review (Annex K paragraph K.26), the requirement for functional access to the internet cannot be provided by the current (second) generation of mobile phones. As such, mobile availability is not a substitute for a fixed line.

Assessing eligibility

4.21 Ofcom welcomes the proposed reliance on self-declaration rather than means testing. BT's concern that self-declaration may expose it to abuse is understandable. The use of a status checking exercise to identify applicants with higher income profiles would seem to be a relatively low level of intervention.

Marketing

4.22 Ofcom notes that BT's marketing plan places heavy reliance on promotion by government agencies and consumer groups. To-date such an approach has not always been successful.

Q4 Ofcom is seeking views on all aspects of BT's proposals:

- *the tariff structure and levels*
- *the use of direct debit and monthly payment plan discounts*
- *the target market of households within the governments' definition of poverty and in receipt of means tested benefits*
- *the relevant means tested benefits*
- *the proposed exclusion of IA/CPS and mobile users*

- *the use of self-declaration and of a credit checking agency to minimise BT's exposure to risk of abuse; and*
- *the marketing approach.*

Options for consultation

4.23 Ofcom has identified three options set out below. For all options, USO Condition 2 would remain unchanged. Ofcom would however expect to make a direction under this condition (specifying amongst other things the requirements to be met by a scheme) which would be the subject of a further formal consultation under S.49 The Act .

Option 1: No change to the BT schemes

4.24 Under this option, LUS and In Contact would remain in their current form.

Option 2: BT's proposed new scheme would replace LUS and IC

4.25 BT proposals would be accepted as proposed and replace the current schemes. Customers on the current schemes would be migrated to the new scheme, if eligible and if they so choose, or to another commercial service.

Option 3: BT's proposed new scheme would replace LUS and IC but modifications to the scheme would be required

4.26 The BT scheme would be modified following consideration of the responses. Customer migration would take place as set out under Option 2.

Ofcom's view

4.27 At this stage, Ofcom is seeking views on the options. Whilst Ofcom sees benefits in moving from the current schemes, including better targeting and increased tariff transparency, it is not clear that BT's proposed scheme offers the optimal replacement. In particular, Ofcom has serious concerns about the proposed reliance on DD to provide significant benefits to customers and the proposed continued exclusion of mobile users. In respect of Kingston's schemes, Ofcom will consider the outcome of the consultation on BT's proposals and review their applicability for Kingston.

Q.5 Ofcom is seeking views on the three options proposed: (i) No change to the BT schemes (ii) BT's proposed new scheme to replace LUS and IC (iii) BT's proposed new scheme to replace LUS and IC but modifications to the scheme would be required.

Disconnections

Background

4.28 Universal Service is not just about enabling people to become connected, it is also important that all consumers, but particularly low income consumers, stay connected. One aspect of USO is to ensure that companies have appropriate processes to cover non-payment of bills. This aspect of the USD has been implemented via General condition 13. This states that when providers take steps relating to disconnection they should be: proportionate and not unduly discriminatory; give due warning beforehand of service interruption or disconnection; and except in cases of fraud, persistent late payment or non-payment, confine any service interruption to the service concerned, as far as technically feasible. Providers have agreed a voluntary code of practice which explains how they will deal with customers who may be liable to disconnection.

BT Disconnections

4.29 For some time there has been concern about high levels of disconnection for debt. BT disconnections for bill payment reasons have been running at around 1 million residential customers per year for several years. This level of disconnections represents just over 5 per cent of BT's residential customer base. Telewest, ntl, and Kingston have residential disconnection rates slightly below 5 per cent. BT's disconnections rate is much higher than in the utilities sector where there are around 15,000 disconnections per year for gas and electricity.

Research

4.30 Ofcom carried out research during 2004 examining the level of disconnections. The detailed results are set out in Annex D and the key findings are summarised below.

4.31 Customers who were disconnected were more likely than average to be in D/E social groups, had lower incomes and tended to be younger than average. The average bill prior to disconnection was £110. 92 per cent of disconnected households had a mobile phone (higher than the UK average). The research suggests that of those disconnected in the last year approximately 45,000 do not currently have any telephone service at home. These 45,000 are almost entirely social grade E, and from low income (under £9.5k pa) households. Almost 1 in 3 (28 per cent) of those disconnected had previously been disconnected (and some of these on more than one occasion).

4.32 As part of its disconnections code of practice BT is obliged to make various contacts with customers who are vulnerable to disconnection before it takes place. Almost half (46 per cent) of disconnected customers felt that they were not given adequate opportunities by BT and a similar proportion (44 per cent) felt that BT was unfair in their handling of the disconnection. A significant proportion of those who were disconnected claimed that this caused them a lot (37 per cent) or a few (36 per cent) difficulties. Groups that were most likely to have experienced a lot of difficulties after disconnection were higher spenders, those without a mobile in the house, older consumers (aged 45+) and the unemployed. Difficulties caused by disconnections included lack of social contact, not being able to make emergency calls, work related problems, exacerbating some sort of personal crisis, and loss of a phone that was needed for health reasons.

4.33 Prior to disconnection only a quarter (24 per cent) used a scheme to help control or reduce costs. Two-thirds said that they had not been offered any scheme to help them manage their bill payments. Amongst those that had not taken up any of these schemes prior to disconnection over half (54 per cent) said that some sort of pre-pay scheme would have helped them to avoid disconnection.

Ofcom's analysis

4.34 There is a need for providers to be able to disconnect customers who do not pay their bills. However, it is of concern that BT has higher levels of disconnections than other non-USO providers even though it is the Universal Service provider and has to provide special tariff schemes for vulnerable consumers.

4.35 BT already offers a range of services that should help address the needs of customers with affordability and debt management problems, for instance:

- **Call Levels** Customers agree a quarterly call level which represents the maximum value of calls they would expect to make in a quarter. If the call level is reached, BT will contact the customer to agree a course of action.
- **Monthly Payment Plans** Allows customers to pay a monthly set payment by direct debit based on their average bill amount.
- **BT Payment Card** aimed at customers without a bank account, it allows customers to make payments to BT at Post Offices and PayPoints
- **Pay & Call** BT's commercial pre-pay scheme (more details in Annex E).
- **USO Special Tariff Schemes** The Light User Scheme and In Contact.

4.36 Ofcom believes that if these services were promoted actively to customers in contact with BT's debt management centre, the levels of disconnections could be significantly reduced, particularly customers currently being repeatedly disconnected. Ofcom's research suggests this is not happening. Moreover, mystery shopping by Ofcom suggests that two thirds of callers to BT's 150 customer service, when claiming affordability problems, were not informed about BT's USO or other pre-pay schemes.

4.37 One approach would be for all customers prior to disconnection to be offered a prepay scheme as an alternative to disconnection. Ofcom considers that it is disappointing that BT's Pay & Call service, introduced to address the needs of customers with debt and affordability problems and which had a target of hundreds of thousands of customers, has been taken up by relatively few customers.

4.38 Consumer stakeholders have suggested that BT could use the proposed new social tariff scheme, discussed above, as a credit management tool by making it available for short periods, beyond the eligible group, for instance to customers who are repaying debt to BT. A low rental product with pre-pay functionality might be useful in helping customers manage their bills while they pay off the outstanding debt.

Q6 Ofcom invites comments on Ofcom's view that BT should promote its portfolio of debt management and affordability services more effectively to customers experiencing payment difficulties.

Section 5

Public Call Boxes

Summary

- Public Call Boxes (PCBs) provide a service that is valued and needed by many people without a land line or a mobile or those away from home, who cannot, for whatever reason, use their mobile.
- USO PCBs are particularly valued in rural areas, some of which suffer from lack of mobile coverage and in communities, rural and urban, where there are disadvantaged and vulnerable consumers who still rely heavily on PCBs.
- BT and Kingston are each required to ensure the adequate provision of PCBs and Call Box Services (CBS) to meet the reasonable needs of users in terms of geographical coverage, number and quality and in accordance with any direction that has been made.
- Ofcom's view is that the question of what constitutes adequate coverage is best determined at a local level. For this reason, under the current Direction, BT and Kingston have to consult with local public bodies and cannot remove the last PCB from a site if those bodies object ('the local veto').
- The local veto was not contentious until a few years ago – few PCBs were removed. Indeed, the number of PCBs rose for many years. This situation has now changed.
- Revenues from BT's PCBs have been falling and according to BT over 60 per cent of BT's PCBs are now unprofitable. BT argues that the local veto is unduly restrictive. Currently 43 per cent of BT's proposed removals are being rejected, on average across the UK.
- Ofcom is reviewing the rules for PCBs to establish an appropriate balance between delivering adequate local provision of PCBs while enabling BT to respond to changing commercial circumstances.
- Ofcom believes this is best ensured by continuing the local veto supported by measures to make the process more transparent, accountable and consistent.
- Therefore, Ofcom proposes to issue guidance on issues to be taken into account by local bodies when considering requests for PCB removal. The consultation and appeals process will also assist in that regard.
- Ofcom is also inviting views on the definition of a 'site'. How a site is defined determines which PCBs are subject to the local veto.
- Ofcom is also reviewing which public bodies should have the right of veto to ensure they represent the most appropriate level of local government.
- Ofcom has also considered, but at present does not prefer an approach that would define a set of USO PCB's which would be protected from removal. Other PCBs could be retained or removed at BT's discretion. This would have replaced the local veto.

The payphone market

5.1 A Public Call Box (PCB) is a pay telephone located on a public highway. There are also other types of call boxes; these are described in Annex F. There are approximately 75,000 PCBs in the UK, of which around 71,000 are provided by BT. Ofcom research shows that over a third of adults use PCBs at least occasionally and 7 per cent use them regularly. The most frequent users of PCBs are younger consumers, customers from lower income groups and those consumers with a mobile telephone only or those without a fixed or mobile telephone.

5.2 BT Payphones is a cash positive and profitable business. BT's regulatory Financial Statements 2004 show that BT Payphones' turnover was £176 million per annum and achieved a return of £60m. For the previous year, turnover was £190m and the return £63m. Nevertheless, BT's revenues from payphones have been falling – by around 40 per cent between 2000 and 2004. BT argues that this trend is mainly due to increased mobile phone penetration. (Some caution should be applied to these figures, as a transfer charge from BT's Network Business in respect of the public payphone supplementary call conveyance charge may under-recover the fully attributed costs of this service by approximately £40m – see more detail in Annex F).

5.3 The contrast of the continuing profitability of the business overall while revenues are declining reflects BT's success in maximising the profitability of parts of its PCB network. PCBs mainly in city centres are highly profitable; others primarily in rural areas are highly unprofitable.

5.4 According to BT, the average annual running costs per PCB are £1914. This figure is based on BT's operational costs and includes its indirect costs. BT advises that of its PCBs 26,189 (37 per cent) are profitable and 45,458 (63 per cent) unprofitable. Of the unprofitable PCBs, 25,597 PCBs do not cover their operational costs - for example cash collection, cleaning, maintenance and vandalism. The balance of 19,861 PCBs cover their operational costs but do not cover their indirect costs - for example people costs, external contracts, accommodation, depreciation, research and development.

5.5 BT has started a rationalisation programme with the aim of reducing the number of unprofitable PCBs and so improving the profitability of its business. It has already removed about 20,500 PCBs since March 2002 and has signalled its intention to consult on the removal of further PCBs over the next 18 months. Kingston has not yet commenced a rationalisation programme, although Ofcom is aware that Kingston proposes as some point in the future to remove about 70 (or 15 per cent) of its estate of 465 PCBs.

5.6 In carrying out any rationalisation, BT and Kingston have to ensure that USO is met and follow Ofcom rules set out in a Direction published in 2003. BT has argued that these rules are now preventing it making appropriate commercial decisions. Consumer stakeholders have also raised concerns about the rules.

5.7 BT and Kingston must not remove a PCB and/or cease to provide CBS if this would result in the complete removal of PCBs and or CBS from a Site, unless they have complied with certain consultation requirements set out in the Direction. “Site”, in relation to a PCB, is defined in the Direction to mean any area within a walking distance of 100 metres from that PCB. This means that if there are two PCBS within 100 metres of each other, BT can remove one box without consultation but if it wants then to remove the remaining payphone/service BT has to follow the consultation requirements set out in the Direction.

5.8 The Direction requires BT (and Kingston) to display a notice on the PCB which they propose to remove informing the public of the proposed change and setting out the period for representations (42 days) and to whom such representations can be made. Notice of the proposal to remove a PCB must also be given to relevant public bodies setting out the nature and effect of the proposal and that objections may be made by the bodies to which the notice has been given.

5.9 Public bodies that have to be notified are:
a) The local planning authority;
b) The local Parish Council (in the case of England);
c) The local Community Council (in the case of Scotland and Wales); and
d) In Northern Ireland, the local council and any appropriate local community groups.

5.10 BT and Kingston must not remove the PCB if they have received any written objection by any of these public bodies within the 42 day period for representations. Any such objection must state that it is an objection to the proposal and must provide reasons for this objection (the local veto).

International context

5.11 The obligation to provide PCBs applies across the EU but has been implemented in different ways in different Member States. For example, some countries such as Germany and Latvia specify the number of universal service public pay telephones. Others such as the Czech Republic and France set the number of universal service public pay telephones based on *X per '000* inhabitants. The number of PCBs include: Italy (270,000 of which 130,000 are universal service payphones), Germany (110,000), Spain (61,296) and Czech Republic (26,123). These figures suggest that the UK is at the lower end of the number of PCBs to meet the obligation.

5.12 The procedures for the removal of PCBs vary between countries. In Germany, factors such as the distance between alternative payphones, the revenue individual payphones generate and mobile coverage are considered in consultation with local authorities. By contrast, in the Slovak Republic, the universal service provider can determine whether or not to remove a public pay telephone.

5.13 The majority of Member States have not defined a “site” for the purposes of the installation and/or complete removal of public pay telephones. However, in Germany a site is two to three kilometres whereas in Switzerland it is 250 metres.

5.14 In Germany, the regulator is piloting a scheme whereby Deutsche Telekom is trialling a "basic payphone" which is fully functional but costs considerably less to install and maintain. There is no coin module or lighting. Calls are charged at normal payphone rates using calling cards and credit cards. Calls to the emergency organisations are free. 7,500 “basic payphones” have been installed to date.

5.15 In Australia, Telstra has the responsibility of ensuring that payphones are reasonably accessible to all people in Australia on an equitable basis. Australia has over 68,000 payphones. Telstra operates just over 34,000 payphones. Before removing the final payphone from a site Telstra will consult with the local community, site owner, and local Government authority. This will include the posting of a notice at the site for at least three months. Any comments provided will be taken into account in making a final decision about removal of the service.

Issues identified with current removal procedures

5.16 In pre-consultation discussions with stakeholders, Ofcom has identified several areas of concern with the current procedure for the removal of PCBs.

Issue 1 - reasonableness of objections

5.17 When the procedures were amended in 2003, it was hoped that they would encourage a more constructive dialogue between BT and public bodies. The obligation for public bodies to provide reasons was considered a proportionate obligation in relation to their power to object to the removal of the last PCB from a Site and improved the transparency of the procedure.

5.18 Between January and October 2004, the average objection rate across the UK by public bodies to BT's planned removals was 43 per cent (BT figures). Many objections to proposals to remove the last PCB from a Site relate to social inclusion, for example proximity to communities with relatively low fixed-line phone penetration (both urban and rural) or rural/remote areas with no mobile phone coverage. Other types of reasons are also sometimes provided; set out below are some examples of objections which BT says it has received:

- The removal of a payphone area serving 19 households, taking £1.40 in revenue per annum and with no calls to the emergency services in the preceding four months, was objected to by the parish council on the grounds that it provided a "useful landmark" and it was needed to make calls to the emergency services.
- A parish council objected to the removal of the PCB as "the light from the payphone illuminated the parish council notice board at night". The PCB took £12.98 in revenue per annum.
- Another parish council objected "because the light provides a useful beacon on dark nights."

Issue 2 – the consultation process

5.19 As explained above, when they propose to remove the last PCB from a Site, BT and Kingston must consult the specified public bodies and display a notice on the PCB. Concerns raised about this process include:

- There are approximately 10,000 parish and town and community councils in England and Wales and 1,200 community councils in Scotland. The consultation process is resource intensive and there are difficulties in obtaining contact details for some councils.
- Some MPs have suggested that they should be involved in the consultation.
- Concern has been expressed that the consultation process does not allow sufficient time for the body to raise objections with BT.
- Several stakeholders have suggested that the notice to local authorities should make clear that BT will not remove the PCB if they receive a reasoned objection.
- BT has expressed a concern that there is no right of appeal.

Approaches to regulation of PCBs

5.20 In response to the changes to the market for PCBs, Ofcom has identified three approaches for consideration (Annex K contains the Regulatory Impact Assessment):

- Retain but modify the current arrangements: local public bodies would keep their veto but the process would be made more transparent, accountable and consistent;
- Define a set of USO PCBs which would be protected from removal; or
- Remove the existing Direction.

5.21 Ofcom favours the first approach.

Approach 1: Retain the local veto

5.22 Under this approach, the current policy would remain: local communities are considered to be in the best position to bring to BT's attention particular factors in relation to specific sites. Local authorities represent these communities. Ofcom would continue to delegate its powers in this area of regulation to local public bodies. BT and Kingston would continue to need to consult and to seek approval from local bodies for the removal of the last PCB on a Site.

5.23 To deal with some of the problems identified above, there are proposals for modifications to the current procedure to reflect concerns raised by stakeholders. These proposals could be included in a modified Direction (which would be subject to formal consultation). The proposals relate to:

- The definition of a site
- Public bodies with whom BT and Kingston should consult
- The consultation process
- The reasons provided by public bodies
- An appeal process

In addition, the required consultation and appeals process set out in the Act will assist in making the process more transparent and accountable.

Definition of a "Site"

5.24 The definition of "Site" is crucial as to whether or not BT is required to consult with, and obtain consent from, relevant public bodies before the PCB can be removed. The larger the Site, the more likely a particular PCB will form part of an existing Site with another PCB and therefore consultation prior to its removal will not be necessary, providing that a single PCB would remain on this site.

5.25 Factors that need to be considered in the definition of Site, many of which are subjective, include different consumers' ability or willingness to walk or travel the specified distance to the next available PCB. Ofcom's research indicated that there was an urban/rural split in terms of expectations of distance in relation to a PCB. A maximum five minutes' walk was deemed reasonable in urban areas, and 20-30 minutes' walk in rural areas. Details of the research are set out in Annex D.

5.26 Ofcom considers it appropriate to review the 100 metre definition. For example, a definition of 200 metres might be considered to be a relatively short distance. A definition of 300 or 400 metres would represent approximately five minutes walking time for most PCB users, although such distances could represent a more significant burden for some older and disabled consumers. The impact of these new distances on the number of PCBs that BT could remove without consultation is set out in Annex F.

Public bodies with whom BT and Kingston should consult

5.27 Under the terms of the current Direction under the USO condition, BT and Kingston have to consult with the public bodies set out above. The number of bodies is around 12,000. This represents a significant regulatory burden. In addition there is the difficulty in identifying some of the bodies. Further, the more bodies, the more difficult it is to achieve a consistency of approach. There is a question as to whether the bodies that need to be consulted should be reduced.

The local body consulted could in turn have an obligation to consult with other public bodies in the area and with the local community.

5.28 A possible revised list of higher-level bodies through which BT and Kingston could consult is set out below:

England	**County Councils(35):** Two-tier Counties (34); Unitary Council (1) **District Councils (351):** Two-tier Districts (238); Metropolitan Counties (36); Unitary Authorities (45); London Boroughs (32) **Other Councils (2):** Corporation of London; Council of the Isles of Scilly
Scotland	**Unitary Councils (32)**
Wales:	**Unitary Counties (22)**
N Ireland:	**Unitary Districts (26)**

Consultation process

5.29 Under the first approach, BT would remain obliged to place a notice in the PCB and to consult with the relevant local public bodies. In exercising the delegated power, the body has to comply with the notification and consultation requirements set out in the Act; these are explained in below.

5.30 Before it objects to the removal of the last PCB from a Site, a public body must publish a notification:

a) Stating that there is a proposal to give, modify or withdraw it;
b) Identifying the person whose proposal it is;
c) Setting out the objection to which the proposal relates;
d) Setting out the effect of the objection or of its proposed modification or withdrawal;
e) Giving reasons for the making of the proposal; and
f) Specifying the period within which representations may be made about the proposal to the person whose proposal it is. (Section 49(4))

5.31 A public body may give its objection to the removal of the last PCB from a Site only if it has considered every representation about the proposal that is made to it within the period specified in the notification and it has had regard to every international obligation of the UK (if any) which has been notified to Ofcom for the purposes of this requirement by the Secretary of State. (Section 49(9))

5.32 The publication of a notification under this section must be in such manner as appears to the public body publishing it to be appropriate for bringing the contents of the notification to the attention of such persons as it considers appropriate – this could for example be an advertisement in the local press. (Section 49(10))

5.33 It is clearly important that the public bodies understand that they have the power to object to a removal and that there are notification and consultation requirements placed on them by the Act. It has been suggested that BT and Kingston should advise the public bodies of its powers and duties when they write to them. This could be in the form of standard text or a leaflet included in the letter and agreed with Ofcom.

5.34 The current consultation period stands at 42 days. This period has to allow sufficient time for people to see the notice, for the public body to publish its notification, for comments to be received and considered and for the body to object. Ofcom does not consider 42 days to be an adequate period to allow due process. An overall consultation period between BT and the local body of 90 days may be more appropriate, allowing 42 days for the payphone notice and one month for the notification.

Obligation on public bodies to provide reasons

5.35 In exercising their delegated powers, public bodies must provide reasons for their objection in writing and comply with the requirements in section 49(2) of the Act that the objection must be objectively justifiable, not discriminate unduly, and be proportionate to what it is intended to achieve and transparent. The public body must also act in accordance with the six Community requirements including, the requirements, to promote competition and to promote the interests of all EU citizens.

5.36 To assist public bodies in carrying out their duties and to promote consistency between bodies, Ofcom is proposing to develop a set of guidelines. Some of the factors which might be considered objectively justifiable and relevant to the public body's decision and which could form the basis of guidelines include the number of households in the area; the distance to the nearest alternative PCB; housing type in the area; the incidence of vandalism; the profitability of the PCB; annual volume of calls; annual cost; the number of emergency calls and mobile phone coverage at the site. More details are given in Annex F.

Appeals

5.37 If this approach is adopted, the decision by the public body to object to a proposed removal would be subject to appeal. The Competition Appeals Tribunal would be the appellate body and decide appeals on the merits.

Revenue Threshold

5.38 It may be appropriate to consider whether there could be a revenue threshold so that if a PCB takes so little money BT could be required to consult and have to take account of objections but the veto might not apply. This approach could require an amendment to the USO Conditions.

Q7 Comments are invited on the preferred approach, in particular on:

- *The principle of delegating power to local public bodies to object to PCB removal;*
- *Whether there are other bodies that could undertake this delegated power;*
- *an amendment to the definition of "Site";*
- *the appropriate public bodies to have the power to object;*
- *the consultation period for the public body to object;*
- *factors that might be considered in guidance for objecting*
- *the use and level of a revenue threshold.*

Approach 2: Defining a Universal Service PCB

5.39 This approach assumes the current procedures would be replaced with a new definition of a universal service PCB by reference to an algorithm or a set of threshold criteria. Defined PCBs would be protected from removal. Other PCBs could be retained or removed at BT's commercial discretion. The primary difference with the favoured approach is that this would be an automated process that does not provide for local consultation and input. The local veto would be removed. It would however provide a consistent approach across the UK.

5.40 An algorithm is a program using a set of rules to make a calculation. Ofcom has developed an outline model for an algorithm that could be used. Factors included in the model to date are similar to those identified in the context of guidance on factors to be considered by public bodies (see Annex F). The factors would include number of households in the area; distance to the nearest alternative PCB; housing type; incidence of vandalism.

5.41 Ofcom considered further factors as possibly relevant in creating the model for an algorithm if data could be obtained: profitability of a PCB; annual revenue from a PCB; annual volume of calls from a PCB; annual cost of providing a PCB; annual volume of emergency calls from a PCB; and mobile phone coverage at the site of a PCB.

5.42 BT has suggested the use of threshold criteria, whereby each PCB is assessed and those meeting the criteria would be defined as a USO PCB. The approach is similar to that of using an algorithm. It will be open to BT to put forward this evaluation criteria as a future approach as part of its response to this consultation.

Q8 Comments are invited on this approach, in particular on

- *whether the use of an algorithm would be a practical, effective, transparent mechanism for defining a USO PCB; and if so*
- *the factors that might be included in the algorithm*
- *Whether there are other alternative methods of defining a USO PCB that could be considered.*

Approach 3: Remove the existing Direction

5.43 This deregulatory approach assumes that the detailed requirements would be removed. There would continue to be a general requirement that BT and Kingston meet the reasonable needs of PCB users. There would be no local veto. PCB removal would be a matter for BT and Kingston by reference to the Universal Service Order and USO Condition 3. BT and Kingston could be required to report on their performance in complying with its USO, for example by providing information on the number of PCBs installed, removed or re-sited. Normal enforcement powers would be available to Ofcom if it considered that BT or Kingston was not meeting the overall obligation.

Ofcom's preferred approach

5.44 Ofcom's preferred approach is to maintain the local veto but improve procedures. In Ofcom's view, local public bodies and communities are in the best position to know about relevant factors in relation to specific sites In addition, the procedures should encourage a more transparent and constructive dialogue between public bodies and BT and Kingston. The first approach would ensure that the PCBs to meet the obligation are provided via the least intrusive regulatory mechanism to achieve the policy objectives, is transparent as to purpose and that no undue discrimination arises.

5.45 The obligation for public bodies to consult and to provide reasons is a proportionate measure in relation to local bodies' power to object to the removal of the last PCB from a Site. It also improves the transparency of the procedure. The development of guidelines should help address concerns about the consistency and nature of objections. The rights of USPs to appeal the decisions of public bodies provide a balance to the rights of public bodies to object to such removals.

5.46 Ofcom is not supporting the definition of USO PCBs through the use of an algorithm. Although it would provide a consistent approach across the UK, Ofcom considers that the use of an algorithm would not be fully transparent and would not offer the flexibility to take account of relevant local factors. In addition, Ofcom is concerned that an algorithm which models a very complex area and where some relevant data is not available might not generate a consensus among Ofcom's stakeholders.

5.47 Ofcom is also not proposing the removal of the Direction. Ofcom believes that the lack of local input would lead to the loss of transparency and to an inconsistent approach. A Regulatory Impact Assessment is set out in Annex K.

Other Issues

Requirement to offer cash payment facilities in PCBs

5.48 BT and Kingston must ensure that at least one PCB at a Site offers cash payment facilities, except for sites which, for historical reasons, have no cash payment option. This requirement was to ensure that customers had easy access to PCB services. BT says that it has experienced a high incidence of 'cash box attacks' on low revenue PCBs in rural and semi-rural locations and that the annual cost of crime to its PCB business is substantial.

5.49 Ofcom's stakeholders have in the past supported multi-payment options for single PCB sites, including the requirement to offer cash payment facilities. However, it may not be reasonable to expect BT or Kingston to continue to provide PCBs that are subject to constant vandalism and crime with a cash payment facility.

5.50 BT has suggested that a basic cashless PCB, offering at least emergency, operator assistance and freephone calls, could in some circumstances replace the final PCB at a site, in particular at roadsides outside town or villages. Such PCBs may be little used but can be important for making emergency calls. BT has suggested that instead of removing these boxes, it could replace them with emergency call boxes that would be less expensive for BT to operate but still meet local need. Ofcom can see potential benefits in this approach. However, Ofcom believes that any such replacement of the PCB would have to be with the agreement of the local public bodies.

Q9 Should the existing requirement on BT and Kingston to offer cash payment facilities in the last PCB at a Site be retained or amended? Please give reasons.

Q10 Comments are invited on the introduction of emergency and freephone call boxes. In what circumstances could they replace the PCB? Should the local public body have to consent if they are to replace the last PCB on a site?

Alternative funding, requests for new PCBs and future contestability

5.51 In Annex F Ofcom considers issues around a) the contribution by other bodies to the costs of providing particular PCBs and b) the handling by BT and Kingston of requests for new PCBs. In relation to the future provision of USO PCBs, as set out in Section 3 and in the Strategic Review, it may at some stage be appropriate to determine new methods of supplying and funding USO. It is conceivable that provision of USO PCBs could be made contestable and/or subject to an auction with the potential for a contribution from any USO fund that has been established.

Section 6

Services for customers with disabilities

Summary

- Some of the most important Universal Service measures relate to provision of services for customers with disabilities. They ensure access to, and affordability of, a range of essential services.
- One of the key services is the text relay service which is highly valued by customers. However, it needs to evolve as demand and technology changes. Ofcom is proposing a study into the expansion of the service to include video relay. Ofcom is encouraging the introduction of IP based technology which will enhance the range of services that can be provided.
- The transparency and accountability of the text relay service should be improved. Ofcom is seeking views on the establishment of a Stakeholder Advisory Panel and on a new requirement for the publication of an annual plan and report on the operation the service.
- Ofcom is encouraging payphone providers to meet their obligations to consult on accessibility of payphones to customers with disabilities.

Introduction

6.1 A number of services have to be provided to end-users with a disability. With one exception they apply to all providers through the general conditions:

- Funding of a text relay service (BT only by means of a specific condition);
- Access to text relay service and rebate scheme (all providers);
- Certain requirements to make all public payphones accessible to customers with disabilities (all public payphone providers);
- Directory information free of charge and through connection (all providers);
- Bills/contract provision in Braille/ large print (all providers);
- Priority fault repair (all providers);
- Safeguard third party bill management (all providers);

6.2 This section focuses on the provisions that relate to the text relay service, payphones and bill/contract provisions.

General or specific requirements

6.3 Part III of the Disability Discrimination Act 1995 (the DDA) requires providers to make reasonable adjustments to services and to their premises to overcome barriers to access to disabled persons. It could be argued that the DDA requirements are sufficient to implement the relevant provisions of the USD and Order and could perhaps replace the specific telecoms requirements in the general and specific conditions described above. Reliance on the DDA alone could avoid 'double jeopardy'; there would be just one set of rules and a lightening of the regulatory burden.

6.4 Following a pre-consultation with affected stakeholders Ofcom believes there is a strong case against relying exclusively on the DDA. Ofcom considers that the

DDA is not specific enough to be relied on to implement the specific provisions of the USO and in particular the Order. Moreover the Disability Rights Commission takes the view that reliance on the DDA alone is insufficient. A second consideration is that enforcement of individual rights may be more difficult for disabled customers under the DDA than under the conditions. Ofcom considers a general condition offers a simpler, cheaper and quicker process. For these reasons, Ofcom believes that it still appropriate to continue to have specific obligations.

The text relay service

6.5 The text relay service, which provides live translation by operators of voice into text and vice versa enables deaf, hard of hearing and speech-impaired users to communicate. Research conducted by MORI for Ofcom (Annex D) revealed that textphones, were highly valued as the most immediate way of contacting a hearing person. Further details about the relay service are set out in Annex G.

The international context

6.6 Services for disabled people vary considerably across the EU. It is up to Member States to determine, according to national conditions, what services are to be required. Many countries have equivalents to the text relay service. Sweden has gone further and implemented a video relay service. A similar scheme is in operation in the USA. Video relay schemes are at present not cheap. The Swedish service costs around £750 per user per year or £39 per call; the US video service is over five times more expensive than the text relay service, on a per minute basis. Further details of these costs and take-up estimates are given in Annex G.

Issues for consultation

6.7 The relay service is rooted in traditional voice telephony. Many stakeholders consider that, despite the innovations brought about by TextDirect, the service has not kept pace with technology. This view emerged strongly in the research (see Annex D). Accordingly, a number of proposals have been made to Ofcom by stakeholders suggesting an updating of the relay service. The main ones are to extend the relay service to encompass video, to provide web-based access to the relay service and to input messages using email and SMS.

Video relay

6.8 Video relay is comparable to text relay with the difference that the relay element would offer British Sign Language (BSL)/voice rather than text/voice interpretation. The key components of such a service would be a video terminal for the BSL user and a link to a BSL interpreter. Video relay is more flexible than video interpretation services, which tend to be by appointment only and require the BSL user and the other party to the conversation to be together in the same place, connected by videophone to a remote interpreter. A video relay service offers communication, ideally at any time, between a BSL user, a hearing person and an interpreter, each in a different place.

6.9 Support for the introduction of a relay service arises from a number of developments, the most significant of which are:

- the roll-out of video relay services in the USA and Sweden;

- the Government's March 2003 recognition of BSL;
- IP-based technologies can support multiple forms of data communication.

Option 1: Require the implementation of a video relay service now

6.10 The British Deaf Association (BDA) and other disability stakeholders have pressed for a video relay service to be made available by means of a change to the definition of relay services in the specific conditions. The effect would be that BT would be required to provide funding for a video relay service and all providers subject to the condition would be obliged to offer access to it. At present, the definition of relay service relates only to text/voice. The main case made for establishing a video relay service is that it would enable the estimated 50,000 BSL users in the UK to communicate with hearing people in their language of preference. Although the majority of BSL users are able to use the existing text relay service, video relay is said by its proponents to offer the prospect of a more personal form of communication. A further argument is that it would make the optimal use of the 200 qualified BSL interpreters in the UK. These arguments carry some weight but Ofcom also needs to take account of a number of other factors.

- **Linguistic issues** The primary case that has been put for a video relay service rests on BSL's linguistic status. It is the language of choice for many members of the UK's deaf community.
- **Technical issues** A video relay service requires a high speed data connection. This could in theory be an ISDN link but broadband has advantages in terms of speed and the ability to use equipment such as a web cam-enabled PC or laptop. However, not everyone has broadband which means that it is not itself mainstream. The issue of wider availability of broadband is a matter considered in the Strategic Review.
- **The market for a video relay service** Any mandatory obligation would need to satisfy the proportionality test amongst others, by addressing the question of whether the promised benefits outweigh the additional burden. Ofcom estimates that the total number of users of a video relay service is at present unlikely to exceed a few thousand customers - based on the proportion of the hearing impaired customers who currently use the text relay service and experience in countries where video relay services operate. The experience of Sweden and USA outlined in the international contexts paragraph above suggests that video relay services are at present extremely costly compared to traditional voice services. Further details of these costs and take-up estimates are given in Annex G.

6.11 Ofcom recognises the importance of the linguistic issue however, for the technical and practical reasons set out above, does not consider the analysis currently supports the option to implement a video relay service obligation now.

Option 2: Rule out the introduction of a video relay service

6.12 Another option would be to recognise the likely small demand for a video relay service and the high cost and technical difficulties. On this basis, the option of a video relay could be ruled out. Ofcom does not consider it appropriate to foreclose the debate at this time, particularly as a video relay service would offer considerable benefits as explained above.

Option 3: Commission a study into a video relay service

6.13 A number of unknown factors need to be assessed before a realistic assessment of the costs and benefits of a video relay service can be drawn up. Accordingly, Ofcom's preferred option is that a feasibility study should be undertaken. Ofcom proposes to commission this study during 2005. Amongst the issues to be considered would be technical feasibility, the market for this service, how much would the service cost and how and by whom would the service be provided. The findings would be published.

Q11 Do you agree that a feasibility study of a video relay should be carried out? Comments are invited on the scope of such a study.

Governance of the relay service

6.14 The relay service depends on collaboration between the RNID and BT. Responsibility for the interpretation element of the relay service and the employment of the relay operators rests with RNID. The funding and network connections are BT's responsibility. The introduction of TextDirect in 2001 transferred some of the intelligence and functionality away from the relay centre into BT's network. This shift has been paralleled by BT's growing involvement in the administration of the relay service.

6.15 Some stakeholders have raised concerns about this shift. These stakeholders argue that as BT's primary duty is to its shareholders it lacks the incentive to invest in improvements to the relay service. Furthermore stakeholders argue that Ofcom should award a contract to provide relay services through an open tender process. Ofcom believes that at this stage it would not be reasonable to separate BT's funding of a universal service from its ability to oversee the delivery of that service. Moreover, in the short term it may not be possible to provide a relay service that excluded BT involvement. The functionalities of the relay service element (Typetalk) and the network element (TextDirect) are closely integrated. It would take time and substantial new investment to build an alternative network gateway.

6.16 Nevertheless, Ofcom considers the relay service should take more account of the views of its users and other stakeholders. Typetalk established a Customer Forum for the relay service. Ofcom welcomes this development, however the Forum may be perceived as being insufficiently independent and not integrated into the decision-making process. Moreover it does not include other communications providers.

6.17 Ofcom believes it may be beneficial to establish an Advisory Panel which could look at more strategic issues and involve both users and communications providers. As the Advisory Panel would not wield executive powers or a veto, it should not impose additional costs. The intention is not to stifle BT's capacity to manage the service but to promote a dialogue with stakeholders before reaching informed decisions. One model is provided by the Australian National Relay Service Consultative Committee (NRSCC) which provides specialised consumer advice on National Relay Service issues. Another measure that would promote transparency could be the publication of performance targets and an annual report.

Q12 Ofcom invites views on a Stakeholder Advisory Panel including the membership and terms of reference of such a Panel.

Q13 Do you agree that the relay service could publish an annual plan and report?

Web-based access to the relay service

6.18 A number of stakeholders would like to access the text relay service from their PC. Amongst the advantages would be use of a mass market product, a better screen, a more user-friendly keyboard, the ability to print conversations and, by connecting a laptop to a local area network, mobility. Ofcom's research revealed that web access was viewed as the most attractive future development path for the relay service. In practice it is already possible to download software into a PC and connect to the relay service.

6.19 Web access to the relay service links the twin ideas of being able to access the service using a PC and connecting to an Internet Protocol (IP) network which offers the advantages of speed, bandwidth, non-dedicated terminals and multimedia transmission. It is increasingly used in the USA to provide a backbone for the relay service (see www.fcc.gov/cgb/consumerfacts/iprelay.html). Ofcom sees considerable advantages in the relay service migrating to an IP platform that would enable web-based access. However, two issues require consideration.

6.20 It would not be appropriate for Ofcom to mandate the migration to IP. It is for providers to choose between competing technologies. Ofcom can instead encourage BT to take full account of the advantages of a relay service reliant on new technology.

6.21 Second, web-based services are traditionally 'free' at the point of delivery. Current access to the relay service enables charging without prior registration. This offers flexibility and avoids any obligation for users to prove their medical entitlement to the service. Free access to the relay service through web-access could undermine its economic underpinning and expose providers to fraudulent use. Before an IP-based service is launched there will need to be consideration on how best to reconcile the twin objectives of fraud avoidance and flexibility for the customer. Ofcom is drawing attention to this issue now so that potential solutions could be explored by stakeholders in Typetalk's Consumer Forum or the proposed Stakeholder Advisory Panel.

Alternative text formats

6.22 There is evidence, supported by the research, that mobile users would value being able to send a SMS message to contacts who have textphone access but no mobile. However, the market for such a service is likely to be small, because mobile penetration is high amongst the deaf and hard of hearing community. 75 per cent of respondents to the City University's Text Communication Survey (see Annex D) had a mobile phone. A Typetalk service is available which enables SMS, fax and email messages to be made from a textphone. As access to the relay service becomes more widely available from mobiles, demand for SMS/textphone service seems likely to shrink.

6.23 People with hearing difficulties have embraced email. Over half (52 per cent) of the respondents to the City University's Survey used email on a daily basis, with a further 26 per cent recording weekly use. There is no widely-expressed enthusiasm for linking emails with the relay service. Users viewed it as another aspect of a prospective migration of the relay service to packet-switching.

Q14 Ofcom invites views on its conclusion that mobile/email access should not be pursued at this stage.

Payphone accessibility

6.24 The requirements in relation to accessibility of PCBs are that:

- At least 75 per cent of PCBs provided in the UK (except Hull) and 50 per cent of PCBs provided in Hull must be accessible by reasonable means to customers in wheelchairs,
- At least 70 per cent of all PCBs must incorporate additional receiving amplification,
- Providers must consult with Ofcom from time to time on "… all future material changes to the design of its PCBS where the interests of disabled persons are likely to be affected"

6.25 At the time these provisions were introduced, wheelchair accessibility was about overcoming the barriers imposed by the design of traditional PCBs. As these PCBs were replaced, there was an expectation that the percentage of accessible PCBs would increase. However, although there are fewer traditional PCBs, accessibility issues have not been solved automatically. Wheelchair accessibility is about more than physical entry to the PCB. Some wheelchair users have reported difficulties with multimedia kiosks because they find the coin and card slots are virtually unreachable from a wheelchair. Accessibility issues also arise for non-wheelchair users. Visually impaired users have argued that more could be done to make call boxes more accessible. Hearing impaired users may wish to see a requirement for hearing-aid compatibility. There are essentially two ways to address these issues.

Option 1: Imposition of new accessibility requirements

6.26 The first option involves greater regulation, specifying new requirements. This would provide clarity to providers and ensure that modifications were implemented. The case against this approach is that it is too prescriptive. Imposing a single design solution precludes alternative solutions and stifles the possibility of innovation. There is no one ideal design solution that will overcome barriers for all users.

Option 2: Maintain existing obligations

6.27 Ofcom's preferred option is to maintain the existing requirements but to ensure providers meet their obligation to consult on the design of PCBs. The need to consult will encourage providers to take account of the diversity of PCB users and to avoid installing PCBs that exclude significant groups of users. To date no such consultation has taken place. Given stakeholders concerns, Ofcom believes that it is now appropriate for providers to fulfil their obligations.

Q15 Do you agree that Option 2 offers the best opportunity for improving the accessibility of public call boxes?

Acceptable formats for bills and contracts

6.28 The Order requires measures to ensure that methods of billing and of accepting payment are available in an appropriate format. General Condition 15 requires providers to supply contracts and bills in reasonably acceptable formats to blind or visually-impaired subscribers on request and free of charge. Stakeholders have argued that it is not only blind or visually impaired subscribers who might experience difficulties in reading standard formats. It has been proposed that the obligation be revised to require the provision of bills and contracts in an alternative format to any subscriber whose disability prevents their reading bills or contracts in conventional formats. Ofcom agrees and proposes that the condition should be amended accordingly and proposes to consult on an amendment to the condition.

Q16 Do you agree that the obligation should be redefined to apply to all subscribers who are not able to read printed bills and contracts?

Other issues

6.29 Three other issues are considered in Annex G: first, a mystery shopping exercise by Ofcom into how providers promoted services for disabled customers; second, the duty in section 10 of the Act on Ofcom to encourage the development and availability of telecoms apparatus. Third, Ofcom considers the requirement on providers to consult with the Consumer Panel on the requirements and interests of disabled customers and proposes an amendment to the general condition 15.1.

Section 7

Provision of a connection upon reasonable request

Summary

- BT and Kingston are each required to provide access to basic telephone services upon reasonable request and at uniform prices, irrespective of location.
- Where installation of a new line costs £3400 or less, BT makes a standard charge (£74.99 for residential, £116.33 for business). Where installation costs over £3400, BT requires the user to pay the excess costs (plus its standard charge).
- Although connections costing more than £3400 mostly occur in rural areas, the provision of a connection upon reasonable request is not exclusively a rural issue. It can also cost more than £3400 for a connection in an urban area.
- Ofcom believes that BT's general approach of a 'threshold' is sensible in the interests of efficiency and consistency, and therefore intends to issue a formal consent to BT to allow it to charge non-uniform prices.
- Ofcom is therefore seeking further information from BT and other stakeholders to help it decide an appropriate threshold and proposes to publish guidance.

Background

7.1 BT and Kingston are required to meet all reasonable requests for a connection to the telephone network at a fixed location. The obligation also requires that telephony services are priced uniformly, irrespective of geographic location. The uniform pricing requirement means services must be charged at the same price even where there are differences in the cost of provision. Such pricing ensures that services are affordable in all geographic areas of the UK where the high costs of provision could disadvantage groups of customers. Connections that cost more than £3400 are more likely in rural locations but not exclusively so they also occur in urban areas. Under the Order and Universal Service Condition 1 Ofcom may consent to non uniform prices, but only where there is clear justification for doing so.

International Context

7.2 The policies adopted with regard to reasonable access differ across Europe. In Austria, the USP makes a standard charge for connection, as long as the new customer's premises are within 500 metres of the next cable box. Beyond this distance, the customer must bear the additional costs. The relevant legislation in Finland requires provision to anyone at a 'reasonable price'. This has been defined as a price reasonable for an average user but does not mean that the price must be the same irrespective of geographical location or the costs of connection. The Finnish regulator has not set a specific financial threshold. No special consideration is given to people in areas without mobile reception. In Norway, the incumbent has a similar obligation to BT in that it refers to meeting all reasonable requests. There is no financial threshold. Instead, where premises are located outside the 'normal delivery area', the provider may charge the customer the extra cost.

BT's and Kingston's connection charging policies

7.3 BT makes a standard charge for new connections of £74.99 (inc VAT) for residential customers, £116.33 (inc VAT) for businesses. Where BT calculates that its installation costs will exceed a threshold of £3400, it requires the customer to pay the excess, i.e. the cost of installation minus £3400, plus the standard connection charge. Kingston has a standard connection charge.

Issue 1: BT's threshold policy

7.4 Under BT's threshold policy, all customers pay the standard charge throughout the UK if the costs are below £3400. Above £3400, prices are not uniform and customers pay according to their individual circumstances. While BT may be applying its £3400 rule uniformly across the UK (excluding Hull), the price paid by end users is variable, as it depends on the cost to BT of providing the connection and whether this falls below the £3400 threshold. It could therefore be argued that BT is not complying with its obligation to provide connection at a uniform price. Ofcom considers there are two ways to address this situation.

Policy Options

Option 1: BT meets all reasonable requests for connection at a standard price

7.5 Under this option, BT would have to abandon the threshold and would be required to meet all reasonable requests for connection at a standard price, irrespective of costs, i.e. it would no longer be able to charge extra. BT would have the right not to meet requests that are unreasonable.

Option 2: BT applies a threshold and Ofcom consents to non uniform charges

7.6 This option would maintain the current approach in practice with BT charging a non uniform tariff where the costs of connection exceed a threshold, whatever that might be.

BT's policy in practice

7.7 The £3400 threshold only applies to the first narrowband line at a site. Multi-tenanted premises are eligible to one discount per site. Excess construction charges can be shared providing customers organise this co-operation themselves, with each customer having their own £3400 allowance. BT does not take into account whether other customers in the geographical area in question may subsequently want service. Further details on inclusions/ exclusions are given in Annex H. Over a recent twelve month period, under its USO, BT provided connections involving excess charges to 28 customers. In the same period, BT completed a total of two million orders; this figure covers USO and non-USO lines.

Need for more information

7.8 Against the total of two million new lines, the issue of excess charges appears to be relatively minor. However, there is a need for caution about coming to this conclusion. BT has not retained data on requests for connection where an excess charge is involved, only those where the customer agreed to pay the excess. Ofcom does not know how many cases have arisen where costs would exceed £3400 but a customer has decided not to proceed. Nor does Ofcom know the full range of excess charges that have been quoted. BT has now agreed to keep full records over a three month period. This data will be useful but will not reveal the extent of ‘suppressed demand’ i.e. people who have previously tried to get connection but who did not pay the excess charge.

Connection charges in other utilities

7.9 In both the water and energy sectors, but more particularly in energy, the policy in relation to connection charges involves more intervention by the relevant regulator under their respective sectoral powers than in the telecoms sector (see Annex H).

Ofcom's conclusions

7.10 Option 1 would benefit consumers who would otherwise be required to pay excess charges. However, if the number of requests for such connections proved to be high, BT might be incentivised to refuse requests for connection on the basis that the requests were not reasonable. BT is concerned about such ‘suppressed demand’. It is therefore possible that Option 1 would either increase the financial burden upon BT or lead to customers who would otherwise be prepared to pay the excess at the current rate, not being able to have connection to the network. In view of the potential risks of either BT being exposed to high costs and/or of BT refusing requests for connections altogether on the grounds that they are ‘unreasonable’, Ofcom supports Option 2.

7.11 The use of a threshold means the price paid by end users is variable and could conflict with the requirement to provide connection at a uniform price throughout the UK, unless Ofcom has consented otherwise. Ofcom may consent to non-uniform prices where there is clear justification. Ofcom considers that the ability to raise additional charges where the cost of connection exceeds a given threshold represents a clear justification because the threshold is a sensible balance between the interests of the majority of its customers in keeping costs down and the needs of those customers often in remote areas. In this way, Ofcom believes that there is a good reason for issuing a consent that will allow BT to apply a threshold in calculating the costs of providing connection.

Q17 Ofcom invites views on the proposal that there should be a threshold and that Ofcom should consent to BT to charging non-uniform prices above the threshold.

Issue 2: Level of the threshold – is £3400 appropriate?

7.12 If Ofcom were to consent to non-uniform pricing in the form a threshold, Ofcom also needs to consider the level of the threshold to which it should consent. This was previously based on an assessment by BT of how many man-hours would be required to complete the work. If it was less than 100 man-hours, a standard charge applied. If over 100 man-hours, the customer was required to pay a charge based on the additional work involved. This was known as the ‘100 man-hours rule’. In 2001, BT changed its approach as the contractors it employed no longer charged on the basis of man-hours. BT instead fixed a figure of £3400, based on a notional rate of £34 per hour, and this is now referred to as the ‘£3400 rule’.

How far does £3400 go?

7.13 Ofcom considers that going forward the £3400 figure seems rather arbitrary. This does not mean, however, that it is too low. Ofcom asked BT to explain what distances could be covered by a connection costing BT no more than £3400. The results which are rough estimates suggest that £3400 may not go very far. £3400 would pay for 160 metres of overhead cable supported by four poles or 25 metres of ducted cable under carriageway or roadway or 109 metres of directly buried armour cable.

7.14 Where the £3400 threshold is exceeded, BT requires the customer to pay only the amount over and above £3400 (plus the standard connection charge). BT claims that it would take over 13 years for a connection to generate enough revenue to pay back the £3400 discount. Further details are set out in Annex H.

Cases involving excess charges

7.15 Between April 2003 and March 2004, BT provided connections, under USO, involving excess charges to 24 residential and 4 business customers. Many of these customers were in rural areas but there were some who were in urban areas. BT's records indicated that the residential customers paid excess charges ranging from about £20 to £7200, the average excess being approximately £1000, and that the business customers paid excess charges ranging from £360 to £5000, the average excess being £2200. Ofcom has carried out research amongst these customers; details are in Annex H.

Guidance on BT's obligation to meet reasonable requests

7.16 Ofcom is proposing guidance on BT's obligation that would operate alongside the threshold. This guidance would help both BT and consumers understand the matters that Ofcom would take into consideration should it receive a complaint as to whether BT has met its obligation. These factors might include the following: does the request relate to a fixed location that is used for ordinary business or residential purposes? Has BT offered the consumer the possibility of doing the work themselves? Has BT considered the cheapest possible means of provision? Is the consumer elderly or disabled? Is there mobile phone reception?

Policy Options

Option 1: Consent to non-uniform charges where costs exceed £3400

7.17 Under this option, Ofcom would consent to BT continuing to apply its £3400 rule and charge a non-uniform price for connections.

Option 2: Consent, guidance and revision of threshold

7.18 This option comprises three key elements:

- A threshold would be retained; how this would be set would depend on information from BT about 'cancelled requests' for connection and on responses to this consultation;
- Ofcom would consent to BT charging non-uniform prices for connections; and
- Ofcom would issue guidance, setting out issues that Ofcom would take into consideration in deciding whether BT had complied with its USO.

Preferred option

7.19 Ofcom believes Option 2 furthers the interests of consumers by providing certainty but also enables individual circumstances to be taken into account. Option 2 also has the advantage of controlling the possible cost increase for BT and provides greater clarity about whether or not a request for connection is reasonable.

Q18 If Ofcom were to consent to a threshold, what should the threshold be and what factors should be taken into account in deciding whether or not BT has complied with its universal service obligation?

Section 8

Functional internet access

Summary

- As designated USPs, BT and Kingston are required to provide users upon request with a narrowband connection capable of ‘functional internet access’ (FIA).
- FIA Guidelines were issued in July 2003. These specified that users should be able to expect connection speeds of at least 28.8 kbit/s and also set out measures that USPs should take in response to complaints about unsatisfactory data speeds.
- On the basis of information provided by BT about prevalent data speeds and improvements it is making to its network, Ofcom does not propose making significant changes to the Guidelines at this time. Ofcom considers that the benchmark minimum speed should remain at 28.8 kbit/s for the time being. However, Ofcom believes that, to aid transparency and enforcement, the Guidelines should be refined to help ensure that USPs are complying with the requirement to provide FIA.

Background

Requirement to ensure FIA

8.1 As USPs, BT and Kingston are required upon reasonable request to provide any end-user with a narrowband connection at data rates that are sufficient to permit functional internet access*.* Before July 2003 USPs were only required to provide facsimile or voice band data up to 2400 bit/s (2.4 kbit/s).

What is FIA?

8.2 FIA has not been defined at a European level nor have the data rates that are sufficient to permit such access. The Order requires the provision of FIA but as with the USD does not define FIA. *‘Guidelines on functional internet access’* (‘the Guidelines’) were consulted upon and published in 2003 and are set out in Annex I. The Guidelines were intended to ensure a balance between consumer expectations and the resulting burden upon BT and Kingston.

International Context

8.3 The vast majority of other European countries have neither defined FIA nor specified a minimum data speed. In Sweden, however, the regulator has taken the view that FIA means at least 20 kbit/s. Where a subscriber requests a connection with a minimum data speed, this should be provided without adversely affecting the subscriber’s ability to obtain access to broadband, e.g. the provider should avoid installing Digital Access Carrier System (DACS).

8.4 By contrast, in Australia everyone has access, on request, to a data service with a 64 kbit/s digital data capability. This relates to the provision of Integrated Services Digital Network (‘ISDN’) services which provide two or more connections capable of being used simultaneously. ISDN data speeds are higher than those generally available over the ordinary telephone network. About 4 per cent of the Australian population cannot access an ISDN service and therefore require a satellite solution. These customers are entitled to an industry-funded rebate of a proportion of the cost of purchase and installation of the equipment. It is not permissible under the current EC regulatory regime to mandate speeds of 64 kbit/s. The USD makes clear that the requirement to ensure the provision of FIA is limited to a single narrowband connection and does not extend to ISDN.

The Guidelines on FIA

8.5 The Guidelines apply only to BT and Kingston. They are set out in Annex I:

- A USP will be considered to be providing FIA where it can demonstrate that it is making every reasonable effort to ensure that lines achieve optimal performance, particularly where the line is to be used for internet access.
- Whilst there is no mandatory minimum data speed, end-users should reasonably be able to expect a benchmark speed of at least 28.8 kbit/s.
- Where a user is not getting optimal performance, remedial action may be required: in particular, the provider should take all reasonable steps to avoid the use of line-sharing devices, including the DACS

8.6 Whilst the Guidelines are not binding and do not fetter Ofcom's discretion, they will be taken into account in addressing complaints about data rates.

Speed of the physical connection, not data download speed

8.7 The Guidelines refer to a connection speed of 28.8 kbit/s. Since the Guidelines address FIA (an obligation on a USP) the benchmark connection speed refers to those aspects of an internet connection which are within the control of the USP, that is, the quality of the physical connection, or line, and the rate at which signals can be transmitted over that line. This connection speed (line speed) is different from the speed at which information is downloaded from a website. The difference between the two is explained in Annex I, together with factors that may limit data speeds.

Benchmark speed of 28.8 kbit/s

8.8 The key determinant of whether a connection permits FIA is the speed at which data may be transmitted over that connection. Before the Guidelines were published, a range of possible data speeds that a line should be capable of achieving, were considered. It was decided that a speed of 28.8 kbit/s, which is a standard speed for modems, achieved the right balance between the interests of users and the resulting burden upon USPs. The intention of the Guidelines is that USPs should consider 28.8 kbit/s as the minimum speed, rather than target speed, that lines should achieve. The Guidelines may not be entirely clear on this point and Ofcom proposes to amend them to clarify this point.

Line sharing and DACS

8.9 Line sharing, or line splitting, is a means of creating two telephone lines where previously there was only one. It is a practice used by providers where demand exhausts the number of lines. Where the excess demand is small, the lack of spare lines has sometimes been overcome by providing a second voice channel on a telephone line, often by means of DACS devices. Where a line is being used for voice calls only, DACS is a perfectly acceptable technology.

8.10 If the user subsequently wants internet access, DACS can restrict the achievable rate of data transmission. For example, DACS cannot support maximum V.90 speeds. The achievable speed via DACS varies, but typical speeds seem to be around 24 kbit/s. This falls short of the benchmark speed of 28.8 kbit/s. The Guidelines set out the specific steps that providers should take where an end-user who complains of unsatisfactory internet access has a line fitted with DACS (or other similar device).

Other remedial action

8.11 There is a wide range of possible causes of slow connection speeds. Some of these are easily remedied, e.g. by removing DACS, or by replacing the overhead wire. Other problems can be more serious and resolving them can have serious resource implications. For this reason, the Guidelines clarify the circumstances where it may or may not be reasonable or proportionate to expect the provider to take remedial action on the basis of an individual complaint. Where the provider receives a certain number of complaints which are traced back to a particular piece of its network, it should either take action at the earliest reasonable opportunity to ensure FIA or put in place a work programme to address the problem.

Consumer research

8.12 In 2004 Ofcom commissioned research to evaluate what narrowband internet users understand about internet connection speeds. The research showed low awareness of the minimum speed. Details are given in Annex I. Consumer satisfaction is also relevant to the review of the Guidelines. Research suggests that overall satisfaction with home internet service remained fairly high, at around 90 per cent of homes with narrowband internet access.

Kingston's compliance with the Guidelines

8.13 The Guidelines apply to Kingston as well as to BT. Kingston has advised Ofcom that it encounters no problems in complying with the Guidelines. It does not use DACS or other line-sharing devices and has not received any complaints.

BT's compliance with the Guidelines

8.14 In 2003, BT said that about 3 per cent of its narrowband connections could not achieve 28.8 kbit/s. BT carried out a further study in June 2004, this showed:

- 99.1 per cent of lines achieved an average rate of 28.8 kbit/s or higher;
- 94.2 per cent of lines provided average data rates above 33.6 kbit/s;
- 30 per cent of lines achieved data rates between 43 and 46 kbit/s.

8.15 BT's 2004 study also revealed that only 1.2 per cent of the lines tested had DACS fitted. This is in comparison with the 2003 estimate that 3 per cent of BT's lines had DACS, and may suggest that BT has removed DACS from lines used for data communications. Further details of this study and BT's development of a tool to assess the data rate performance of lines are in Annex I. On the basis of the information provided, Ofcom believes that the Guidelines are helping to ensure the provision of FIA in the UK.

8.16 Since the introduction of the Guidelines, Ofcom has noted a change in BT's position on DACS. In a ten month period, BT has removed or reassigned DACS devices for 259 customers who complained about unsatisfactory line speeds at a total cost of £28,000. A line with DACS will not support DSL services. BT therefore has an incentive to remove DACS in order to roll out broadband services. It is aiming to remove around 70,000 DACS devices by May 2005 at a cost of approximately £8m.

Raising the benchmark speed to 33.6 kbit/s

8.17 The results of the BT study indicated that over 99 per cent of lines achieve average speeds of at least 28.8 kbit/s. This might be interpreted as suggesting that the benchmark minimum speed should be raised. However, this would be to misunderstand the intention of the Guidelines, i.e. users should enjoy 'optimal' speeds and be able to expect that their line will achieve at least 28.8 kbit/s. Competition is helping to deliver good quality narrowband access to the majority of users. It is those users whose line speeds fall below 28.8 kbit/s that the Guidelines are intended to protect.

8.18 This development indicates the real progress that has been made since the introduction of the Guidelines. However, Ofcom occasionally receives complaints regarding unsatisfactory internet speeds. Whilst on the whole BT appears to address these complaints appropriately, it is not always clear that all BT staff are familiar with the FIA requirement. Ofcom therefore considers it may be appropriate to make minor amendments to the Guidelines to ensure that compliance information is provided to Ofcom (see below). Details of BT's approach to other network problems that may affect line speed are given in Annex I.

Overall view on the Guidelines

8.19 The above information suggests that the Guidelines achieve the right balance between the interests of users and the burden upon BT and that BT is taking a responsible approach to its obligation to ensure FIA. However, there appears to be some scope for improvement. The Guidelines state that Ofcom should be provided with regular reports on the level of complaints; BT's use of DACS; and work programmes regarding improvements to its network to deliver FIA.

8.20 To date, information flows have been intermittent, although BT has responded constructively to information requests for the purposes of this review. The flow of information from BT to Ofcom regarding its compliance with the Guidelines could be improved. It is proposed to achieve this by refining the Guidelines. It is also intended to amend the Guidelines to clarify that 28.8 kbit/s is a benchmark minimum speed.

Options for consultation

8.21 The options below apply to BT and Kingston. In practice they impact more upon BT than Kingston, and therefore make specific reference to BT. None of the options involve changing the specific condition upon BT and Kingston. Option 2 is Ofcom's preferred approach.

Option 1: No Change

8.22 Under this option, the Guidelines would remain unchanged.

Option 2: Amendments to the Guidelines by way of clarification

8.23 The substance of the Guidelines would be retained, including the benchmark minimum of 28.8 kbit/s, but there would be an amendment to emphasise that FIA involves the provision of optimal speeds and that 28.8 kbit/s is a benchmark minimum speed. There would also be a clarification of the information to be provided by BT.

Option 3: Benchmark minimum speed of 33.6 kbit/s

8.24 A further option would be to raise the benchmark minimum speed to 33.6 kbit/s. This speed was considered in Oftel's consultation on the guidelines in 2003. It is the next highest standard speed at which modems operate and is above the speeds available over a line fitted with DACS.

Option 4: Removal of Guidelines

8.25 Ofcom has also considered the option of removing the Guidelines altogether and not providing any other clarification or interpretation of the requirement to ensure FIA.

Ofcom's preferred option

8.26 Option 1 offers significant benefits. Although FIA is a new addition to the USO regime and the Guidelines have therefore only been in place for a relatively short period of time, BT has undertaken a number of positive measures to comply with the Guidelines. The Guidelines have already had both direct and indirect benefits for end-users, in particular, on BT's approach to DACS. Major changes to the Guidelines do not seem to be needed at this early stage.

8.27 However, Option 2 provides an opportunity to improve consumer benefits. This is why Option 2 is preferred. Whilst the key aspects of the Guidelines would remain unchanged, the Guidelines would be revised to help monitor the obligation. This will benefit users without creating a disproportionate burden upon BT. Indeed, transparency would be increased for all and it is anticipated that Ofcom's costs of monitoring would be low. In addition, many users appear not to know about the benchmark minimum speed; re-issuing the Guidelines may increase consumer awareness.

8.28 Option 2 also seems to provide the right balance between the interests of consumers and the impact upon the USPs. Option 3 could create a disproportionate financial burden to BT. BT has estimated the costs of complying with a revised benchmark minimum speed of 33.6kbit/s at £42m. This is almost four times BT's estimated cost of complying with the current 28.8kbit/s benchmark speed. Option 4 could leave consumers disadvantaged. It is possible that, without the Guidelines, FIA would not be provided to the standard envisaged by Ofcom, resulting in consumer detriment. The Guidelines encourage USPs to make improvements to their narrowband networks and to deal positively with complaints about internet access speeds.

Q19 Do you agree that the guidelines do not require substantive change but only minor amendments to improve information flows and make them clearer?

Section 9

The costs and benefits to BT of providing Universal Service

Summary

- Universal Service is currently funded by BT and Kingston.
- Under the Communications Act, Ofcom may put in place alternative methods of provision or funding if there is a net cost – that is, the costs once the benefits have been taken into account – that imposes an unfair burden on the provider(s) with the obligation.
- The Telecoms Strategic Review has considered the medium to long term issues around universal service funding. This review focuses on the shorter term – the next two to five years.
- In this review Ofcom has considered whether a full scale review under Section 70 of the Act is required by considering how the net cost to BT of providing USO might have changed in recent years.
- Some local exchange areas, customers and public call boxes lead to a universal service cost because they are expensive to serve and/or generate low revenues.
- Ofcom's indicative estimates suggest that since 2001 the costs of serving uneconomic customers have fallen significantly while the costs of providing uneconomic payphones has risen sharply by a similar amount. Other costs are likely to have remained broadly the same.
- Benefits to BT and Kingston from providing universal services arise primarily from brand image, corporate reputation and advertising on public call boxes.
- Ofcom estimates that benefits have remained broadly the same since 2001.
- Overall, Ofcom's indicative estimates are £52-74m for the current costs to BT and around £59-64M for the benefits to BT.
- Given the lack of significant change in overall figures since 2001, Ofcom believes that there is no undue financial burden on BT as a result of USO that would justify carrying out a full scale review and the possibility of setting in place new Universal Service funding arrangements.
- However, these figures are indicative estimates and Ofcom is proposing changes to aspects of USO in this document. Views are invited on whether Ofcom should carry out a full cost benefit analysis of USO once changes proposed in this review of USO have been implemented.
- If a future analysis finds that an unfair burden does exist, the Strategic Review is examining the ways funding that might work.

Background

9.1 Under Section 70 of the Act , Ofcom may from time to time review the extent, if any, of the financial burden for a particular USP in complying with USO. At the present time, this is done by assessing the net cost of compliance accruing from designation and application to the USP of the Universal Service Conditions. The net cost is the difference in profits with and without the USO ie the costs of uneconomic customers and services less the benefits derived from being a USP.

9.2 The conclusion in the 1999-2001 review of USO was that the costs and benefits to BT were broadly matched. It was considered that if there was a small net cost this did not result in an unfair burden on BT because the net cost could be borne by BT out of profits they make on higher margin services. This conclusion was based on an update of the 1997 estimates of the costs and benefits gained by BT, which were derived by means of a detailed modelling exercise carried by the consultants Analysys.

9.3 In this section Ofcom has considered whether a full scale review under Section 70 is required. Ofcom has therefore aimed to provide an indication of the extent to which the costs and benefits to BT of universal service might have changed since 2001. The detailed analysis is set out in Annex J. Ofcom has approached this by first evaluating whether customers and services are 'uneconomic' for the USP to serve and second, the evaluation of the benefits which requires estimating how much the financial performance would further be affected if the provider would lose its USO status. Finally, the net cost is derived from subtracting the benefits from the USO costs.

International context

9.4 In the EU Italy and France have identified an unfair burden and introduced a fund based on a levy on all providers. All communications providers are obliged to contribute to this fund. In France operators contribute to the USO fund in proportion to their telecoms revenues, which is then managed by the Caisse des Depots et Consignations. Other member states have not to-date identified an unfair burden. Outside Europe, Australia, New Zealand and the USA have funding arrangements where other providers contribute to USO costs. In the USA the framework is quite complex, but providers supplying services that have been designated as communications services, pay into a USO fund in an inverse proportion to their local loop costs. This effectively creates a transfer from long distance carriers to local carriers. While the USA framework has had some success in ensuring provision of the USO, it has also created protracted legal battles over whether a service is designated as communications or information (which does not contribute to USO funding).

Costs

9.5 To evaluate whether or not a customer/service is uneconomic a comparison is made between the costs that the universal service provider would avoid if it were to discontinue service to that customer or a particular service (the *long run avoidable costs)* and the revenues that it would lose (the *long run forgone revenues*). Three components of costs have been identified:

- areas of the UK which give rise to a universal service cost (uneconomic areas)
- customers (in areas that are otherwise profitable for the universal service provider) which give rise to a universal service cost (uneconomic customers)
- PCBs which give rise to a universal service cost (uneconomic call boxes)

Table 9.1: Costs of universal service obligations incurred by BT, annual, (£m)

	1995/96 Estimates	1998/99 Estimates
Uneconomic areas	5 – 10	5 – 10
Uneconomic customers	30 – 40	38 – 48
Uneconomic PCBs	10 – 15	10 – 15
Total	45 – 65	53 – 73

Source: Oftel, Universal Telecommunication Services, a consultative document, July 1999

Uneconomic areas

9.6 Uneconomic areas are those where BT would be more profitable if it did not serve (before taking account of the benefits) – these are the most remote and least densely populated areas of the UK. Ofcom believes that net cost of uneconomic areas is likely to remain between £5M and £10M because:

- the percentage of the UK population that lives in uneconomic areas is thought not to have changed significantly (around 1 per cent);
- in general, there has been a slow decrease in number of the fixed lines and a significant increase in call minutes, leading to an even greater increase in the number of call minutes per line;
- in general, between 2000/01 and 2003/04 the per line margin from line rental improved substantially whereas the per line margin from calls decreased, leading to a significant improvement in the per line margin on average.

Uneconomic customers

9.7 Within economic areas some customers may generate a universal service cost, because they are relatively expensive to serve (e.g. long line from the exchange) or because they generate relatively low revenue (e.g. a low calling customer on LUS). They are referred to as uneconomic customers. The main source of cost is the group of customers on special schemes.

9.8 The number of users of LUS has decreased by 54 per cent since the last update from 2.6m to 1.2m.On the assumption that USO costs per LUS customer remain the same, the universal service costs from LUS users is likely to have been reduced correspondingly by 54 per cent. This suggests that the universal costs of LUS would amount to about £13-17m, (a reduction of about £15-21m). The universal service cost of IC is anticipated to have increased since the last time it was estimated because the number of IC users has doubled since then. This means that assuming an identical USO cost per IC customer the universal service costs of the IC scheme are likely to have doubled from £3m to a maximum of £6m. Taking LUS and IC together, Ofcom's indicative estimate for the cost of uneconomic 'special scheme' customers is between £19-23m.

9.9 The cost of other uneconomic customers, those that are not on a special tariff scheme, was estimated at between £5-8m. Given that the average per line margin has improved and that per call minutes margin has slightly increased since 2001, Ofcom concludes that the cost of these other uneconomic customers is unlikely to have increased. On the basis of the above, Ofcom concludes that the cost of all uneconomic customers is likely to have decreased substantially since the last estimate. Ofcom's indicative estimate is about £24-31m.

Uneconomic PCBs

9.10 Some PCBs may incur a universal service cost when they are relatively expensive to serve (e.g. frequently vandalised) or because they generate relatively low revenues. The 2001 estimate of the universal service cost of USO payphones was £10-15m.

9.11 Since March 2002, BT's programme to improve the profitability of its business has resulted in the removal of about 20,500 PCBs. Information from BT reveals a sharp decrease in the number of calls made from PCBs. Between March 1999/2000 and March 2002/03, these have declined by 53 per cent. On the basis of these changes, Ofcom believes that a reasonable indicative estimate of cost of USO payphones to BT would be in the range of £23-33m.

Conclusions

9.12 The table on the next page summarises the indicative estimates regarding the costs of the main components of USO. The magnitude of the costs does not seem to have changed much although the contribution of its different components has changed. In particular, the indicative estimate of the cost of uneconomic customers has decreased significantly whereas that of the cost of uneconomic payphones reflects a sharp increase.

Table 9.2: Costs of universal service obligations incurred by BT, annual, (£m)

	Original estimate 1995/96	Forecasts for 1998/99	Indicative estimate of costs (£m) for 2003/04
Uneconomic areas	5 – 10	5 – 10	5 – 10
Uneconomic customers	30 – 40	38 – 48	24 – 31
Uneconomic payphone	10 – 15	10 - 15	23 – 33
Total	45 – 65	53 - 73	52 – 74

Source: Oftel, *Universal Telecommunication Services* July 1999; Ofcom calculations

The benefits

9.13 Benefits are the positive effects on the current or future financial performance of the USP of providing Universal Service. The possible benefits generated are: ubiquity benefit, life-cycle effect benefit, brand enhancement, corporate reputation and advertising on call boxes. Renewed discussions have led to the identification of the following additional possible sources of benefits: advertising on other documents (such as bills), customer database, volume discounts, and services not part of USO.

9.14 Ofcom derives an indicative estimate of how these benefits have changed since 1998/9.

Table 9.3: Previous estimates of benefits to BT from USO, annual, (£m)

	Original estimate 1995/96	**Forecast for 1998/99**
Life cycle effect	£1-10m	£0-1m
Ubiquity	£40-80m	insignificant
Brand-enhancement and corporate reputation	£50m	£50m
Advertising on PCBs	£11m	£11m
Total	£102-151m	£61-62m

Source: Oftel, *Universal Telecommunication Services* July 1999

Life cycle effects

9.15 By serving a customer now when unprofitable, the operator may increase its probability of retaining that customer when s/he becomes profitable in the future. On the basis that the key factors do not seem to have increased, Ofcom has retained the same estimate i.e. £0-1m.

Ubiquity

9.16 This benefit arises when a customer moves from an uneconomic area into an economic area in which there are competing suppliers and chooses to take service from BT because they are unaware of the presence of suppliers other than BT (ie such customers would have chosen a supplier other than BT if they had been fully informed). Ofcom believes that the ubiquity benefit only exists when a customer moves from an uneconomic area to an economic one and hence that this benefit is likely to be very small. Accordingly Ofcom considers it appropriate to maintain the estimate at its previous level, namely insignificant.

Brand enhancement and corporate reputation

9.17 Benefits are likely to accrue to the USP from the effect that serving uneconomic areas, customers and PCBs has upon the operator's brand image and corporate reputation generally and hence upon its overall current and future profitability. The perception of the provider by all of its customers, and by the customers of other operators, is affected.

9.18 The brand enhancement can be thought of as being worth an amount of money each year to the USP, in terms of the cost of advertising and marketing that it would otherwise have to undertake to achieve the same effect. It is assumed this benefit could be represented by a certain percentage of BT Retail's expenditure in marketing and advertising. Using the 2003/04 figure for BT Retail marketing and sales expenditure, Ofcom considers that an indicative estimate of this benefit would amount to about £50-52m.

The benefits of serving uneconomic PCBs

9.19 The principal benefit to the universal service provider of PCBs is the value of advertising of the company's logo on uneconomic PCBs. Using the previous methodology, Ofcom believes an indicative estimate of this benefit from advertising on uneconomic PCBs would be about £9 -11m per annum.

Conclusions

9.20 Based on the above considerations, Ofcom derives indicative estimates for benefits as summarised in the table below.

Table 9.4: Benefits from universal service obligations for BT, annual, (£m)

	Initial estimate 1995/96	Forecast for 1998/99	Indicative estimate for 2003/04
Life cycle effect	1-10	0-1	0-1
Ubiquity	40-80	Insignificant	insignificant
Brand-enhancement and corporate reputation	50	50	50-52
Advertising on PCBs	11	11	9-11
Total	102-151	61-62	59-64

Source: Oftel, *Universal Telecommunication Services* July 1999; Ofcom calculations

The net cost

9.21 Overall Ofcom's indicative estimates range between £52-74m for the universal costs and between £59-64m for the benefits. Given the available evidence on costs and benefits, Ofcom does not believe that there is an undue financial burden on BT that would justify conducting a full scale review under Section 70 and any subsequent setting in place of new Universal Service funding arrangements.

Further review

9.22 The exercise carried out in this section does not represent a detailed evaluation of the costs and benefits of USO under Section 70. Rather, it gives an indication whether or not a Section 70 review is worth undertaking. The initial view of Ofcom is that this may not be the case. Indeed the above exercise suggests that an in-depth exercise is likely to confirm that USO does not generate an unfair burden on BT and hence that the case for a full scale review and a change in funding arrangement is not supported at the moment.

9.23 However, Ofcom does not exclude the possibility that a more thorough costing exercise might be needed once the new arrangements are in place following this review. If respondents present a convincing case that the initial assessment understates the net costs to BT, then Ofcom would consider whether to undertake a thorough re-assessment of all the costs and benefits of USO.

9.24 If such a reassessment showed a net cost which Ofcom judged to be an unfair burden, Ofcom would move to set up new funding arrangements. The Strategic Review is inviting views on the type of funding and provision arrangements that might be appropriate in those circumstances.

Q20 Ofcom invites views on its updated estimates of costs and benefits.

Q21 Do respondents consider that a more detailed assessment of cost and benefits should be undertaken once the new USO regime is in place?

Section 10

Responding to this consultation

How to respond

10.1 Ofcom invites written views and comments on the issues raised in this document, to be made by 21 March 2005.

10.2 Ofcom strongly prefers to receive responses as e-mail attachments, in Microsoft Word format, as this helps us to process the responses quickly and efficiently. We would also be grateful if you could assist us by completing a response cover sheet to indicate whether or not there are confidentiality issues. The cover sheet is attached or can be downloaded from the 'Consultations' section of our website.

10.3 Please can you send your response to alan.pridmore@ofcom.org.uk.

10.4 Responses may alternatively be posted or faxed to the address below, marked with the title of the consultation.

Alan Pridmore
Competition & Markets
Ofcom
Riverside House
2a Southwark Bridge Road
London SE1 9HA
Fax: 020 7981 3333

10.5 Note that we do not need a hard copy in addition to an electronic version. Also note that Ofcom will not routinely acknowledge receipt of responses.

10.6 It would be helpful if you can explain why you hold your views, and how Ofcom's proposals would impact on you.

Further information

10.7 If you have any questions about the issues raised in this consultation, or need advice on the appropriate form of response, please contact Alan Pridmore on 020 7981 3861.

Confidentiality

10.8 Ofcom thinks it is important for everyone interested in an issue to see the views expressed by consultation respondents. We will therefore usually publish all responses on our website; www.ofcom.org.uk as soon as possible after the consultation period has ended.

10.9 All comments will be treated as non-confidential unless respondents specify that part or all of the response is confidential and should not be disclosed. Please place any confidential parts of a response in a separate annex, so that non-confidential parts may be published along with the respondent's identity.

10.10 Ofcom reserves its power to disclose certain confidential information where this is necessary to fulfil its functions, although in practice it would do so only in limited circumstances.

10.11 Please also note that copyright in responses will be assumed to be assigned to Ofcom unless specifically retained.

Next steps

10.12 Following the end of the consultation period, Ofcom intends to publish a Statement and consult on any proposed amendments to the Universal Service Conditions in 2005.

10.13 Please note that you can register to get automatic notifications of when Ofcom documents are published, at http://www.ofcom.org.uk/static/subscribe/select_list.htm

Ofcom's consultation processes

10.14 Ofcom is keen to make responding to consultations easy, and has published some consultation principles (see below) which it seeks to follow, including on the length of consultations.

10.15 If you have any comments or suggestions on how Ofcom conducts its consultations, please call our consultation helpdesk on 020 7981 3003 or e-mail us at consult@ofcom.org.uk. We would particularly welcome thoughts on how Ofcom could more effectively seek the views of those groups or individuals, such as small businesses or particular types of residential consumers, whose views are less likely to be obtained in a formal consultation.

10.16 If you would like to discuss these issues, or Ofcom's consultation processes more generally, you can alternatively contact Philip Rutnam, Partner, Competition and Strategic Resources, who is Ofcom's consultation champion:

Philip Rutnam
Ofcom
Riverside House
2A Southwark Bridge Road
London SE1 9HA
Tel: 020 7981 3585
Fax: 020 7981 3333
E-mail: philip.rutnam@ofcom.org.uk

Annex A

Ofcom's consultation principles

Ofcom has published the following seven principles that it will follow for each public written consultation:

Before the consultation

1. Where possible, we will hold informal talks with people and organisations before announcing a big consultation to find out whether we are thinking in the right direction. If we do not have enough time to do this, we will hold an open meeting to explain our proposals shortly after announcing the consultation.

During the consultation

2. We will be clear about who we are consulting, why, on what questions and for how long.

3. We will make the consultation document as short and simple as possible with a summary of no more than two pages. We will try to make it as easy as possible to give us a written response. If the consultation is complicated, we may provide a shortened version for smaller organisations or individuals who would otherwise not be able to spare the time to share their views.

4. We will normally allow ten weeks for responses, other than on dispute resolution.

5. There will be a person within Ofcom who will be in charge of making sure we follow our own guidelines and reach out to the largest number of people and organisations interested in the outcome of our decisions. This individual (who we call the consultation champion) will also be the main person to contact with views on the way we run our consultations.

6. If we are not able to follow one of these principles, we will explain why. This may be because a particular issue is urgent. If we need to reduce the amount of time we have set aside for a consultation, we will let those concerned know beforehand that this is a 'red flag consultation' which needs their urgent attention.

After the consultation

7. We will look at each response carefully and with an open mind. We will give reasons for our decisions and will give an account of how the views of those concerned helped shape those decisions.

Annex B

Consultation response cover sheet

2.1 In the interests of transparency, we will publish all consultation responses in full on our website, www.ofcom.org.uk, unless a respondent specifies that all or part of their response is confidential. We will also refer to the contents of a response when explaining our decision, unless we are asked not to.

2.2 We have produced a cover sheet for responses (see below) and would be very grateful if you could send one with your response. This will speed up our processing of responses, and help to maintain confidentiality by allowing you to state very clearly what you don't want to be published. We will keep your completed cover sheets confidential.

2.3 The quality of consultation can be enhanced by publishing responses before the consultation period closes. In particular, this can help those individuals and organisations with limited resources or familiarity with the issues to respond in a more informed way. Therefore Ofcom would encourage respondents to confirm on the response cover sheet that Ofcom can publish their responses upon receipt.

2.4 We strongly prefer to receive responses in the form of a Microsoft Word attachment to an email. Our website therefore includes an electronic copy of this cover sheet, which you can download from the 'Consultations' section of our website.

2.5 Please put any confidential parts of your response in a separate annex to your response, so that they are clearly identified. This can include information such as your personal background and experience. If you want your name, contact details, or job title to remain confidential, please provide them in your cover sheet only so that we don't have to edit your response.

Cover sheet for response to an Ofcom consultation

BASIC DETAILS

Consultation title:

To (Ofcom contact):

Name of respondent:

Representing (self or organisation/s):

Address (if not received by email):

CONFIDENTIALITY

What do you want Ofcom to keep confidential?

Nothing	☐	Name/contact details/ job title	☐
Whole response	☐	Organisation	☐
Part of the response	☐	If there is no separate annex, which parts?	

If you want part of your response, your name or your organisation to be confidential, can Ofcom still publish a reference to the contents of your response (including, for any confidential parts, a general summary that does not disclose the specific information or enable you to be identified)?

Yes	☐	No	☐

DECLARATION

I confirm that the correspondence supplied with this cover sheet is a formal consultation response. It can be published in full on Ofcom's website, unless otherwise specified on this cover sheet, and all intellectual property rights in the response vest with Ofcom. If I have sent my response by email, Ofcom can disregard any standard email text about not disclosing email contents and attachments.

Ofcom can publish my response: on receipt ☐ once the consultation ends ☐

Name Signed (if hard copy)

Annex C

Consultation questions

Questions related to Section 3 – Universal Service and the Strategic Review of Telecoms

1. What should be the arrangements for funding USO in future?

2. How could competition for the delivery of USO be organised in future?

3. Should mobile technologies be used to help address the existing USO?

Questions related to Section 4 – Special Tariff Schemes and Disconnections

4 Ofcom is seeking views on all aspects of BT's proposals for a new special tariff scheme:

- the tariff structure and levels
- the use of direct debit and monthly payment plan discounts
- the target market of households within the governments' definition of poverty and in receipt of means tested benefits
- the relevant means tested benefits
- the proposed exclusion of IA/CPS and mobile users
- the use of self-declaration and of a credit checking agency to minimise BT's exposure to risk of abuse; and
- the marketing approach.

5. Ofcom is seeking views on the three options proposed: (i) No change to the BT schemes; (ii) BT's proposed new scheme to replace LUS and IC and (iii) BT's proposed new scheme to replace LUS and IC but modifications to the Scheme would be required.

Disconnections

6. Ofcom invites comments on Ofcom's view that BT should promote its portfolio of debt management and affordability services more effectively to customers experiencing payment difficulties?

Questions related to Section 5 – Public Call Boxes ('PCB')

7. Comments are invited on the preferred approach regarding arrangements for the removal of PCBs (ie to retain but modify the existing arrangements), in particular on:
   - the principle of delegating power to local public bodies to object to PCB removal;
   - whether there are other bodies that could undertake this delegated power;
   - an amendment to the definition of "Site";
   - the appropriate public bodies to have the power to object;
   - the consultation period for the public body to object;
   - factors that might be considered in guidance for objecting;
   - the use and level of a revenue threshold

8. Comments are invited on the approach to defining a Universal Service PCB, in particular on:
   - whether the use of an algorithm would be a practical, effective, transparent mechanism for defining a USO PCB; and if so
   - the factors that might be included in the algorithm;
   - whether there are other alternative methods of defining a USO PCB that could be considered.

9. Should the existing requirement on BT and Kingston to offer cash payment facilities in the last PCB at a Site be retained or amended? Please give reasons.

10. Comments are invited on the introduction of emergency and freephone call boxes. In what circumstances could they replace the PCB? Should the local public body have to consent if they are to replace the last PCB on a site?

Questions related to Section 6 – Services for customers with disabilities

11. Do you agree that a feasibility study of a video relay service should be carried out? Comments are invited on the scope of such a study.

12 Ofcom invites views on a Stakeholder Advisory Panel including the membership and terms of reference of such a Panel.

13 Do you agree that the relay service could publish an annual plan and report?

14 Ofcom invites views on its conclusion that mobile/email access should not be pursued at this stage.

15 Do you agree that Option 2 (ie maintain existing obligations) offers the best opportunity for improving the accessibility of public call boxes?

16 Do you agree that the obligation should be redefined to apply to all subscribers who are not able to read printed bills and contracts?

G1 Supplementary question: (Annex G). Do you agree that communications providers should be required to consult Ofcom to ensure that the requirements and interests of disabled End-users are fully taken into account in the development and provision of services?

Questions related to Section 7 – Provision of a connection upon reasonable request

17. Ofcom invites views on the proposal that there should be a threshold and that Ofcom should consent to BT to charging non-uniform prices above that threshold.

18. If Ofcom were to consent to a threshold, what should the threshold be and what factors should be taken into account in deciding whether or not BT has complied with its Universal Service obligation?

Questions related to Section 8 - Functional internet access

19. Do you agree that the guidelines do not require substantive change but only minor amendments to improve information flows and make them clearer?

Questions related to Section 9 – The costs and benefits of providing universal service

20. Ofcom invites views on its updated estimates of costs and benefits.

21. Do respondents consider a more detailed assessment of cost and benefits should be undertaken once the new USO regime is in place?

Glossary

Broadband	A service or connection generally defined as being 'always-on', and providing a bandwidth greater than 128kbit/s.
Communications Act	Communications Act 2003 which came into force in July 2003
CPS	Carrier Pre-Selection. The facility offered to customers which allows them to opt for certain defined classes of call to be carried by an operator selected in advance (and having a contract with the customer) without having to dial a routing prefix, use a dialler box, or follow any other different procedure to invoke such routing.
DSL	Digital Subscriber Line. A family of technologies generally referred to as DSL or xDSL, capable of transforming ordinary phone lines into high-speed digital lines, capable of supporting advanced services such as fast internet access and video-on-demand. ADSL, HDSL (High data rate Digital Subscriber Line) and VDSL (Very high data rate Digital Subscriber Line) are variants of xDSL.
IA	Indirect Access. The facility offered to customers which allows them to opt to route their calls over alternative providers' networks. With IA you must dial a short code (or sometimes a freephone or other phone number) before you dial the number you want. Or, you can have an adaptor plugged in between the socket and your phone and the adaptor will dial the code for you, from calls from that socket.
In Contact (IC)	A BT special tariff scheme where the customer pays the rental charge by post-pay and calls by pre-pay. Also known as In Contact Plus.
Internet	A global network of networks, using a common set of standards (e.g. the Internet Protocol), accessed by users with a computer via a service provider.
IP	Internet Protocol. The packet data protocol used for routing and carriage of messages across the internet and similar networks.
Light User Scheme (LUS)	BT's special tariff scheme launched in 1993. Normal rental charge applies, but users receive a rebate if call charges are less than £15.07 per quarter.
Narrowband	A service or connection providing data speeds up to 128kbit/s, such as via an analogue telephone line, or via ISDN.
Ofcom	Office of Communications. The regulator for the communications industries, created by the Communications Act.
Oftel	Office of Telecommunications, whose functions transferred to Ofcom on 29 December 2003.
Payphone Access Charge (PAC)	An additional charge paid by freephone and indirect access operators to PCB and managed payphone operators to cover the cost of providing and maintaining those payphones and for the use of the exchange line (the cost of which is normally covered by line rental).
Pre-pay services	Method for paying for telecoms services where the customer pays for the calls before making them by adding money to an

	account or to a payment card.
Post-pay services	Method for paying for telecoms services where the customer is billed (quarterly or monthly) for the calls after they were made. This is the most common method of paying for fixed telecoms services.
RNID	The Royal National Institute for Deaf People.
Textphone	A device used by hearing and speech impaired people to communicate over networks in typed text rather than speech (the device is needed at both ends of the call, or a text relay service is needed).
Text relay service	A service enabling textphone users to communicate via the network with other customers by means of an on-line translation service.
USD	Universal Service Directive. Directive 2002/22/EC of the European Parliament and of the Council of 7 March 2002 on universal service and users' rights relating to electronic communications networks and services.