



## Audit Committee Report

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**Report of:** Chief Executive

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**Date:** 26 September 2012

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**Subject:** South Yorkshire Digital Region Project

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**Author of Report:** Edward Highfield 0114 223 2349

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**Summary:**

This report updates Audit Committee on the latest progress of the Digital Region Broadband project, of which Sheffield City Council is a shareholder and customer.

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**Recommendations:**

Audit Committee is recommended to note the steps being taken

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**Background Papers:** None

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**Category of Report:** OPEN

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\* Delete as appropriate

## Statutory and Council Policy Checklist

<b>Financial Implications</b>
YES Cleared by: E Walker
<b>Legal Implications</b>
NO – not of this specific report
<b>Equality of Opportunity Implications</b>
No
<b>Tackling Health Inequalities Implications</b>
NO
<b>Human rights Implications</b>
NO:
<b>Environmental and Sustainability implications</b>
NO
<b>Economic impact</b>
YES
<b>Community safety implications</b>
NO
<b>Human resources implications</b>
NO
<b>Property implications</b>
NO
<b>Area(s) affected</b>
All
<b>Relevant Cabinet Portfolio Leader</b>
Cabinet Member for Finance
<b>Relevant Scrutiny Committee if decision called in</b>
Not applicable
<b>Is the item a matter which is reserved for approval by the City Council?</b>
NO
<b>Press release</b>
NO

## **South Yorkshire Digital Region Broadband Project**

### **1.0 INTRODUCTION**

- 1.1 Audit Committee receive brief updates on Digital Region via the monitoring of key external relationships. At its meeting in August, Audit Committee requested a more detailed report.

### **2.0 BACKGROUND**

- 2.1 Digital Region Limited (DRL) is a company set up to provide high speed broadband access across South Yorkshire. It was initially jointly owned by the four South Yorkshire local authorities and Yorkshire Forward, but with effect from 30<sup>th</sup> March 2012 Yorkshire Forward's rights and obligations in relation to DRL have transferred to the Department for Business, Innovation and Skills (BIS).
- 2.2 Digital Region aims to be a groundbreaking transformational project that will deliver step change in the economic performance of South Yorkshire. Unfortunately history will judge that the original business plan was based on technological and trading assumptions that have been overtaken by events and DRL now cannot continue to trade based upon current operating models. The critical issues are that the market is increasingly competitive and dominated by a few key players, the economic outlook has fundamentally changed, the model for national public support to roll out broadband has changed and technological innovations have changed the way internet is delivered to the consumer.
- 2.3 The government's approach to super fast broadband roll out is now fundamentally different to the way Digital Region has been established. Although both models are supported by significant levels of European and government funding the sharing of risk and involvement of the private sector is in direct contrast. The risks are largely borne by the private sector using their existing networks and customer base. Local authorities and Department for Culture Media and Sport (DCMS) co-finance an extension of the broadband network to ensure coverage of 90% where there is no commercial case for doing so.
- 2.4 The Digital Region project is now at a critical stage. Its main contractor has largely completed the network to time and cost. A new Chief Operating Officer is in post and changes have occurred within the DRL Board. The management team and staff are focussed on a solution and the pressure of the trading position has acted as a real catalyst across Government and shareholders to explore a range of options for the way forward. There is a strong commitment across central and local government to seek a viable solution and ensure Digital Region delivers outcomes for South Yorkshire.

- 2.5 The original Business Plan has been superseded. Operating costs are too high compared to the revenue model that does not reflect the reality of current market conditions. This is clearly not sustainable with insufficient prospect of increasing revenues to the levels required in the short term.
- 2.6 The financial position of DRL is therefore paramount. Each of the four local authorities has agreed to provide further funding to enable the company to operate in order to allow time for further exploration of the operating model.

### **Alternative Options**

#### **2.7 Closure of Digital Region**

There is a major strategic pressure to ensure delivery of 90% superfast broadband coverage nationwide. DCMS's programme to deliver this is an important part of the Government's National Infrastructure Plan. If Digital Region closed local authorities in South Yorkshire would come under pressure from government, businesses and residents to start a replacement project.

- 2.8 The costs of closure are significant. Direct termination costs would be very significant indeed. These costs include the potential repayment of European Funding, the writing-off of loans and the costs of a replacement project to achieve government targets.
- 2.9 The impact of project failure on the region in terms of reputation should not be underestimated, but most important is the delay in achieving the economic growth in South Yorkshire that was the basis for the original Digital Region concept.

#### **2.10 New business model**

A wide range of proposals have been explored in detail. These include social housing pilots designed to connect the unconnected, an unsuccessful bid for 'Super-connected cities' funding, re-engineering local authority services for digital delivery and extending shared ICT services across South Yorkshire. Many of these look exciting in terms of longer term benefits to the region and Government is keen to explore them further. However they do not sufficiently impact on the viability of DRL in the short term to mean they are potential solutions to our current problems. This is an issue of timing and scale.

- 2.11 In order to secure a future for Digital Region the only option is to develop a new model in collaboration with a major telecommunications company and to procure a new supplier who will maintain the network with responsibility for operating costs, sales, marketing and revenues. In

effect the supplier would run the business with financial risks significantly reduced for shareholders and operational risk – including revenue risk - transferring to the private sector in line with the government favoured model.

- 2.12 European State Aid and procurement rules require that this must be by open competition and hence a re-procurement exercise is currently underway. Two significant telecoms businesses are currently in negotiation with DRL via the Competitive Dialogue procurement process.
- 2.13 Specific details of the re-procurement are confidential and it is too early to predict what the outcome might be. Full details of the recommended way forward are expected by the end of 2012.

### **3.0 Financial Implications**

- 3.1 The Council made provisions to allow DRL to continue trading as part of its 2012/13 budget decisions. This has in effect bought time to see whether the re-procurement will be successful and the network has got a viable future.
- 3.2 The full financial implications of the recommended way forward will not be known until the outcome of the current procurement exercise. In financial terms, the two bidders' proposals are being scored against a third option, which is the costs of closing the network altogether.

### **4.0 RECOMMENDATIONS**

- 4.1 Audit Committee is recommended to note the steps being taken

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