COMMENTS ON DRAFT 11TH EDITION
OF ICSTIS CODE OF PRACTICE

This is a response to the consultation document dated 23 September 2005 and the draft 11th Edition of the ICSTIS Code of Practice ("the Code"), set out at Appendix A of the consultation document.

This response should be read in conjunction with the response provided by Juliette Levy of Selborne Chambers which addresses specific legal and regulatory issues and in particular the provisions of sections 8 to 10 of the draft 11th Code concerning procedures, sanctions and appeals.

Summary

(1) Some provisions of the draft 11th Code go beyond the requirements of the recommendations made in the Ofcom review published on 9 December 2004 ("the Recommendations") and/or could be construed or applied in a manner which is not intended by the Recommendations.

(2) Subject to (1) above, whilst the new and amended provisions helpfully address some of the difficulties faced by ICSTIS in the recent past in respect of scams and/or aggravating elements of legitimate services, they fail to fully address the difficulties faced by the industry and those entities subject to regulation by ICSTIS. In other words, the proposed changes specifically address the problems the regulator has faced in applying the Code, but not the problems the industry has faced in the application of the Code to their businesses and the PRS market in general and is very one-sided. The regulation of the industry is a two–way process and this has yet to be fully taken on board.

(3) The draft 11th Code contains elements which directly contradict the principles of de-regulation and open competition which underpin the European Directives and the Communications Act.

(4) The changes to the definitions of network operator ("NO") and service provider ("SP") are unnecessary, contrary to legislative requirements and create a false and distorted approach to regulation. They are also counterproductive in that numerous companies which fall within the old definition of NO will now be treated as SPs and consequently will be outside the scope of the new obligations on NOs and the referral procedure to Ofcom. Further, the changes are contrary to the principle of "targeting" and they completely fail to address the wide range of roles played by the various entities in the PRS market. Unfortunately this protracted issue is left unaddressed and has been swept under the carpet in the draft 11th Code.

(5) Read in its entirety, the new Code places an unnecessarily heavy burden on the industry in an attempt to address the unacceptable activities of a minority. This could prove to be particularly onerous on smaller entities which may find they do not have the resources or ability to continue to compete in this marketplace. As a result, the Code could be construed as stifling competition as well as failing to observe the principle of 'targeting'.

As a result of the above, whilst the draft 11th Code is a step in the right direction, it requires some re-working prior to its adoption.

In light of the fact that the changes will have a significant impact on the PRS market, sufficient time must been given under Article 6 of the Framework Directive to consider this and any other responses submitted.

Introduction

The consultation document helpfully provides guidance to those who wish to have input in the consultation and highlights the amendments it considers are the most significant. Importantly, it invites comments on the "scope and application of ICSTIS regulation" and "the appropriateness of regulation for new and developing forms of content, mobile and otherwise".

It is useful to briefly consider this question of scope at the outset of this response given that it underpins the entire Code and the manner in which the amendments are perceived.

In particular, the following issues are key factors to any consideration of the scope and application of ICSTIS regulation:

- The confidence and trust of the industry needs to be earned. There must be fairness of treatment and observance of rights of the entities regulated by the Code, as well the principle aim of preserving the interests of consumers.

- There must be true impartiality and independence in the application of the provisions of the Code and the role of Director must be defined. In particular, the Director should not get involved in individual cases or endeavour to influence the decisions of the Committee, the Oral Hearing panel and/or Ofcom.

- Use of the informal procedure and the ability to take the route of least resistance where appropriate are essential objectives which have yet to be achieved.

- ICSTIS must have confidence in the application and interpretation of the various provisions of Code in line with its aims and objectives and the ability to be flexible in light of new technologies/services rather than following letter of the Code in every case.

- ICSTIS must have confidence in its decisions and the ability to set precedents / issue constructive guidance / copy advice and should adopt an analogous approach to the ASA / Ofcom in its treatment of stakeholders.

It has long been established that a heavy-handed and draconian style of regulation is ineffective. The adoption of the principles of the Better Regulation Task Force is therefore warmly welcomed.

Whilst in theory the 'goal based approach' referred to in the consultation document is useful, this has previously resulted in the complete prohibition of various types of promotion rather than targeted action against illegitimate providers. Accordingly,

when considering the scope and application of ICSTIS regulation this, together with the factors outlined above, must be taken into consideration.

SECTION ONE
Definitions

The amended definition of "network operator" serves to introduce a new elite class of network operators by limiting the application of the definition to major network operators (40 million+ turnover only) with the result that all other network operators will fall within the definition of "service provider". The draft 11th Code then imposes new obligations on network operators which largely mirror the obligations of service providers.

The consultation document rightly states that "The role of the NO is fundamental to premium rate services regulation" because, inter alia, premium rate services are dependent on NOs for connectivity. It therefore seems illogical to limit the application of this definition (and the obligations and responsibilities which flow from it) in the manner proposed. Any such limitation would also serve to exacerbate the remoteness between the regulator and the actual provider of the PRS.

The consultation document reasons that, "Increasingly, ICSTIS has been faced with companies claiming that they are NOs with little by way of evidence of 'physical' ability to show in what capacity they act in the premium rate value chain." This statement does not, however, support the 'turnover test' introduced under the amended definition. NOs operate switched telecommunications networks; they have connectivity agreements with other NOs and are subject to general (and possibly special) conditions issued by Ofcom. They do not necessarily turnover 40 million+ a year.

Further, whilst this reasoning may be a relevant consideration under the existing Code, it seems otiose under the draft 11th Code which proposes enhanced regulation of NOs. In other words, the attractions of the less onerous role of "NO" under the old Code will no longer apply. In fact, the amendment does little to prevent "real SPs" from avoiding their obligations but rather serves to wrongly categorise NOs as SPs when they are not true provider of the service in question.

The proposed limitation is somewhat inconsistent with the spirit and letter of the new European regulatory framework which expressly rescinded the licence regime and created a new regime based on special and general conditions with a view to opening up the marketplace and promoting competition.

Although under the new regime major networks are subject to enhanced regulation (for obvious and legitimate reasons), there is no logical or convincing reason for dividing network operators into two categories with a view to treating them separately under the Code. Such a practice could be construed as anti-competitive and discriminatory and in any event is unnecessary for the reasons outlined in this response.

The consultation document rightly states that, "Regulated parties in any sector need to be provided with certainty from the regulator as to their status and responsibilities." This requirement does not, however, support the proposed amendment. Certainty can be achieved without recourse to potentially unfair, anti-competitive and discriminatory practices, as outlined in this response.

A more helpful alternative would be to introduce criteria which are based on true indicators of an entity's role such as:
- does it have interconnect agreements with other NOs and in particular with BT;
- does it operate a switched telecommunications network;
- is it a terminating network operator in that call traffic terminates on its switch;
- is it the legitimate holder of premium rate numbers, as allocated by Ofcom?

In specific response to the Questions raised in the consultation document on this issue:

Section 1 Question 1: The test discriminates against smaller companies by presuming that they will not have the ability to comply with their obligations as a network operator when this may not be the case.

Section 1 Question 2: This does not seem an appropriate or necessary requirement. NOs are by their very nature subject to interconnect agreements which contain such provisions. Further, this is outside the scope of ICSTIS.

Section 1 Question 3: See above.

Section 1 Question 4: The changes to the definitions do not really address ease of identification but simply determine objectively and strictly the role of a particular entity without reference to its actual role. An entity should be categorised by its true role and not by its turnover.

The consultation document states that ICSTIS will 'put the appropriate accountability on all parties for their action' (on paragraph one of page 5) but fails to reflect this in the definitions. In particular, the definition of "Service Provider" fails to address the varying roles within the industry and is inconsistent with the principle of 'targeting'.

Scope of the Code

The consultation document refers to the 'principle of universality' as a necessity, relying on principles of 'proportionality' and 'targeting' as safeguards for lower-risk services and entities. This model is highly dependent on the regulator obtaining the trust and confidence of stakeholders (as achieved by the FSA), but ICSTIS has a long way to go to achieve this goal.

Unfortunately, the aim of ensuring that regulation is proportionate to the extent of the risk of consumer harm is not achieved on the existing balance and application of PRS regulations. This will need to be firmly addressed under the new 11th Edition of the Code given the new and extensive requirements proposed.

Section 1: Question 7: Unfortunately existing PRS regulations are not applied proportionately, "with more intrusive measures sufficiently focused on higher risk activities or providers". This is predominantly due to the fact that ICSTIS fails to adequately enquire into the culpability of the relevant SP/individual prior to exercising the more intrusive measures and/or imposing more onerous and

potentially crippling sanctions. In particular, ICSTIS does not observe the right to an Oral Hearing and/or to apply for a suspension of a sanction prior to adopting such practices. Further it fails to take account of true role of the entity in question which can and has resulted in highly disproportionate treatment. This will only be exacerbated by the new categorisation of NOs and SPs.

SECTION 2

Administrative Provisions (Network Operators)

Paragraph 2.1.2.a

Draft paragraph 2.1.2a requires the new elite class of network operators to provide evidence of their status, including evidence that they satisfy the 'turnover test'.

This new 'evidence test' acts to prevent bogus network operators from wrongly claiming to be NOs. The criteria, however, need NOT include their turnover but rather some more suitable objective test which does not exclude smaller operators (thereby avoiding the need to falsely identify them as SPs and observing the principle of targeting).

A more appropriate means of measuring the true role of an entity was considered above. This more appropriate test can work together with the evidence test to ensure that all NOs of whatever size refrain from providing premium rate services until they have demonstrated that they satisfy the relevant criteria. In other words, a more suitable objective NO test (together with the evidence test) will serve to ensure that ICSTIS' concerns regarding identification and communication are satisfied.

Paragraph 2.1.2b

All that is needed here is to reflect the obligations placed on solicitors and other sectors to satisfy certain identification requirements under money laundering regulations. The wording, 'such information as ICSTIS may require…' wrongly and unnecessarily introduces a subjective element to the obligation.

The right that should be reserved by ICSTIS is to prevent the operation of a premium rate service until the (objective) identification requirements are met rather

than allowing entities to supply evidence 'promptly following' the commencement of PRS services. Further, the Code currently fails to address the precise procedure concerning identification.

Paragraph 2.1.4

It may not be possible for NOs to 'adhere to' a time period specified by ICSTIS for legitimate reasons. What happens then?

Data protection

Paragraph 2.2.2 may cause practical difficulties for NOs insofar as it applies to 'others' given the sheer volume of contacts that major network operators have.

Arrangements with service providers

Given that this section applies only to terminating network operators, namely "those who contract directly with the SP" (TNOs), and only then to TNOs with a turnover exceeding 40 millon, it seems that these provisions will only apply to a small category of network operators.

Consequently, notwithstanding that they are the relevant terminating operator and holder of the relevant 090 numbers and that the relevant call traffic terminates at their switch/ they have a contract with the relevant SP, many TNOs will not be required to comply with this section. Instead they will be construed as SPs themselves and therefore will only have to supply information concerning their own entity/activities and not those of the true SP.

In particular, they will not be bound by the 30 day rule at paragraph 2.3.2b which obligation will presumably fall on the relevant transit operator (normally BT), nor the provisions concerning number exportation. In addition, they will not be bound by paragraph 2.5 (provision of information pursuant to a complaint/investigation; termination of numbers/services and withholding of revenues).

This does not appear to coincide with the intention of Recommendation 4 and rather confuses matters as opposed to easing the identification burden. Significantly, the

transit operator may be required to retain and potentially handover to ICSTIS large sums of monies (although it is not clear if transit operators fall within this section). In all likelihood any such requirement will involve significant future dealings between BT and ICSTIS, which would not seem appropriate given BT's market position, particularly in light of the quasi-regulatory role BT has already adopted in the PRS market. In addition, a significant burden may be placed on transit operators to comply with provisions of this section (eg paying shortfalls in fines and receiving sanctions for non-compliance) which is probably not the intention. Further, the true TNO is the entity which is best placed to ensure the termination of its numbers and not an operator which is further up the chain.

In any event, this section goes beyond the requirements of the Recommendations. In particular, the following provisions are problematic:

Paragraph 2.3.1b goes beyond that which can reasonably be expected of an NO. To promote regulatory compliance through carrying out due diligence on SPs is sensible. However, the requirement to "obtain satisfactory evidence that the service provider is solvent and has sufficient resources to discharge its obligations under this Code" should not be the responsibility of the NO beyond posing the relevant question to the SP and supplying the response to ICSTIS. In any event, what would "satisfactory evidence" or "sufficient resources" be?

Paragraph 2.3.1g requires the NO to satisfy itself that its network is not being used for services "not compliant with this Code". This provision has been drafted too widely and as such will be difficult for the NO to comply with, given the sheer volume and detail of the provisions under the new Code.

Paragraph 2.3.3 (30 day rule): In principle, the new thirty day rule has largely been viewed as a positive step by the industry and has already been incorporated into the 10th Edition of the Code. There remain, however, concerns about the manner in which this provision will be relied upon by ICSTIS to direct the retention of funds for periods far in excess of 30 days. In one case a direction by ICSTIS to a network operator to retain monies from a company which had been the subject of an investigation and subsequent adjudication lasted some 12 months, notwithstanding that the company had paid the fine and associated administrative charge some 10

months earlier. Eventually, following considerable debate and costs, ICSTIS directed that the balance of monies held by the NO be released.

In addition:

- There should be a provision to enable NOs to seek relief from this requirement if the circumstances justify it;
- The ability to direct the retention of monies beyond 30 days should only apply if the emergency procedure applies;
- There needs to be an additional layer or access to the IAB where retention decisions can be reviewed quickly and fairly;
- There is no provision for payment of interest and prima facie no other method of recovering interest on monies retained. This is particularly onerous if monies are retained for considerable periods.

Paragraph 2.5.1e provides that bank details must be provided on the direction of ICSTIS. There is no justification for disclosure of such confidential information and this requirement goes far beyond that which is reasonable or necessary.

Unless clear reasons are given for requiring bank details, together with carefully drafted provisions regarding the manner in which this information will be used by ICSTIS and any applicable restrictions, this requirement should be deleted. Any legitimate reasons for requiring such information should be passed to an appropriate enforcement authority with clear powers and guidelines regulating its activities in this regard.

Paragraph 2.5.2f should state 'from retained funds' for clarification.

Paragraph 2.5.3 has been drafted far too widely, is unworkable and unreasonable, particularly the wording "must not enter into or continue arrangements with anyone who …is likely to cause non-compliance with or frustration of any sanction…" This provision should be reconsidered and re-drafted and should at least be without prejudice to any Oral Hearings/ Appeals of the sanctions in question to cover the scenario where adjudications are disputed.

Paragraph 2.5.4 (regarding an NO's failure to withhold sums on the direction of ICSTIS) needs clarifying to ensure that only sums which NOs 'could' have withheld are payable. In other words, the NO may not have received (and paid to the SP) sums of the level of the fines imposed. Presumably this provision is not intended to apply to any shortfalls.

Paragraph 2.6 fails to take account of the culpability of the NO. That is to say, whether the NO made a mistake, was negligent or reckless or acted in wilful disregard of the Code.

Further, the paragraph is drafted so as to apply to breaches of "any" of its obligations by an NO, giving rise to the potential for ICSTIS to instruct a major network to cease to supply an entire category/type of PRS for minor breaches.

Previously, ICSTIS has been responsible for barring an entity from running <u>all</u> premium rate services even though it was not the true SP but was acting as a reseller, as a result of which it was put out of business notwithstanding that it had notified ICSTIS of its role, had complied with ICSTIS' directions and had applied for an Oral Hearing.

In light of the above, the proposed "Statement to show how the sanctions will be determined" requires careful consideration. In particular, it will need to ensure that, inter alia:

- the culpability of the NO is taken into account
- sanctions b,c and d do not apply to minor contraventions
- sanction c is applied carefully and proportionately and in recognition of the potential consequences the sanction

SECTION 3
Administrative Provisions (Service Providers)

<u>Help Notes</u>

The introduction of Help Notes is a welcomed development. This should greatly assist the industry in interpreting the Code/ICSTIS' requirements with confidence. (Previously, there has been a lack of certainty / inability to rely on previous decisions / inability to request meaningful assistance/ input from ICSTIS prior to the launch of a service.)

Help Notes should be backed up with informal meetings with stakeholders / constructive feedback on draft promotions etc.

Paragraph 3.1.1

This provision should be carefully considered in light of the fact that this now covers a much wider definition of SPs. Many NOs will have direct responsibility for complying with this obligation even though they are not the true SP. This is far too onerous and goes beyond the intended objectives of the amendments and the Recommendations.

Section 3 Question 5

A Specific Help Note relating to customer service arrangements would be helpful.

SECTION 5

General Provisions Applicable to all Premium Rate Services (Service Providers)

The minor amendments made to these provisions appear sensible and together with the proposed Help Notes should assist stakeholders in achieving compliance.

It is useful, however, to briefly consider paragraph 5.10 of the draft 11th Code (which largely mirrors paragraph 4.9 of the 10th Edition) which requires further clarification, notwithstanding the proposed amendment. In the past this provision has been widely interpreted and inappropriately used by ICSTIS to plug gaps and address deficiencies in other paragraphs of the Code. Whilst the amendment to this provision is helpful, the second sentence should clearly be linked to the test outlined in the first.

SECTION 6

Live Services

The proposal to remove some types of live services from the requirement to obtain prior permission seems very sensible. ICSTIS prefers the third of the three options it identifies in the consultation document as possible means of addressing this proposal and this does appear to be the most practical and workable solution.

In addition to identifying specific categories which do not require prior approval, it would be advisable for ICSTIS to reserve the right to waive the prior permission requirement where, in its reasonable opinion, it considers it appropriate. In other words, there should be some sort of mechanism for making specific exceptions where appropriate in addition to the mechanism for adding to the published list of exceptions. This is because the definition of 'Live Services' is potentially very wide and could be construed as applying to services which it is not intended to cover or 'one-off' services which are of low-risk to consumers. This includes new and innovative services which may need to be transposed into the existing wording of Code but the appropriate treatment of which cannot yet be envisaged.

Victoria Russell
Hextalls LLP
28 Leman Street
London E1 8ER

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