

## **Business Plan & Budget 2016/17**

### **A PUBLIC CONSULTATION**

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# 1. Executive Summary

- 5% real-term reduction in budget
- Fines and admin charges expected to be significantly lower
- Market size predicted to be 4% lower
- Adjusted levy 0.74%
- Variation to current levy model proposed
- Longer-term commitment to comprehensive funding review

- 1.1. The full-cost operating budget for PhonepayPlus is subject to approval by Ofcom, who have to be satisfied, following consultation, that we have the capacity and capabilities to meet its statutory obligations and are sufficiently resourced to do so. The agreed budget for 2015/16 was £4,444k.
- 1.2. PhonepayPlus continues to deliver its Strategic Plan 2014-17. We are on-track to meet the key business plan commitments made for 2015/16, and on-budget in doing so.
- 1.3. The business plan for 2016/17 is presented as an enhancement to the progress being made in 2015/16 – in particular around the new, holistic approach to regulation, with a balanced emphasis on prevention of future harm to consumers alongside seeking to hold to account those responsible for consumer harm and bringing the market into disrepute.
- 1.4. The full-cost operating budget for 2016/17 for which we will be seeking Ofcom approval is £4,269k. This represents a saving of 5% in real terms.
- 1.5. However, the two factors that have the biggest impact on the adjusted levy are the level of fines and admin charges collected during the current year and the size of the PRS market:
  - Collected fines and admin charges are expected to be significantly lower in 2015/16, with £800k forecast as available retained funds to adjust the levy (compared with £1,471k the previous year);
  - We currently estimate market size for 2016/17 (as measured by total outpayments from network providers) to be £430.5m. This is a 4% reduction from our current forecast for 2015/16.

Based on these two estimates, the adjusted levy will rise to 0.74% (from 0.6% in 2015/16).

- 1.6. We plan to undertake a comprehensive review of the levy funding model in collaboration with industry stakeholders, to take effect from 2017/18 at the earliest, if changes to the Code are required.
- 1.7. To address the instability built into the current model we are proposing a variation to the adjusted levy model:
  - PhonepayPlus' budget would be recovered initially through an unadjusted levy of 0.93% (same rate as 2015/16);
  - Fines and admin charges collected during the year would be redistributed directly back to network operators.

If agreed, this can be applied in 2016/17 without requiring a change of Code.

- 1.8. Registration Scheme fees are proposed to remain unchanged at £155 + VAT, with exemptions remaining the same.

## 2. About PhonepayPlus

2.1. We are the UK's independent regulator of premium rate services, and our **vision** is that anyone can use premium rate services (PRS) with absolute confidence in a healthy and innovative market.

As the telecoms, internet and payments sectors continue to experience an unprecedented rate of change and innovation, we take positive action to safeguard consumers and help cutting-edge providers of digital content and services to thrive. Within our remit and expertise, we seek a more consistent approach to regulating micropayments that are like PRS.

2.2. Our **mission** is to achieve our vision and be a world-class regulator by:

- Putting the consumer at the heart of everything we do through providing effective regulation, information and assistance;
- Understanding the market in which we operate and how it is evolving, so that we can take early, proportionate and targeted action where needed to prevent consumer harm;
- Working with providers to build a healthy market with high standards of compliance;
- Having a Code of Practice, approved by Ofcom, that is cutting-edge in protecting consumers while also supporting innovation in a fast-changing digital landscape;
- Applying our Code in a way that is impartial, fair, transparent, effective and proportionate;
- Working with Government, other regulators, industry, consumer bodies and international partners on matters within our remit and expertise.

2.3. Our core **values and behaviours** are our drivers to ensuring we adhere to the principles of good regulatory practice:

- *Forward looking* - we understand the market in which we operate and understand how technology, business models and consumer behaviour are changing and may change in future. We seek proactively and collaboratively to build compliance and to work with industry at an early stage to address emerging consumer issues rather than responding to problems after they have emerged;
- *Credible and trusted* - we act in a way that demonstrates that we are independent, impartial, trustworthy, transparent, accessible and consistent in all we do. Consumers can rely on us to deliver effective regulation and industry can rely on us to understand their business, to act proportionately and to explain and consult on what we do;
- *Reasonable and intelligent* - we demonstrate sound judgment and act on the basis of evidence. We are principled and pragmatic towards providers and are aware of the commercial and technical environments under which industry operates;
- *Focused on delivery* - we are effective and accountable. We project manage our work effectively to deliver results. We manage resources efficiently so as to ensure we continue to provide good value for money;
- *Prompt, open and transparent* - we understand that both providers and consumers benefit from prompt action to resolve issues. We are transparent about our processes and the reasoning behind decisions.

### 3. 2015/16 Performance

3.1. As published in our Strategic Plan 2014-17, we have five key objectives that shape our work as a quality regulator and ensure we adhere to high standards however the market fluctuates.

During 2015/16 – either through work already delivered, or in train through to March 2016 – adherence to these strategic objectives is enabling us to pursue our mission with clarity and confidence in a fast-moving market:

- Objective 1: to continue to drive up compliance levels and trust in the market
- Objective 2: to identify and prevent emerging risks to consumers
- Objective 3: to help consumers use premium rate services with confidence
- Objective 4: to ensure that regulatory frameworks keep pace with market changes
- Objective 5: to deliver effective and efficient regulation

3.2. In summary, we are executing the 2015/16 business plan we set out in December 2014. **Headline achievements** include:

- Launch and implementation of Code 13, in time to meet Ofcom's changes to non-geographic call services;
- Review of Part 4 of this Code, leading to extensive consultation on changes to our investigations, adjudication and sanctions procedures;
- Significant development of a collaborative approach to regulation, through increased engagement and partnership with industry stakeholders;
- Increased market insight, through initiatives such as the Annual Market Review, a discussion paper on vulnerable consumers, and commissioned research into consumer interaction with PRS services;
- Enhancement of market intelligence capabilities alongside development of collaborative approaches to sharing information and resolving identified issues;
- Improvements in consumer education, both in terms of using PRS and how to resolve complaints;
- Delivery of an app store pilot, through which major players have been able to identify and agree service amendments to provide high levels of consumer protection;
- Enhancement of leadership, management and staff capabilities through a comprehensive organisational development programme;
- Identification and negotiation of significant operating efficiencies, including relocation to new offices saving £0.5m over 8 years.

3.3. The **range and depth of our regulatory work** in 2015/16 is set out below against each of our strategic objectives:

## Objective 1: to continue to drive up compliance levels and trust in the market

### *Updating our Code of Practice and Guidance to ensure they are effective and future-proof*

During 2015/16 we have continued to devote the appropriate level of resources needed to ensure we maintain and develop our Code of Practice in collaboration with all stakeholders:

- Code 13 came into force on 1 July 2015 to coincide with the implementation of Ofcom's changes to non-geographic call services. At the same time a series of new special conditions were introduced and we published a number of pieces of amended guidance to take account of the new Code provisions. Guidance and special conditions were the subject of full consultation and industry seminars, with industry feedback informing the final versions published;
- We recognised the need to initiate a comprehensive review of Part 4 of the Code, taking in our investigations, adjudication and sanctions procedures. We have conducted informal consultation with industry and Ofcom in advance of publishing a formal consultation document on the new model in November 2015. We will continue to work towards incorporating changes into a new Code 14, for which we need to both obtain Ofcom's approval and meet a requirement to notify the EU. At this stage we expect to implement Code changes later in 2016, ahead of which we will also be publishing a draft of the supporting procedures associated with the new Code provisions;
- In continuing to review and develop our Code guidance to industry, we plan to review all of our published guidance that was not updated at the time of the publication of Code 13 to make sure it remains effective and deals with current market issues. We aim to consult with stakeholders on revised guidance in early 2016.

We have also issued a number of other pieces of information for industry, including:

- A compliance update on the Consumer Contracts (Information, Cancellation and Additional Charges) Regulations 2013;
- An information note on the Alternative Dispute Resolution for Consumer Disputes (Competent Authorities and Information) Regulations 2015;
- An information note on the Consumer Rights Act 2015.

### *Engaging actively, and sharing information with industry and other stakeholders throughout the value chain*

We have aimed to deliver high levels of compliance in partnership with industry, through:

- Working alongside a new chair, developing the Industry Liaison Panel into a more effective forum for engagement and dialogue between industry and PhonepayPlus. In particular we have instituted a Rapid Response Team with terms of reference designed to speedily address issues of concern to both the industry and the regulator;
- Expanding our programme of one-to-one meetings and engagement with industry representative bodies, network operators, service providers (merchants and aggregators), and their compliance companies;
- Embedding our Spring and Autumn Forums (held in April and November 2015 respectively) as a central part of our dialogue with industry, with greater industry participation both as speakers and panellists and from the audience.

### *Making effective and proportionate use of enforcement powers under our Code of Practice*

Increased industry collaboration is enabling us to better develop proportional policy solutions, and we continue to ensure we apply a proportional approach into how we regulate:

- We have strengthened the application of the "polluter pays" principle in Code 13. Working with government we have also clarified our power to impose sanctions of up to £250,000 per breach of the Code;
- We have built checks and balances into our internal systems to ensure a proportional approach is applied when deciding on whether to pursue enforcement or not, and, if so, whether this is informal (Track 1) or formal (Track 2);
- Our review of Part 4 of the Code during 2015/16 is intended to produce provisions that will ensure effective, fair and proportionate use of our enforcement powers.

## Objective 2: to identify and prevent emerging risks to consumers

### *Using research and market intelligence to identify emerging issues in the market*

In collaboration with industry stakeholders, we are developing our collective market insight capabilities through research:

- We have invested in an Annual Market Review to best inform a collective view on the outlook for Premium Rate Services. Our Annual Market Review 2015, published in July 2015, showed that the market continues to be challenging, with most areas of the market continuing a recent trend of decline. There were, however, three service areas - gaming, giving and gambling - that bucked this trend and showed significant growth;
- We plan to commission further work in 2015/16 that builds on the research done for the AMR 2015 to understand better consumer attitudes to PRS. We are currently in the process of commissioning research that will give us further insight into how consumers interact with PRS, particularly PRS discovered and consumed online. This will inform further engagement with industry and the development of best practice guidance.

Alongside this we have continued to develop how we collect, handle and share market intelligence we receive directly:

- We have improved our telephone and online consumer contact processes, enabling better granulation of data;
- We have developed an independent search tool that comprehensively scans the market, and has significantly enhanced our pre-emptive policy making and enforcement work.

In 2015/16 both of these developments have in particular informed our work with industry on competition services and adult services, and enabled us to better support complaint handling by network operators and service providers.

### *Developing our market expertise and partnerships with other regulators, consumer bodies and organisations such as internet security companies*

We recognise the importance to the PRS market of a joined-up and collaborative approach to regulation, and during this year:

- We have supported the Association for Interactive Media & Entertainment's (AIME) development of its Early Warning System as a tool to aid industry compliance;
- Following on from the work of the Rapid Response Team on competition services, we are supporting AIME's engagement with Trading Standards on issues relating to compliance of certain Premium Short Message Services (PSMS) with the Consumer Contracts Regulations;
- We will continue to build partnerships with an extensive range of regulatory and enforcement bodies, including the Financial Conduct Authority, Competition and Markets Authority, Advertising Standards Authority, Payments Systems Regulator, Information Commissioner's Office, Action Fraud, Trading Standards, Telecommunications UK Fraud Forum, Which?, and the Consumer Forum for Communications.

### *In collaboration with phone providers and others, taking early action through enforcement, policy development and other tools to prevent emerging issues from becoming active problems.*

We have been able in 2015/16 to make significant strides in embedding our new, holistic approach to regulation, with a balanced emphasis on prevention of future harm to consumers alongside seeking to hold to account those responsible for consumer harm and bringing the market into disrepute:



- The Rapid Response Team approach, under the auspices of the Industry Liaison Panel, has been agreed, with a set of principles published on the PhonepayPlus website. A Rapid Response Team was convened in June to tackle unusually high complaint volumes arising on competition services. This resulted in the Mobile Network Operators taking action on their Payforit scheme rules, and further industry development of best practice guidance on PSMS payment flows. Current analysis indicates that this work has been a factor in seeing complaint levels to PhonepayPlus start to drop in the third quarter of 2015;
- Alongside this we continue to work both with individual networks and the Mobile Broadband Group to build an understanding of those areas where a greater consistency of approach can be achieved, particularly with regard to the networks' own compliance frameworks for PRS providers;
- Our consultative work with industry on the review of the second phase of guidance to Code 13 aims to provide greater clarity on compliance to providers, which in turn is designed to prevent consumer harm through inadvertent non-compliance with the Code.

### Objective 3: to help consumers use premium rate services with confidence

#### *Helping consumers to obtain redress where they have suffered harm.*

During 2015/16 we have developed a number of ways in which consumer confidence in PRS can be underpinned through improved means of redress:

- We have improved our signposting of consumers to the correct organisation that can resolve their problem in the first instance. This has included the installation of a new interactive voice recording on the PhonepayPlus consumer helpline, and enhancing our website to provide clearer information for consumers, e.g. the Solutions Centre content developed in conjunction with industry;
- We are taking a more targeted approach to our contact with industry, with a specific contact programme designed for those L2 providers responsible for the 30 most complained about services;
- We are working with individual networks (with Ofcom engagement) to identify opportunities for improved consumer complaint resolution;
- We continue to seek increased informal contact with L1 and L2 providers to support the practical application of improved consumer journeys;
- We are starting to explore how best to develop Number Checker into a more consumer friendly Bill Checker, incorporating differences in all network billing systems;
- We are developing plans to work with industry to scope a refreshed "mystery shopping" programme.

#### *Putting in place additional protections for vulnerable consumers, such as children.*

We continue to work with industry to ensure the highest standards of protection are in place for vulnerable PRS consumers:

- Following desk research undertaken at the start of 2015/16, we published in July a discussion paper on consumer vulnerability and PRS. We are subsequently using the paper and industry feedback to build vulnerability into the second phase of guidance to Code 13. As part of that work, we will be holding a workshop in partnership with AIME, to explore how industry can deliver the highest standards of protection while avoiding unintended consequences;
- We will be working with App Stores during their grace period of exemption from price caps on services targeted towards children. Our aim is to ensure that the measures they are putting in place as an alternative to price caps provide sufficient protection to enable the exemption to be made permanent.

#### *In collaboration with partners, providing information and support to consumers about potential risks and how to avoid them.*

We are committed to enhancing consumer education around the use of PRS services, and have undertaken a number of different initiatives in 2015/16:

- The PhonepayPlus website has been overhauled and updated to provide better and clearer information for consumers. We have also increased our use of social media to highlight relevant information from our own work and the work of partners such as Ofcom for consumers – and our monitoring suggests that this is increasing the reach of our consumer information;

- We have targeted consumer information towards younger people using our PhoneBrain website <http://www.phonebrain.org.uk/>. We have also partnered with Childnet International to reach young people by sponsoring a PhoneBrain category in Childnet's existing national film competition. Young people have been able to engage with the issues through participation in the competition, and by viewing the winning entries which are available on our website and those of partners;
- We are currently reviewing the consumer education material available through our website, and plan to enhance this through producing short and punchy videos on specific aspects of PRS;
- We continue to develop our relationships with other regulators and consumer representative bodies in order to increasing the syndication of PhonepayPlus consumer advice through those organisations;
- The research that we are commissioning will provide us greater insight into how consumers interact with PRS. In addition, therefore, to developing best practice guidance with industry, we also hope to use the findings to be able to provide better information for consumers that will help them use PRS with greater confidence and safety.

#### Objective 4: to ensure that regulatory frameworks keep pace with market changes

*Developing our knowledge of how the market in digital content and services is changing and of the implications of this for consumers, providers and regulation.*

With our approach to regulation focussed on outcomes, we have aimed in 2015/16 to balance support for the development of new and innovative business models with high levels of consumer protection:

- The launch and application of Code 13 moves from a regime of prior permissions (which had to be sought before a new service could be launched) to published special conditions, which now allow service providers from the outset to design services in compliance with our Code;
- The completion of our App Stores pilot resulted in one provider introducing a series of amendments and additional protections, leading in turn to a significant reduction in related complaints addressed to PhonepayPlus. With such protection in place, this has allowed us to confirm that the exemptions in the pilot could be made permanently available. We will also be working with App Stores on alternatives to price caps for services targeted towards children, and on assessing the impact of the grace period we granted;
- We conducted analysis on mobile voice shortcodes charged at 20ppm or less, and were able to conclude that this service represented low risk of consumer detriment - leading to our exemption of these services from some requirements of the Code in June 2015;
- We are continuing to work with providers and other regulators - notably the Financial Conduct Authority - to understand new digital payment models, the interaction (or otherwise) of PRS regulation in this area, and the possible impact on consumer behaviour.

*Working with industry, other regulators and government to build a consensus on the best and most effective responses to these changes.*

Our work in this area in 2015/16 covers potentially highly significant legislation for the PRS industry:

- We have worked closely with industry representatives to ensure that the industry position was fully understood by UK government officials negotiating the revision of the EU Payment Services Directive (PSDII);
- We continue to work with industry representatives, HM Treasury and the Financial Conduct Authority as they prepare for the implementation of PSDII in the UK. We expect government to begin consultation in the first half of 2016;
- We are working with Ofcom and Department for Culture, Media and Sport officials to contribute to the development of the UK negotiating position on the review of the EU regulatory framework for electronic communications, with a focus on ensuring that EU legislation provides for strong levels of consumer protection for services provided from within the EU.

## Objective 5: to deliver effective and efficient regulation

*Ensuring that our regulation continues to deliver the outcomes for consumers set out in our Code of Practice.*

The launch and application of Code 13 in 2015/16, with its associated special conditions and guidance, has been designed to further embed our outcomes-based approach to regulation. Within this environment, we have also specifically:

- Responded to the challenge at the start of the year of rising complaint numbers relating to competition services and, to a lesser extent, adult services, through extensive analysis of the complaint drivers and the subsequent targeted Rapid Response Team work described above;
- Worked with Ofcom and the Department for Culture, Media and Sport to ensure that the proposed Investigatory Powers Bill will contain measures that preserve our ability to investigate complaints effectively, and agreed an approach that enables our regulatory effectiveness to be maintained as the Bill progresses through Parliament.

*Ensuring that we use resources efficiently and provide good value for money*

We have continued during 2015/16 to identify and implement opportunities that yield both material financial and operational efficiencies:

- We have enhanced our leadership, management and staff capabilities through significant organisational development, including the appointment of a new Chair and Leadership Team. We plan for our Board refresh at the end of the year to contribute towards the financial control of total people costs in 2016/17, and our imminent internal cultural shift programme is being designed to ensure all of our work and structure is fully aligned with our holistic approach to regulation;
- We have successfully completed our office relocation project, saving £0.5m over 8 years;
- We have undertaken a broad range of systems development work, with expected savings to be generated in the 2016/17 financial year;
- We have ensured the primary focus of our contact centre operation has been to collect and analyse market intelligence arising from complaints, and have carefully managed the capacity we need in line with complaint and enquiry levels. We will continue to explore resourcing options, including outsourcing and other automated processes, that best balances our need for timely access to independent market intelligence with the cost of acquiring it;
- We plan to continue to develop our call centre operations by further reviewing our new interactive voice recording in collaboration with industry expertise, to optimise our contact handling and better direct consumers towards appropriate resolution;
- We reviewed and updated our investigators' time recording systems, to enhance the "polluter pays" principle through the better allocation of costs;
- We are currently reviewing the level of contingency provisions held on the PhonepayPlus balance sheet, so that we accurately reflect the financial impact of major risks and identify those exceptional items that should not be funded to the detriment of our capabilities to regulate as planned.

We also continue to ensure we follow best business practices, even where financial and operational efficiencies may be relatively small. Examples during 2015/16 include putting our legal work out to tender, ensuring our staff handbook is fully up to date with current employment legislation, and reviewing our insurance arrangements to best support our ability to act as an independent regulator.

## 4. 2016/17 Business Plan

4.1. We aim during 2016/17 to continue to build our holistic approach to regulation, while tangibly demonstrating our effectiveness and efficiency.

4.2. The **key business plan activities** through which we will add to the positive developments of 2015/16 include:

- Systematically reviewing our compliance processes (monitoring; informal and formal communication with providers, including guidance provision; benchmarking of compliance; contact handling etc), in order to best manage the balance between a vibrant PRS market for providers and ensuring consumers are properly protected;
- Extending the depth and range of our stakeholder relationships, to include:
  - further enhancement of industry engagement and liaison;
  - increased engagement with other regulatory bodies, to ensure clarity and consistency of regulation in a complex environment;
  - a comprehensive stakeholder satisfaction survey, to ensure we are meeting the standards expected of us;
  - developing our understanding of consumer experiences, through e.g. consumer panels and mystery shopping;
- Developing further our ability to anticipate and understand market changes, including work on horizon scanning, risk management, and how we can best promote a healthy PRS market into the future;
- Continuing to enhance our data capture and reporting systems to ensure that, where economically viable, we meet the information needs of all our stakeholder audiences;
- Contributing to policy development and managing the impact on the PRS market of key legislation, including e.g. EU Payment Services Directive (PSDii), EU regulatory framework for electronic communications, Investigatory Powers Bill;
- Working closely with Ofcom to ensure that, in satisfying their own statutory remit, our budget is both sufficient to deliver effective PRS regulation, while looking to develop further efficiency drivers;
- Constructively engaging with industry to review the current levy-based funding model, and to explore whether there are alternatives that, in theory and in practice, better deliver agreed funding criteria. We would look to implement any change from 2017/18 onwards, subject to any revisions required to our Code of Practice;

4.3. Specifically, we plan to deliver the following **range of activities for 2016/17**, as set out against each of the strategic objectives:

## Objective 1: to continue to drive up compliance levels and trust in the market

### *Updating our Code of Practice and Guidance to ensure they are effective and future-proof*

Work next year on our Code of Practice will include:

- Publishing revised guidance arising from the second phase of the current guidance development project in early 2016/17. We will then subsequently develop a programme of rolling updates, with a commitment to annually review each area of guidance;
- Ensuring the completion of the consultation process on Code 14 with all industry stakeholders, with the aim of securing approval from Ofcom and the EU during the summer. Our target date for launching Code 14 is July 2016, and at the same time we will publish the finalised associated procedures document to accompany the new Code;
- Managing with clarity across the whole of the PRS industry the transformation from the current adjudicatory process to the new process currently under consultation;
- Recruiting members of the new adjudication body recommended within the new Code consultation document, and inducting them in time for the launch date. Work in this area will include ensuring any Tribunal panel is able to combine adjudicatory ability with relevant skills and experience in key PRS areas such as marketing and digital content delivery.

### *Engaging actively, and sharing information with industry and other stakeholders throughout the value chain*

We expect that the programme of industry engagement that we have put in place in 2015/16 will be fully embedded in our way of working. We aim to ensure this is the case through:

- Measuring our performance through a stakeholder satisfaction survey covering industry views;
- Building feedback loops and analysis into our cultural shift programme, to ensure our people and processes continue to be aligned with a holistic approach to regulation;
- Regularly reviewing the effectiveness of the different ways in which we engage with industry to ensure we have a collaborative approach that leads to high levels of compliance with the Code. We will build a stakeholder mapping exercise into this process of continuous review, which we expect to include: the Industry Liaison Panel; the Rapid Response Team; and our programme of one-to-one meetings and engagement with industry representative bodies (including AIME and Mobile Broadband Group), network operators, service providers (both L1 and L2), and their compliance companies;
- Applying feedback from the 2015/16 Spring and Autumn Forums to ensure the corresponding 2016/17 events optimise desired industry participation.

### *Making effective and proportionate use of enforcement powers under our Code of Practice*

We will continue to ensure we demonstrate a proportional approach to regulation through:

- Application of Code 14, with clear communication on the benefits of the new adjudicatory process;
- Seeking to develop our funding model, to ensure there is a strong emphasis on the independence of PhonepayPlus' operating costs from the level of fines and administration charges applied through regulation.

## Objective 2: to identify and prevent emerging risks to consumers

### *Using research and market intelligence to identify emerging issues in the market*

We plan to develop our market intelligence and how it is applied through:

- Prioritising a full review of our reporting capabilities. This will include audience research, gap analysis, and subsequent development of our data capture systems;
- Commissioning an Annual Market Review for 2016/17. We aim to develop the Annual Market Review to include research on consumer satisfaction, and will re-align the prior year's data from the 2014 calendar year to enable operating year-on-year comparisons. This will also have the added advantage of providing fresher data for funding model assumptions on the size of PRS outpayments for the coming financial year;
- Developing a programme of dissemination that allows for all industry stakeholders to benefit from research findings, including Annual Market Review conclusions and findings from the research that will give further insight into how consumers interact with PRS;
- Working with industry partners to identify technological developments, tools and analysis that support horizon scanning for emerging risks, and establishing the most appropriate forum in which findings can be shared. In doing so we will explore opportunities to enhance our analytical and market intelligence capabilities, including evaluation of the applicability of commercially available market analysis.

### *Developing our market expertise and partnerships with other regulators, consumer bodies and organisations such as internet security companies*

Specific areas we have identified for 2016/17 include:

- Exploring how compliance benchmarks can be developed to measure our effectiveness;
- Building collaboration with audit houses to best develop market intelligence in areas such as app farms. In doing so we will aim to minimise duplication and maximise expertise, while retaining independence of our market intelligence capabilities;
- Developing our in-house understanding of technological and security advances through ILP partners and their wider networks.

### *In collaboration with phone providers and others, taking early action through enforcement, policy development and other tools to prevent emerging issues from becoming active problems.*

We aim to continue to deliver a balanced approach to preventing future harm to consumers through:

- Ensuring, through detailed monitoring, that the launch of Code 14 and its associated procedures provides for streamlined enforcement and opportunities for both earlier settlement of issues and redress earlier in the process than under the current approach;
- Ensuring the Rapid Response Team approach remains fit for purpose, with regular review both of its terms of reference and long-term effectiveness;
- Developing deeper working relationships with individual networks and the Mobile Broadband Group to better understand how PRS fits into their digital commerce portfolios, and the key operational challenges they face as part of this;
- Undertaking any further organisational development work necessary to develop our investigations processes and allow for greater informal service resolutions.



### Objective 3: to help consumers use premium rate services with confidence

*Helping consumers to obtain redress where they have suffered harm.*

We will build on our work to help consumers use PRS with confidence in 2016/17 through:

- Scoping the development and roll-out of a new Bill Checker service to consumers (as a replacement for Number Checker), with inbuilt online consumer data capture (e.g. feedback form);
- Focussing on complaint handling by merchants and aggregators. This will include revisiting guidance; conducting a programme of workshops to support informal compliance; and strong enforcement if complaint handling standards do not meet guidance;
- Delivering a mystery shopping programme, with a clearly communicated process of sharing and implementing findings with industry.

*Putting in place additional protections for vulnerable consumers, such as children.*

We will build on our work with industry in 2015/16 to ensure protection for vulnerable consumers is a top priority:

- We will continue to push at every opportunity for good levels of protection for vulnerable consumers;
- Where necessary, develop a programme of workshops and/or seminars to ensure vulnerability issues are understood in detail and related to service delivery.

*In collaboration with partners, providing information and support to consumers about potential risks and how to avoid them.*

During 2016/17 we aim to develop our consumer education work through:

- Exploring the option of a consumer panel to provide timely and detailed insight into collective consumer experiences (in addition to the consumer intelligence we gather from individuals). We will work in partnership with other regulators to determine whether the most efficient and effective way to proceed is in collaboration with their existing consumer panel work, or through establishing our own independent panel;
- Understanding and publishing any additional findings that the AMR research process generates, where this supports an improved insight into consumer behaviour in relation to PRS.
- Building our engagement with segmented PRS consumer groups. We will explore ways in which our reach and impact can be maximised, including reviewing our PhoneBrain initiative for young people, to see:
  - How building relationships with a range of partners can best develop content that resonates with different audiences;
  - Whether incentivised engagement can have a multiplier effect on reach and impact;
  - How industry partners and other stakeholders can be engaged to deploy their audience reach and impact.

## **Objective 4: to ensure that regulatory frameworks keep pace with market changes**

*Developing our knowledge of how the market in digital content and services is changing and of the implications of this for consumers, providers and regulation.*

With an enhanced programme of engagement with industry stakeholders and government bodies, we expect to be in position to ensure we understand and manage changes in the PRS market. At this stage we expect our work in 2016/17 to include:

- Supporting the compliant development of new and emerging PRS models, including app stores; quasi-physical goods; and new service areas;
- Developing the Annual Market Review to identify more granular key market change information, thus affording us the opportunity to develop our regulatory approach early and appropriately.

*Working with industry, other regulators and government to build a consensus on the best and most effective responses to these changes.*

We will continue to ensure we work closely with industry and government on the legislative processes begun in 2015/16. We expect, therefore, to:

- Respond to the government consultation process on the implementation of PSDII in the UK, which is expected to begin in the first half of 2016, and to develop regulatory clarity around e-money business models;
- Continue to engage with Department for Culture, Media and Sport officials as they work through the UK's response to the review of the EU regulatory framework for electronic communications.

## **Objective 5: to deliver effective and efficient regulation**

*Ensuring that our regulation continues to deliver the outcomes for consumers set out in our Code of Practice.*

We are resolutely committed to our outcomes-based approach to regulation, which we will reinforce during 2016/17 through:

- The launch and application of Code 14 in 2016/17, which will establish a more streamlined adjudicatory process and enhanced clarity on the use of Track 1 rather than Track 2 resolution;
- Undertaking stakeholder satisfaction research, and using the findings to ensure we collaboratively address any issues or gaps in our approach.

*Ensuring that we use resources efficiently and provide good value for money*

We are committed to delivering financial and operational efficiencies, and specifically for 2016/17:

- We have comprehensively reviewed each of our cost areas to plan for savings of 5% in real terms (see 5.4 below);
- We will continue to explore avenues for investment (e.g. compliance monitoring tools) that will yield long-term savings;
- We aim to work with industry to undertake a comprehensive funding review (see 8.1 below);
- We will further develop our data capture and analysis, to ensure our reporting meets the expectations and needs of all stakeholder audiences.

## 5. 2016/17 Operating Budget

5.1. The agreed full cost operating budget for PhonepayPlus for 2015/16 was £4,444,075 including VAT. Of this, £4,075,087 related to the core budget for levy purposes, and £368,988 related to the costs of the Registration Scheme.

5.2. We are now forecasting total expenditure for 2015/16 will be £4,450,041 (a variance of 0.1%).

Within this forecast we will successfully accommodate:

- £112k additional net costs of relocation;
- £103k spike in additional enquiry and complaint handling staff costs, reflecting the need to add short-term capacity to meet increased call activity;

This has been funded principally through:

- £115k organisational development savings delivered through a reduction in full time equivalent staff across the rest of PhonepayPlus;
- £100k cost savings across a range of activities, achieved through careful management and cost control (consumer education, market intelligence research and consultancy, website development).

5.3. During 2015/16, we have absorbed the costs of the Registration Scheme into the total operations of PhonepayPlus. This is after full consideration, and reflects:

- The significant overlap between PhonepayPlus' core data systems and those used to drive the functionality of the Registration Scheme;
- The impact of recent organisational development work, with roles undertaken by staff on core systems work and servicing the Registration Scheme being integrated;
- The increased complexity of allocating costs to the Registration Scheme.

The rationale for the Registration Scheme, and its functionality for members and users, however remains unchanged.

5.4. The proposed full cost operating budget for 2016/17 for which, subject to consultation, we will be seeking Ofcom approval is **£4,269,266** including VAT, as set out in Appendix A. This represents a **saving of 5% in real terms**, and 4% in cash terms, over the forecast for 2015/16.

Driven through effective management and cost control, we will principally achieve this saving through:

- The full year impact of relocating our offices, enabling overall property costs to fall by 26% (22% if the increase in asset depreciation is included);
- Delivering the planned improvements to our IT and business systems, enabling costs in this area to be reduced by 8% (21% if the reduction in asset depreciation is included);
- Ongoing organisational development work, enabling us to more flexibly manage our staff capacity and identify opportunities to minimise overall wage inflation within total staff costs.

5.5. Appendix A also provides a full allocation of the budget across each of our strategic objectives, which gives a broad indication of the financial weighting of our work (as described in headline terms in 3.3 and 4.3). Each budget cost area has been allocated separately, and combines time estimates with an assessment of direct relevance to each strategic objective.

## 6. Market Size and Levy Model

6.1. The levy funding model, as set out in Annex One to the Code of Practice, is the way in which PRS providers pay for the cost of the regulation of their market i.e. the budget for PhonepayPlus as approved by Ofcom.

The levy is applied to the actual size of the PRS market, defined as total PRS outpayments from network operators to their PRS industry clients i.e. after retaining their network charges from total revenues received.

6.2. To date, a theoretical **unadjusted levy** has been set, which is the rate that would be required to recover the full cost PhonepayPlus budget\* as a proportion of PRS outpayments.

\*total expenditure, less budgeted other income (Registration Scheme fees and bank interest).

6.3. In practice, an **adjusted levy** has been applied as the rate required to recover the full cost PhonepayPlus budget after the following adjustments:

- Deductions made in respect of:
  - Estimated over recovery of levy in previous year;
  - Retained funds available, based on estimated fines and administrative charges collected in the previous year;
- Additions made in respect of:
  - Estimated under recovery of levy in previous year;
  - Exceptional need to increase PhonepayPlus' contingency reserves.

6.4. The levy calculations for 2015/16 were:

	£
Estimate for total PRS outpayments for 2015/16 made in February 2015	448,341,379
PhonepayPlus full cost budget	4,444,074
Budgeted other income	(293,250)
	-----
Amount to be funded by unadjusted levy	4,150,824
Estimated over recovery of 2014/15 levy	(250,000)
Retained funds available	(1,221,243)
Amount for contingency reserves	0
	-----
Amount to be funded by adjusted levy	2,679,581

Unadjusted levy =  $4,150,824 / 448,341,379 \times 100 = 0.93\%$

Adjusted levy =  $2,679,581 / 448,341,379 \times 100 = 0.6\%$

6.5. The current estimated market size for 2016/17 is £430,400,000, as set out in Appendix B. This figure will be reviewed in February 2016, once 2015/16 Q3 outpayments data is available.

## 7. 2016/17 Levy

7.1. The levy calculations for 2016/17 are:

	£
Estimate for total PRS outpayments for 2016/17	430,500,000
PhonepayPlus full cost budget	4,269,266
Budgeted other income (7.2)	(262,500)
	-----
Amount to be funded by unadjusted levy	4,006,766
Estimated over recovery of 2014/15 levy (7.3)	0
Retained funds available (7.4)	(800,000)
Amount for contingency reserves	0
	-----
Amount to be funded by adjusted levy	3,206,766

Unadjusted levy =  $4,006,766 / 430,500,000 \times 100 = 0.93\%$

Adjusted levy =  $3,206,766 / 430,500,000 \times 100 = 0.74\%$

7.2. We propose the Registration Scheme annual fee remains unchanged at £155 + VAT, and have budgeted for a decrease in the total number of registrants to 1,500. We also propose that the current exemption remains in place for charities and first-year entrants to the PRS market.

Bank interest has been budgeted at £30,000.

7.3. We are forecasting that the total market size for the current 2015/16 year will be as estimated in February 2015. Therefore while there may be variations in recovery from individual networks, we do not currently expect to over or under recover the levy in total.

7.4. Fines and admin charges collected in 2015/16 are expected to be significantly lower than in previous years. This continues a downward trend (fines and admin fees in 2014/15 were lower than 2013/14), and reflects:

- The financial impact of the holistic approach to regulation that has been developed;
- Ongoing pressure on recovery rates due to the nature of the providers being fined e.g. they are situated overseas, or were always going to go bust if caught.

7.5. The increase in the adjusted levy from 0.6% to 0.74% illustrates the inherent instability in the current model. Changes to PhonepayPlus' budget has a relatively low impact on the size of the adjusted levy, with the two main influencing factors being the size of the market and the amount of collected fines and admin charges. In very broad terms and based on the assumptions above, to achieve a decrease in the adjusted levy by 0.1 percentage points (e.g. from 0.74 to 0.64) would require:

- A further £450k reduction in PhonepayPlus' budget for 2016/17 (moving from savings of 5% in real terms to 15%);
- The market size increasing by 9.3% to £490m (instead of the estimated 4% decline to £430.5m);
- An increase of £450k in 2015/16 of expected collected fines and admin charges, increasing retained funds to £1,250k.

## 8. Review of Levy Model and Proposed Variation for 2016/17

8.1. Through extensive consultation over the next 9 months, we wish to undertake a comprehensive review of the current levy funding model. Where any changes are identified that would require a revision of Annex One of the Code of Practice, we would not look for these changes to be implemented before the 2017/18 financial year.

The reason for seeking this review is to achieve the following:

- Updated and agreed principles behind the funding model, including a review of the “polluter pays” principle and how it is applied;
- Greater understanding and agreement on the level of operating costs PhonepayPlus needs to be an effective and efficient regulator;
- An agreed funding model that both (a) best delivers against principles, and (b) works in practice, to enable agreed operating costs to be recovered efficiently.

8.2. For 2016/17, we wish to consult on an interim approach that keeps a levy at the heart of the funding model, but is applied in a way that:

- Addresses the current in-built instability in the size of the adjusted levy;
- Emphasises the independence of PhonepayPlus’ operating costs from the level of fines and administration charges applied through regulation:

8.3. The proposed variation for 2016/17 is:

- 8.3.1. PhonepayPlus will recover its agreed full cost budget through an unadjusted levy. This will mean a clear break is established between the variation in annual fines and admin charges (and therefore the large swings in amount of retained funds available to adjust the levy amount required).
- 8.3.2. PhonepayPlus will only recover its agreed full cost budget. Therefore it will not seek to over or under recover the levy based on changes in the size of the market; instead the only post-year reconciliation will be for changes in market share between network operators. Note that this calculation will be confidential between PhonepayPlus and each individual Network operator.
- 8.3.3. PhonepayPlus will therefore account for any budget overspends by drawing on its contingency reserves. This circumstance will be identified as a key operating risk and will be managed accordingly both by the Executive and, as a governance issue, by the Audit, Risk and Corporate Governance Committee of the Board.
- 8.3.4. To retain adherence to the “polluter pays” principle, PhonepayPlus will redistribute back to network operators any fines and admin charges collected during the year. This will be done on the same market share ratio and at the same time as the reconciliation described in 2 above.
- 8.3.5. In the exceptional event that PhonepayPlus identifies an agreed need to increase its contingency reserves, this will be funded through retaining a share of fines and admin charges before they are redistributed back to network operators. The annual levy will therefore be clearly identified with only funding PhonepayPlus’ annual operating budget.
- 8.3.6. If this approach is agreed, PhonepayPlus will redistribute back to network operators any retained funds held on PhonepayPlus’ balance sheet at 31 March 2016. This will be done based at the same time as the levy reconciliation for 2015/16 is completed, and will be based on market share.

## 9. Consultation Process

9.1. We are keen to gather feedback from all stakeholders. In considering your response, we would particularly welcome comments against the following:

- The strategic priorities as set out, and our holistic approach to regulation;
- The range and nature of activities planned for 2016/17;
- The operating cost budget for 2016/17, and how that relates to our planned activities;
- The estimated size of the PRS market for 2016/17;
- The current levy funding model, and the suggested variation for 2016/17;
- The longer-term review of the funding model.

We plan to publish the outcome of this consultation and to make available all responses received. If you want all, or part, of your submission to remain confidential, please clearly identify where this applies along with your reasons for doing so.

9.2. The closing date for responses is 29 January 2016, which is designed to allow the time necessary to issue notices regarding changes to the levy and registration fees in good time for the start of the financial year on 1 April 2016.

9.3. Where possible, comments should be submitted in writing and sent by email to:  
[pbarker@phonepayplus.org.uk](mailto:pbarker@phonepayplus.org.uk)

Copies may also be sent by mail to:

Peter Barker  
Director of Corporate Services and Operations  
PhonepayPlus  
25<sup>th</sup> Floor, 40 Bank Street  
Canary Wharf  
London E14 5NR

Tel: 020 7940 7405

If you have any queries about this consultation please telephone or email Peter Barker using the above contact details.



## Appendix A – Budget Analysis

### Expenditure breakdown by cost area

	2015/16		2016/17
	Budget	Forecast	Budget
<b>People costs</b>	2,666,057	2,653,742	2,697,849
Salaries, NI, pension costs, training and recruitment			
<b>Policy, External Relations and Communications</b>	335,649	267,230	296,736
Research, forums, seminars, publications, consumer education and other communications activity			
<b>Legal Fees</b>	171,396	171,396	155,028
External advice, debt recovery and non-recoverable hearing costs			
<b>IT Systems</b>	357,819	362,534	333,560
Business continuity, office systems (including printing), contact information handling, case management, data analysis, and Registration Scheme			
<b>Telecoms</b>	72,027	82,642	81,093
Line rental (including handsets), incoming and external call charges, call data storage, Broadband, mobile monitoring			
<b>Premises</b>	475,397	556,763	410,304
Rent, service charge, rates, utilities and facilities management			
<b>Overheads</b>	134,005	130,366	135,814
Insurances, audit and other finance costs, office supplies, travel, couriers and postage, meeting costs			
<b>Depreciation</b>	231,726	225,403	158,883
Leasehold improvements, equipment and furniture, IT and systems, asset disposals			
<b>Total</b>	<b>4,444,075</b>	<b>4,450,076</b>	<b>4,269,266</b>

### Budget allocation by strategic objective

	2015/16		2016/17
	Budget	Forecast	Budget
<b>Objective 1: to continue to drive up compliance levels and trust in the market</b>	1,274,476	1,289,323	1,240,996
<b>Objective 2: to identify and prevent emerging risks to consumers</b>	1,027,596	1,063,500	996,367
<b>Objective 3: to help consumers use premium rate services with confidence</b>	722,100	713,941	676,775
<b>Objective 4: to ensure that regulatory frameworks keep pace with market changes</b>	557,001	565,328	540,998
<b>Objective 5: to deliver effective and efficient regulation</b>	862,902	817,985	814,130
	<b>4,444,075</b>	<b>4,450,076</b>	<b>4,269,266</b>



## Appendix B – PRS Market Size by Outpayments

	2013/14						2014/15						2015/16	2015/16
	Q1 actual	Q2 actual	Q3 actual	Q4 actual	Total		Q1 actual	Q2 actual	Q3 actual	Q4 actual	Total		Q1 estimate	Q2 estimate
3rd Party - Landline	24,185,492	22,394,017	22,463,211	18,094,724	87,137,444		17,524,567	16,366,013	17,886,609	13,805,951	65,583,140		13,324,460	12,078,624
Own Services - Landline	2,395,190	2,240,829	2,054,816	1,860,743	8,551,578		1,852,190	1,840,274	1,782,999	1,748,438	7,223,901		1,719,079	1,756,790
Total Landline	26,580,682	24,634,846	24,518,026	19,955,467	95,689,023		19,376,757	18,206,287	19,669,608	15,554,389	72,807,041		15,043,539	13,835,413
3rd Party - Mobile	43,097,048	40,040,615	46,843,832	46,885,616	176,867,111		35,593,309	41,003,510	45,333,296	37,278,207	159,208,322		37,537,770	38,129,086
Own Services - Mobile	14,166	9,722	7,670	7,175	38,733									
Voice Shortcode							4,217,788	3,880,839	4,286,871	3,697,445	16,082,943		3,698,358	3,297,108
PayFort / Operator Billing	7,767,383	6,801,359	8,259,004	10,446,984	33,274,730		13,224,919	15,378,135	21,222,793	22,581,168	72,407,015		26,210,240	27,573,172
Total Mobile	50,878,597	46,851,696	55,110,506	57,339,775	210,180,573		53,036,016	60,262,484	70,842,960	63,556,820	247,698,280		67,446,368	68,999,365
3rd Party - DQ	5,442,525	5,956,661	5,400,478	4,835,428	21,635,091		4,452,968	4,574,513	4,219,686	3,619,552	16,866,719		3,579,712	4,105,447
Own Services - DQ	18,676,540	19,187,808	18,934,366	17,184,059	73,982,772		15,517,815	15,661,610	14,764,968	12,500,040	58,444,433		12,087,391	12,064,515
Total DQ	24,119,064	25,144,469	24,334,844	22,019,487	95,617,863		19,970,783	20,236,123	18,984,654	16,119,592	75,311,152		15,667,103	16,169,962
3rd Party - 087	13,732,049	14,161,886	12,806,548	12,535,983	53,236,466		12,557,506	12,018,974	8,811,448	9,131,896	42,519,824		9,184,372	8,855,063
Own Services - 087	1,588,722	1,599,183	1,470,921	1,323,591	5,982,417		1,298,510	1,365,413	1,262,208	1,327,845	5,253,976		1,298,059	1,011,591
Total 087	15,320,771	15,761,069	14,277,469	13,859,575	59,218,884		13,856,016	13,384,387	10,073,656	10,459,741	47,773,800		10,482,431	9,866,653
<b>Total PRS outpayments</b>	<b>116,899,114</b>	<b>112,392,080</b>	<b>118,240,845</b>	<b>113,174,304</b>	<b>460,706,343</b>		<b>106,239,572</b>	<b>112,089,281</b>	<b>119,570,878</b>	<b>105,690,542</b>	<b>443,590,273</b>		<b>108,639,441</b>	<b>108,871,394</b>

### 2015/16 calculation

- In February 2015 we estimated the market size for 2014/15 would turn out to be £446.4m (compared with the actual size of £443.6m).
- Our estimate for 2015/16 of £448.3m was based on allowing for growth of £25.5m in operator billing, but then (with the exception of a couple of specific network provider reviews) an overall market decline of 5%.

### 2016/17 calculation

- Based on Q1 and Q2 data for 2015/16, we are forecasting that the market for the whole year will be as forecast i.e. £448.3m. This includes the assumption that any areas of additional market decline will be offset by additional growth in operator billing.
- Our cautious and prudent assumption for 2016/17 at this stage is an overall decline in the market of 4% to £430.5m.