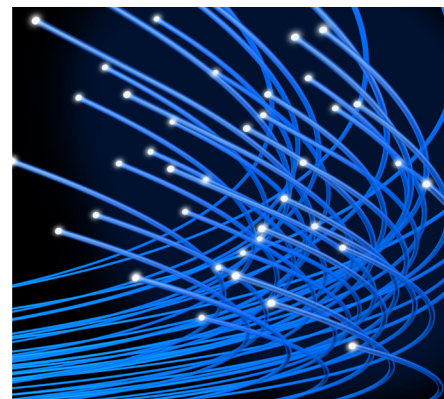
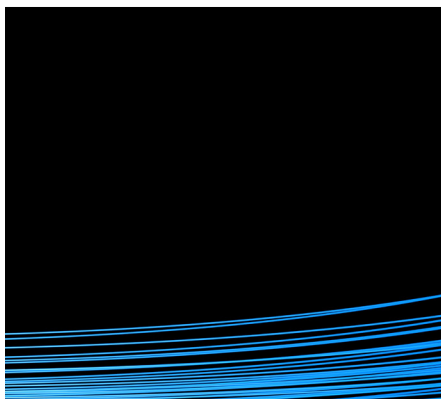
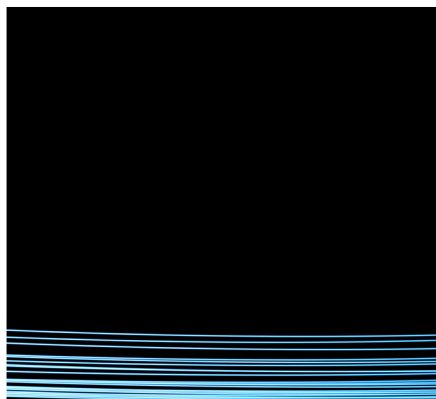


Legal separation of BT Openreach

Significant reforms announced by Ofcom



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On 10 March 2017, the UK telecoms regulator, Ofcom, announced significant reforms to how BT's network arm, Openreach, will be governed.

Ofcom has stated that these changes represent the "biggest reform of Openreach in its history" and it seems certain that they will have a material effect on UK telecommunications markets. However, a number of important issues are yet to be fully worked out and, as such, the full impact of these new arrangements may take time to fully emerge.

Background

Serious movement towards these recently announced changes began in February last year when Ofcom published its Digital Communications Review (the **DCR**). The DCR identified strengthening Openreach's independence as a key priority in terms of reform of telecommunications markets. This was substantially due to concerns that BT still had the incentive and ability to favour its own retail business when making strategic decisions about new network investments by Openreach and that this was damaging competition. Ofcom concluded, in particular, that taking steps to fix these perceived problems with competition created by Openreach's relationship to BT would improve the quality of service experienced by BT's competitors and in turn improve the experience of UK consumers.

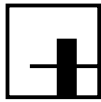
This led to Ofcom notifying the European Commission of its intention to impose further business separation measures on BT. However, negotiations between BT and Ofcom led to a consensus being arrived at and BT voluntarily agreeing to further business separation

measures and, in particular, to establishing Openreach as an independently operated business entity.

Overview

Ofcom and BT have published a [number of documents](#) which explain the new framework that BT and Openreach Limited will operate in. The key substantive documents are a set of Commitments made by BT plc and the new Openreach Limited to Ofcom (the **Commitments**) and a Governance Protocol which provides further details on how Openreach Limited will be governed going forward (the **Governance Protocol**). Please see 'Key changes' below for an outline of the main provisions contained in the Commitments and the Governance Protocol.

Broadly, the changes aim to provide Openreach Limited with (in Ofcom's words) *"the greatest degree of independence from BT Group possible without incurring the delays and disruption – to industry, consumers and investment plans – associated with structural separation or the sell-off of Openreach to new shareholders"*.



The Commitments and Governance Protocol seek to achieve this aim through implementing a number of business separation measures, which in effect seek to set the Openreach Limited up as a business with a material degree of independence from the wider BT Group.

Key changes

The following changes have the potential to be particularly impactful:

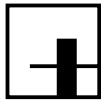
- **Legal separation of Openreach** Openreach Limited will be incorporated as a legally separate company within BT Group. The separately incorporated Openreach will have its own Articles of Association, which will include separate corporate governance arrangements as well as a specific obligation on the Openreach Limited board to treat all customers equally.
- **Corporate governance changes** The Openreach board (which has already been established in anticipation of these changes) has a majority of directors independent of BT. This board will become the board of Openreach Limited. It will be responsible for running the Openreach business, in line with the Governance Protocol.
- **Strategy and budget** In particular, Openreach will be required to develop its own strategy and annual operating plans. However, Openreach's overall budget will continue to be set by BT Group and the BT plc board will continue to have a role in approving Openreach plans.
- **A new relationship with BT plc** Also, the new Openreach's Chief Executive will be appointed by, and accountable to, the Openreach Limited board. BT Group will still have the power to veto such an appointment, but only on notification to Ofcom. In turn, the Openreach Chief Executive will be responsible for other Openreach executive appointments, and will report to the Openreach Chair. There will, however, be secondary accountability to the Chief Executive of BT plc, limited to necessary legal, fiduciary or regulatory obligations.
- **Staff transfer** The circa. 32,000 BT plc staff who currently work in the Openreach business will be transferred across to the new Openreach. Ofcom considers that this will assist with Openreach developing its own distinct organisational culture. The Government has also agreed to take action to protect the pensions of Openreach staff who are members of the BT pension scheme; to do so it

will need to amend legislation to ensure that the Crown Guarantee (a Government guarantee which ensures the solvency of the BT pension scheme) is maintained for Openreach Limited staff. This is likely to be done through an amendment to the Digital Economy Bill.

- **Assets and Trading** Openreach Limited will have control of the assets (such as the physical access network) required to run Openreach's telecommunications network and meet its objectives. The Openreach board will make decisions on building and maintaining these assets. BT plc will transfer these asset management powers to Openreach Limited, while retaining ownership of the assets themselves. Similarly, the new Openreach Limited will manage all supplier and customer relations relevant to the Openreach business, as BT plc's agent. Overall, BT plc will retain all economic benefits and risks associated with the assets and trading managed and operated by Openreach Limited.
- **Branding** Openreach will be prohibited from referring to 'BT' or 'British Telecommunications' in its branding. This requirement is to reflect the more independent relationship these changes seek to create.
- **Other business separation requirements** The Commitments and the Governance Protocol also include other operational business separation requirements. For example, maintaining separate headquarters for Openreach Limited, maintaining (to an extent) separate IT systems and a number of requirements around minimising information sharing between Openreach Limited and the wider BT business.
- **Consultation with other market players** Openreach will also be required to formally consult with other market players such as Sky, TalkTalk and Vodafone on significant network investments. In particular, going forward there will be a 'confidential' phase of such consultations – allowing other carriers to freely discuss ideas and requirements with Openreach without their information being shared with the wider BT business. As noted above, the new arrangements also contain wider protections for confidential Openreach customer information.

Timeline

Detailed arrangements between BT and Openreach in respect of how the Openreach will manage BT's assets and act as its agent in respect of trading are still to be confirmed. Moreover, Ofcom are still to confirm their



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proposals on releasing BT from its previous undertakings on Openreach (to the extent that the new arrangements make these redundant) and, also, how it intends to monitor and enforce the new arrangements.

It is expected, however, that these matters will be dealt with this year and that the new arrangements will fully come into force then.

Get in touch

Shepherd and Wedderburn have a team of vastly experienced regulatory and competition specialists in the telecommunications, media and technology (TMT)

sector. Members of our team have worked in private practice and in telecommunications carriers across the globe. We are able to advise clients on all aspects of TMT regulatory and competition issues; in particular, we have experience of advising on business separation issues in telecommunications (and other utilities) markets in various jurisdictions internationally.

Please get in touch if this briefing has been of interest. Also, please look out for a further, in-depth, analysis of the BT/Openreach business separation that we will be publishing on shepwedd.com/knowledge soon.

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