Business Plan and Budget 2013/14

A statement by PhonepayPlus following its consultation published 29 November 2012

Issued by PhonepayPlus on 27 March 2013

1. STATEMENT ON BUSINESS PLAN AND BUDGET 2013/14

Introduction

PhonepayPlus is the regulator of premium rate telephone services (PRS) in the UK. These are the goods and services that you can buy by charging the cost to your phone bill or pre-pay account, ranging from 118 directory enquiries to in-app micropayments.

This plan sets out the resources we will require to regulate the market and maintain consumer confidence in PRS, as well as our plans to effectively use that resource.

In 2011 we launched our three-year Strategic Plan 2011/14, in which we updated our Vision and Values and set out our regulatory objectives and priorities for the period.

During the current strategic plan's life, there has been an important shift in PhonepayPlus' regulation, with a greater focus on working proactively with industry to prevent problems, on achieving the right outcomes for consumers and on ensuring that the regulatory regime is flexible, proportionate and responsive to changes in technology and business models. This shift has been illustrated in particular by the adoption and implementation of the outcomes-based PhonepayPlus Code of Practice (Twelfth Edition) (the Code) and the Registration Scheme.

The challenge we have set ourselves for this final year of the current strategic plan is to continue embedding these regulatory changes and making sure that they deliver real value for consumers and businesses. This year's business plan therefore has a strong focus on securing a compliant market and on making sure that consumers are treated fairly. We are also putting a particular focus on protecting vulnerable consumers, looking to build on important work we have done this year on child protection and on protecting the financially vulnerable.

Our work over the year 2013/14 will put a focus on preparing for the digital future. PRS and consumers' interaction with them are changing rapidly as a result of wider changes in the digital marketplace, for example the growing penetration of smartphones and the greater use of social networks to engage with services. It is important that regulation keeps pace with these changes so that consumers are protected from emerging threats in an effective and consistent way and that businesses can continue to innovate and develop.

Finally, this year's budget delivers on a commitment we made under our Strategic Plan 2011/2014 to reduce the cost of regulation without compromising on its effectiveness. The overall cost of regulation this year will be reduced by 0.5% in cash terms and 3.7% in real terms excluding irrecoverable VAT. The core levy budget has now been reduced on a like-for-like basis by nearly 25% in real terms since 2010/11, helping to reduce the costs of regulation on businesses during a difficult economic period.

Key themes for PhonepayPlus' Business Plan and Budget 2013/14

We have identified the following three key themes for PhonepayPlus in 2013/14:

Theme One – Strengthening compliance

Building compliance through improved due diligence and risk assessment and control:

We believe that whilst many Networks and providers have brought about changes to their internal processes to improve their controls around due diligence and risk assessment, we still see too many cases and examples where the root cause of the consumer harm could have been prevented or minimised had providers or Networks in the value-chain exercised more control either before contract or during service delivery. Our recent discussion paper[1] on this issue offered a prognosis of the issues and this will form a key theme for work we will undertake in 2013/14 with the industry to drive further improvements.

Making polluters pay:
Complaints to PhonepayPlus about PRS have been increasing for some time, and were on an upward trajectory before the new regulatory framework came into effect. During the year 2012/13, the PhonepayPlus Board developed an enforcement and compliance strategy designed to ensure we prioritise and target our resources to most effect and tackle the root causes of harm, in conjunction with due diligence and risk assessment work. Allied to this is a wider piece of work designed to ensure that PhonepayPlus continues to make polluters pay for the costs and harm that they cause to industry and consumers alike. By continuing to ensure that polluters pay for the incremental cost of regulation borne by all providers, we will ensure that our funding arrangements are equitable, fair and proportionate recognising that all providers benefit from effective regulation of the PRS market.

Theme Two – Improving consumers' experiences

Improving the customer journey:
We are only too aware from the many consumers we speak to daily that the customer experience they have encountered when they incur a problem with a PRS can sometimes be sub-optimal. We recognise that lengthy value-chains can cause consumer confusion but if trust and confidence in PRS is to grow then that journey needs to be seamless, straight-forward and simple to access. Alongside this, some phone companies would appear to be better than others at signposting their customers to us with the correct information so that we are ready and able to immediately assist them with their enquiry or complaint. We will conduct further research into this area in 2013/14 in order to work with providers and Networks on driving better customer satisfaction in this area.

Protecting vulnerable consumers:
Consumers who are vulnerable due to their personal circumstances require extra information and protection. Poor experiences for vulnerable consumers have a serious effect on consumer confidence and trust more generally in the PRS market. We must ensure that all consumers are clear about the costs of a service and its nature and that any information critical to their decision to use the service is not buried in small print. More generally, with the rapid growth of smartphone ownership by young people and children, we will take forward work to ensure that we continue to protect children and young people, including through our PhoneBrain initiative, which targets young users to build awareness and understanding about PRS.

Theme Three – Preparing for the digital future

Tackling the increasing risk from new online and security threats:
One driver of complaints and associated resource activity in 2012 has been from new forms of internet advertising, malware and misleading digital promotions. In 2013/14, we will continue to develop our mobile malware strategy following the success in 2012/13 in tackling this issue. We will also continue to identify further ways to engage with partners (such as

[1] http://www.phonepayplus.org.uk/News-And-Events/News/2012/9/PhonepayPlus-issues-discussion-paper-on-due-diligence.aspx

Facebook with whom we have recently entered into arrangements to tackle rogue affiliate marketing), to ensure that emerging threats, especially across the internet, can be effectively and speedily dealt with through a combination of enforcement powers and industry co-operation.

PRS in the future:
We recognise that PRS is increasingly becoming one online payment option which is competing commercially for consumers, who are presented with a range of options as to how they pay for digital content, across a multiplicity of devices. We need to ensure that we understand the implications of this, both in terms of our everyday regulation, and in terms of how we consider the future regulatory landscape as convergence of payments and communication networks and services takes hold. Now a year into the new Code we will be undertaking a preliminary assessment of the Code to identify what future changes may be necessary, to ensure that providers who offer PRS are not held back by regulation. In respect of future payments, we will be working with a range of other stakeholders to ensure we correctly assess the regulatory challenges as the future of payments unfolds including ensuring that any legislation that could affect this area is proportionate and future-proofed.

Business Plan and Budget 2013/14 Consultation

PhonepayPlus issued a public consultation on its Business Plan and Budget 2013/14 on 29 November 2012, with a closing date for responses of 17 January 2013. Seven responses from stakeholders were received and a meeting of the Industry Liaison Panel (ILP) was also held to discuss the proposals.

A summary of the responses is set out in Section 2 of this document along with our comments on the issues raised; the full stakeholder responses can be found on the PhonepayPlus website. The minutes of the ILP budget meeting can be found in Annex C.

Following consideration of the consultation responses and the ILP discussion, PhonepayPlus submitted the Business Plan and Budget 2013/14 to Ofcom for approval without alteration. Following a period of scrutiny, Ofcom approved the Business Plan and Budget in March 2013.

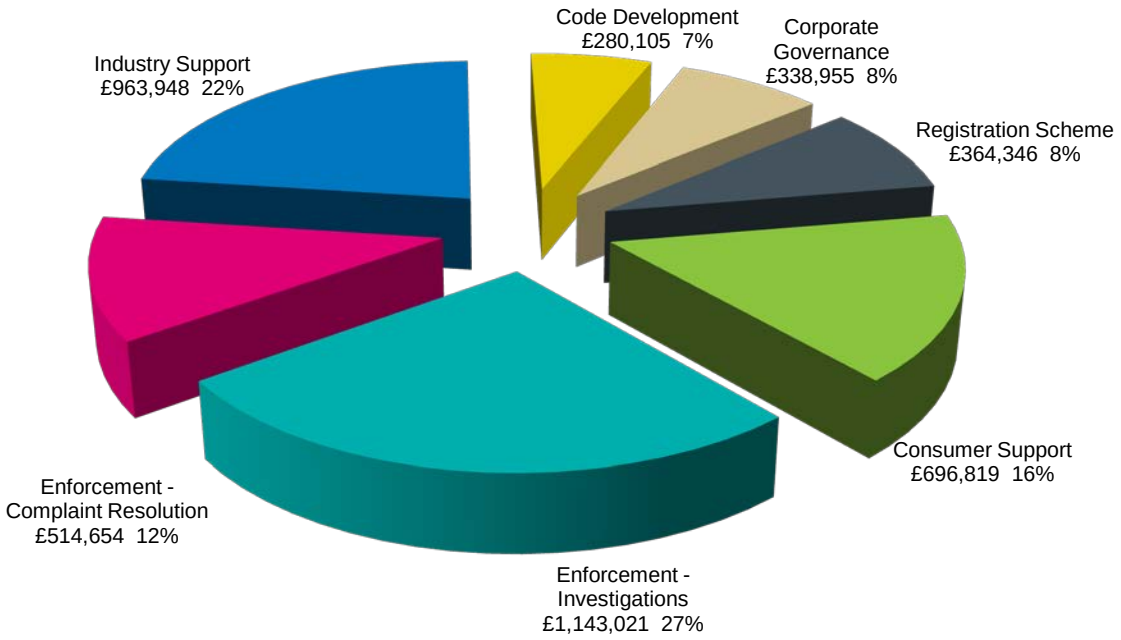
The budget

Total cost of PRS regulation in 2013/14

We expect the total cost of PRS regulation in 2013/14 to be £4,301,849. This comprises a core levy budget of £3,937,503 and a Registration Scheme budget of £364,346. The total cost of regulation excluding irrecoverable VAT will decrease this year by 0.5% in cash terms and 3.7% in real terms. PhonepayPlus' changed VAT status means that we will incur additional costs this year in irrecoverable VAT which we estimate at around £230,000.

The cost of each area of activity is broken down in the figure below. Work streams for the year 2013/14 are detailed in Section 5 of the Business Plan and Budget 2013/14 Consultation.

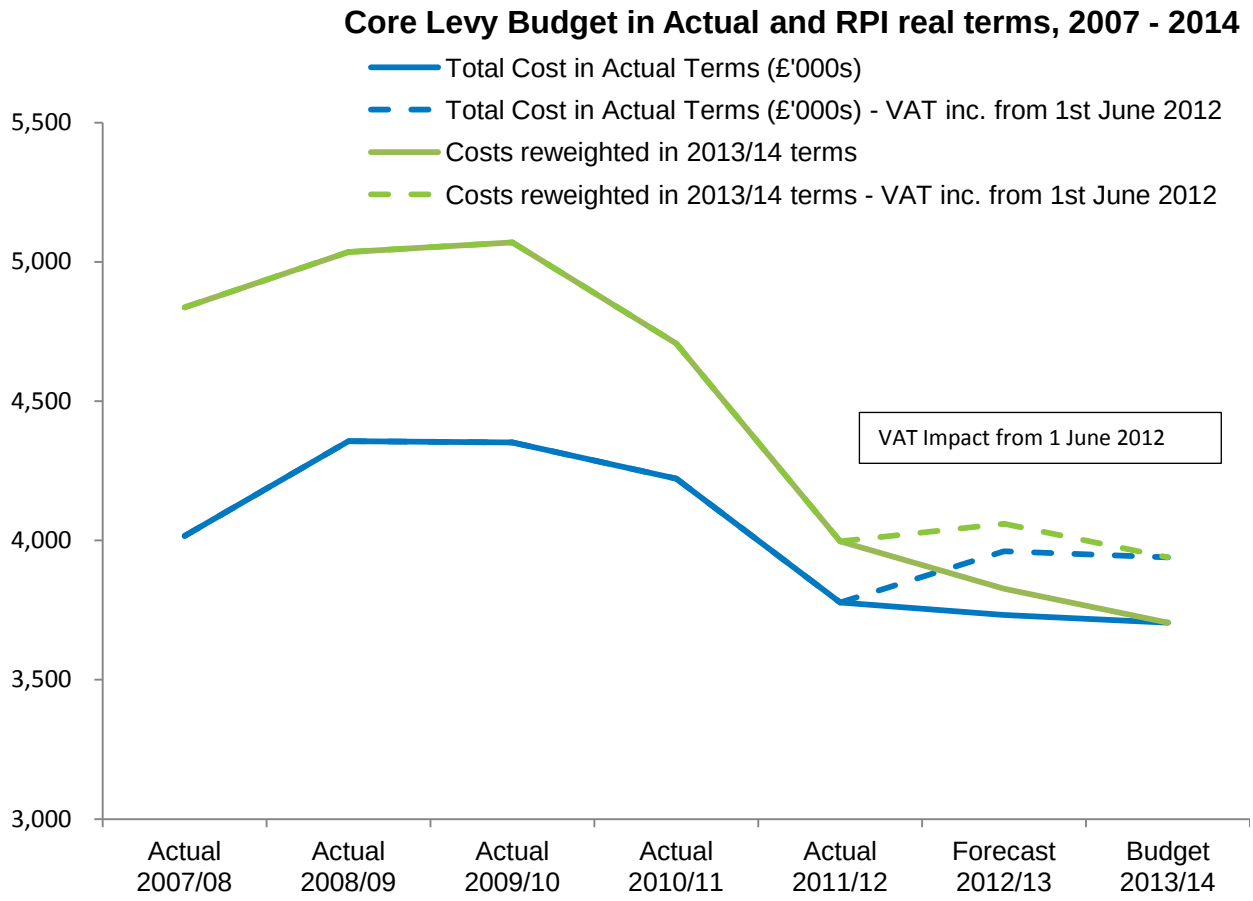
Activity Costing: Budget 2013/14
Total Budget £4.30m (incl. irrecoverable VAT)



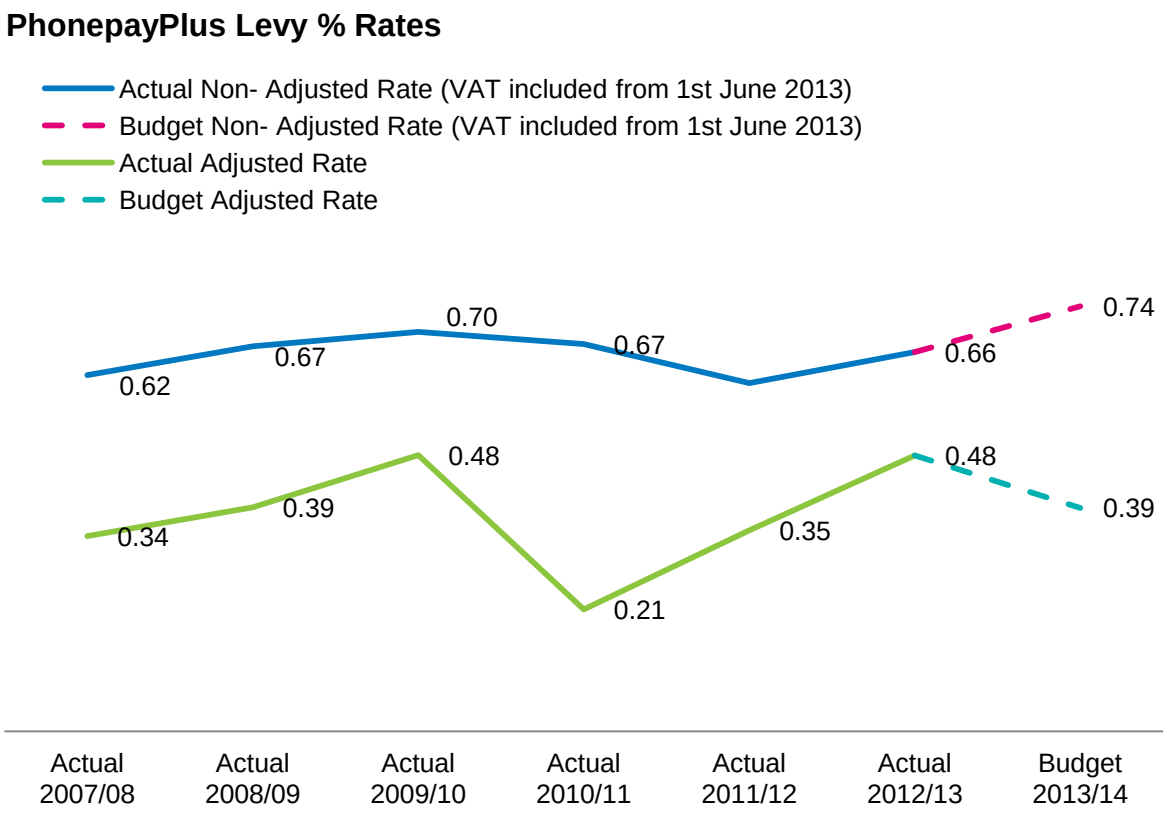
Industry levy

PhonepayPlus' adjusted levy for 2013/14 will be reduced to 0.39%. This adjusted levy applies to all outpayments payable by Network operators to providers in respect of revenue generated by PRS. The PhonepayPlus levy is calculated as a proportion of every outpayment to ensure that PhonepayPlus continues to receive adequate funding to carry out its activities, as required by Section 121 of the Communications Act 2003. The budget for levy-funded activity does not include the costs of implementing the Registration Scheme, as this is funded separately through registration fees. The registration fees and structure have also been confirmed for 2013/14 and are detailed in a later section.

The first graph below shows changes in the core levy budget in actual and real terms since 2007. It shows that on a like-for-like basis (i.e. excluding the impact of VAT changes), PhonepayPlus has reduced its core budget by around 25% in real terms since 2010/1



The second graph below shows changes in the non-adjusted and adjusted levy rates over the same period.



This non-adjusted rate would be the levy PhonepayPlus would need to raise if it did not receive any other income (such as fines, administration charges or bank interest). The adjusted rate is the amount PhonepayPlus is required to levy once the costs of regulation are offset by other income. A number of factors contribute to the calculation of the actual rate levied. Further information on how the PhonepayPlus levy is calculated can be found in Section 8 of our Business Plan and Budget 2013/14 Consultation.

This graph shows firstly that even with the savings made in the core budget, the contraction in the industry over the same period is putting upward pressure on the unadjusted levy rate, as the costs of regulation have to be spread over a declining base of levy-payers. Secondly, the chart shows how annual fluctuations in fine income have a significant impact on changes in the adjusted levy rate for the following year.

The adjusted levy rate this year is reduced to 0.39% from 0.48% last year because of an increase in fine income last year.

Fine income received last year rose, as at January 2013, to £1.816 million from £954,035 in the previous year. This has resulted in a lower levy for the industry as a whole. When calculating the levy rate we look at our requirements for the forthcoming year and adjust for capital, depreciation and fines received. For our budgeted requirements for 2013/14, we estimated that after these adjustments, we need to raise approximately £1.89 million through the levy.

PhonepayPlus' funding model

During the course of last year, PhonepayPlus received representations from a small number of industry members, who requested that PhonepayPlus should review and change its funding model. They raised concerns that the current funding model – with a uniform levy rate across all PRS outpayments – was unfair because it meant that those parts of the industry generating the most complaints were in effect being subsidised by other parts of the industry that generated fewer complaints. In light of these representations, PhonepayPlus raised the question in its consultation on the Business Plan and Budget 2013/14 if it should carry out a review of the funding model this year, with an allocation of additional resources to pay for the necessary technical and financial modelling work that such a review would entail.

PhonepayPlus is not persuaded of the case for carrying out a funding review this year for a number of reasons. Firstly, the consultation showed that there is far from an industry consensus on the need for a change in the funding model, let alone on what an alternative model would look like. This is true even amongst fixed-line providers who might currently benefit from a change to a model weighted more around complaints. There is even less support for allocating PhonepayPlus additional resources to carry out a funding review.

Secondly, as set out in the consultation document, PhonepayPlus considers that the current funding model has the benefits of simplicity and ease of collection that should not be lightly cast aside. It also considers that trends in complaints alone are not a strong basis on which to conclude that a funding model is unfair, as the costs of regulation are influenced by a wider range of factors and indeed can be driven by different sectors at different times.

Thirdly, to the extent that trends in complaint volumes are giving rise to concerns about equity, PhonepayPlus considers that a simpler way of addressing these concerns is by

making polluters pay. If those businesses that are driving complaint volumes pay more for the regulatory costs and consumer harm they are causing, then this will offset the costs of regulation for other more compliant businesses in the market without the need for a new funding model. As set out earlier, making polluters pay is a key theme of this year's business plan.

However, PhonepayPlus does recognise the concerns that have been raised by some industry members around the funding model and it will keep open the option of reviewing the model in future years, should there be a good case for doing so.

Registration Scheme

The Registration Scheme is now entering into its third year of operation. The Scheme, which generally speaking is mandatory for all providers operating in the premium rate market, sits alongside the Code of Practice. The Scheme gives PhonepayPlus and the industry a range of benefits providing transparency of the market, assistance in due diligence, risk assessment and control, easy access for consumers to customer care arrangements. It also contributes to our objectives, shared with stakeholders, of increasing confidence in the development and use of PRS.

The cost of the Scheme for the year 2013/14 is £364,346, which consists of the depreciation costs for the development and build of the system and ongoing operational costs associated with the support and operation of the Scheme. These costs are recovered by means of a registration fee which is paid annually by all those providers registered on the Scheme except for those who are eligible for an exemption.

This year we have been able to maintain the fee at the current rate: £135 plus VAT for all providers unless they are eligible for an exemption. We have retained the fee exemption for registered charities and the exemption for new entrants (new entrants to the market whose turnover for premium rate services is less than £10,000 in their first year of operation will be exempt from the registration fee; after this first year of registration they will then be expected to pay the full fee). Although the fee is likely to need to increase going forward, we believe maintaining the current level in 2013/14 is sustainable, offers good value for industry and provides stability and simplicity to the fee model.

PhonepayPlus is committed to reviewing the level of the fee and the exemption criteria annually. Our objectives here are to ensure the fee is set at a level which recoups the build and operational costs of the Registration Scheme and is fair and equitable to all by keeping costs as low as possible for the majority of providers whilst also looking to ensure barriers into the market are as low as possible for new entrants and charities.

Annual Market Review 2012

PhonepayPlus will publish its latest review on the current and future market for premium rate services in April.

2. SUMMARY OF RESPONSES TO THE CONSULTATION

We received seven formal responses to the consultation on the PhonepayPlus Business Plan and Budget for 2013/14 of which one is confidential. All others are published on our website.

Q1: During 2013/14 we will commence the preparation of the next three-year plan covering the period 2014/17. Do you have any feedback on the continuing appropriateness of both our current Vision and supporting Values?

AIME: AIME agrees that the Vision and Values are still appropriate. AIME also advocates that PhonepayPlus should look to support Networks and Level 1 providers in resolving most complaints and focus on those cases that need to be escalated to it.

BT: BT agrees that the Vision and Values are still appropriate. It suggests that PhonepayPlus should work closely with other regulators to share expertise.

Cable & Wireless Worldwide (CWW): CWW agrees that the Vision and Values are still appropriate.

Communications Consumer Panel (CCP): The CCP supports PhonepayPlus' work and is keen to see a high level of consumer confidence for purchasers in the PRS marketplace.

Mobile Broadband Group (MBG): The MBG broadly supports the Vision and Values presented by PhonepayPlus.

The Number UK (TNUK): TNUK generally agrees that PhonepayPlus' Vision and Values are sensible and uncontroversial. It recognises that "using PRS with confidence" is an admirable and worthwhile aspiration, but feels it should equally sit alongside a determination to help create a healthy, vibrant, successful and competitive PRS sector.

PhonepayPlus Response: PhonepayPlus notes that there is broad acceptance that its Vision and Values remain appropriate and relevant. It will work to engage and consult industry and other stakeholders as it draws up its Strategic Plan for 2014/17 over the coming year.

Q2: Do you agree with our assessment of the PRS market and do you have any other information or data that you could share?

AIME: AIME expects to see 2013/14 revenues ending slightly down on the previous financial year. It believes that market growth may rely on the success of PRS billing in online digital services and the opportunity for other off handset purchases of digital services or cash displacement (loose change scenarios) for quasi-physical goods (e.g. ticketing, parking, vending etc).

BT: BT agrees with the market assessment set out in the consultation document.

CWW: CWW forecasts another challenging year for the market, with continued volume decline in terms of fixed-line and directory enquiries.

CCP: The CCP broadly agrees with the assessment. It strongly urges the undertaking of any work that can be done to ensure that (proportionate) regulation keeps pace with market changes and encourage forward looking analysis of potential drivers of consumer harm.

MBG: The MBG expects the mobile element of PRS, to at least hold its own in the immediate future, with some prospects and opportunities for modest growth.

TNUK: TNUK largely agrees with PhonepayPlus' assessment of the PRS market as it relates to directory enquiries. Although it challenges the reasons given for this as its research shows that there are other factors than those suggested in the consultation.

PhonepayPlus Response: PhonepayPlus is in the process of carrying out its PRS Annual Market Review 2012. This will be published in April and will provide an in-depth analysis of the current state of the market and its future prospects.

Q3: What comments do you have regarding our themes for 2013/14?

AIME: AIME believes it is important that realistic expectations are set as to the level of oversight that Level 1 providers are expected to have over individual Level 2 provider activity on a day-to-day basis. It also asserts that improvements to the consumer experience must be driven by industry rather than at the regulatory level.

BT: BT agrees with the themes set out in the consultation. It notes that preparing for the future must create a compliant Higher Rate PRS environment.

CWW: CWW broadly supports PhonepayPlus' themes. CWW suggests that priority must be given to understanding the drivers behind the increased number of complaints and addressing these issues.

CCP: The CCP will be examining the generic "customer service journey" in the telecoms sector as part of its own work plan for the coming year and strongly endorses PhonepayPlus' attention to the specific area of PRS problems and the work with children (the PhoneBrain project). The CCP believes that all three themes are integral to the plan.

MBG: The MBG believes that PhonepayPlus' efforts to get itself better known to consumers need to look at platforms where PRS numbers are being regularly advertised. They also note that there is considerable work to be done on the part of Government, regulators and stakeholders to review the framework of regulation for this space.

TNUK: TNUK agrees that PhonepayPlus' proposed themes appear to be sensible and well-targeted and, in particular, it agrees with the intended focus on making polluters pay. TNUK further highlights that PhonepayPlus is proposing to undertake very limited work in relation to the directory enquiries sector and they are concerned about the cost of the PhoneBrain project.

PhonepayPlus Response: PhonepayPlus notes that there is broad support for the work themes it is proposing to address around strengthening compliance, improving consumers' experiences and preparing for the digital future. It will therefore work with industry and other partners in addressing these issues over the coming year.

Q4: Do you agree with our proposed work plans for 2013/14? If not why not?

AIME: AIME agrees with the following work plans: A technical review of the Code, Work with Ofcom to ensure Higher Rate PRS and 070 enforcement are effective, Work with providers and Networks to embed a culture of effective due diligence, Make polluters pay, Work with partners on ensuring children can use PRS safely, Work with Get Safe Online and others to ensure consumers are informed about how to use PRS safely, Introduce a time recording

system, Introduce new outcomes-based KPIs and other management information. AIME disagrees with the following work plans: Develop market understanding about the future of payments and Undertake a review of the consumer journey.

BT: BT agrees with the proposed plans. BT believes that PhonepayPlus must ensure that consumer education is integrated between children and adults.

CWW: CWW agrees with the stated objectives and work programmes. CWW suggests that they have not seen any evidence to suggest that the Code requires a technical review at this stage and would prefer a further period of stable regulation. CWW acknowledges that PhonepayPlus is right to consider its ability to enforce the current Code and to address any issues which it has encountered in doing so.

CCP: The CCP broadly agrees, as long as there is due emphasis on a holistic enforcement regime and the review of the consumer journey. The CCP strongly supports the plan to continue to inform young people, and consumers more generally through partnership-working.

MBG: The MBG is broadly supportive of the proposed work plan and welcomes the commitment to work closely with the ILP to keep the regulatory framework updated. The MBG concurs with the need to examine the regulatory arrangements for payment services.

TNUK: TNUK strongly supports the work programme designed to “make polluters pay” which TNUK believes should always be at the heart of everything that PhonepayPlus aims to do.

PhonepayPlus Response: PhonepayPlus notes that there is broad agreement with the proposed work plans for 2013/14 and it will therefore take these plans forward over the coming year. PhonepayPlus note in particular the strong cross-industry support for the workstream on making polluters pay. With regard to the technical review of the Code, we emphasise that this is not intended to undermine regulatory stability, which PhonepayPlus recognises is important. The technical review will not change core elements of the Code – such as the outcomes-based approach – but is rather intended to look at whether any of the more technical provisions in the Code need to be updated in light of market or other developments since the Code was designed.

Q5: Do you agree with our planned resource allocation and activities for 2013/14? If not, why not?

AIME: AIME is pleased to see an increase in the Registration Scheme budget and that there has been a reduction in the compliance advice budget. AIME does not see the need for the size of the Code development budget or the research budget. AIME wants to see a reduction in investigations and more emphasis placed on referring the consumers back to the merchants or informal procedures rather than investigations. AIME believes that PhonepayPlus’ work on future payments should stick to its core remit.

BT: BT agrees with most of the allocations. BT notes that with the forecast growth in Track 2 cases and emerging threats, the proposed increase in Track 2 funding will need robust fines and admin charge collection.

CWW: CWW welcomes the acknowledgement that the current economic climate is challenging and the continued steps that have been taken to provide further efficiencies within the budget.

CCP: The CCP supports the planned activities. The CCP is pleased to note that the proposed allocation for consumer support has been increased, following its reduction in 2012/13.

MBG: The MBG agrees with PhonepayPlus that it would not be appropriate to propose an increase in the cash budget in these constrained times.

TNUK: TNUK largely agrees with the proposed allocation between each of the activities. Enforcement should be PhonepayPlus' principal activity. TNUK believes consumer support is a critical activity which must be sufficiently well-resourced but queries whether compliance advice can continue to be provided free of charge indefinitely.

PhonepayPlus Response: PhonepayPlus notes that there is broad support for the proposed budget for 2013/14 and that this was also reflected in the ILP budget discussion. Therefore PhonepayPlus has decided to recommend the budget proposed in the Business Plan and Budget 2013/14 Consultation to Ofcom.

PhonepayPlus has decided not to make reductions to the Code development, research or investigations budgets as suggested by one respondent. It is satisfied that the amounts budgeted for these areas of work are necessary to meet its regulatory objectives for the coming year and that they provide good value for money for the outcomes they achieve.

Q6. Would you support extra cost for a Funding review in 2013/14?

AIME: AIME believes that the funding arrangements for the operation of some areas of PhonepayPlus should be reviewed and it would welcome discussions between PhonepayPlus and the industry on future funding. In particular AIME would like to look at different usage charges for certain activities such as compliance advice.

BT: BT disagrees with the need for a funding review and attendant cost and instead supports funding in favour of good compliance with rewards for good behaviour. Looking forward, BT suggests it is appropriate to review the arrangements to ensure that the forthcoming revisions to the NTS regime are reflected in the funding structure going forward. BT also suggests that consideration should be given to using caller-paid revenues rather than out payments as the basis for the levy.

CWW: Whilst noting dissatisfaction amongst some stakeholders about the current funding model, CWW did not find a compelling reason to review the model and is of the view that any review would most likely conclude that the current model is the most appropriate. CWW further notes that the debate about a funding review was often characterised by the changing profile of complaints to PhonepayPlus as a source of potential inequity in the current model. It observes, however, that the shift in complaint profile may be offset by reference to previous periods where patterns of complaint were the reverse of today. CWW notes and supports the work by PhonepayPlus to concentrate on making polluters pay and to thus offset these fines against future general levies. Finally, CWW notes that the current NGCS review by Ofcom could have an impact of the PhonepayPlus funding model and signal the need for a review at that point.

CCP: The CCP concludes that this issue was beyond the ambit of the panel to address.

MBG: The MBG does not support the optional budget item and does not believe a funding review is necessary so soon after the last exercise carried out by KPMG. The MBG supports the polluter pays principle and supports PhonepayPlus' intention to improve fine collection rates.

TNUK: TNUK made a number of points which can be summarised as follows:

- PhonepayPlus framed the discussion on the cost of a Funding Review on the costs involved rather than on the fairness and benefits which such a review might generate in the hope that respondents might accept the status quo;
- The DQ sector works well for consumers (as alleged to be evidenced by the low level of complaints to PhonepayPlus) and in this context the current flat rate levy funding model is inequitable and directly contrary to the polluter pays principle;
- TNUK would instead favour a service-orientated funding model by more closely aligning the desire to target information providers and make them more directly responsible for the harm their service causes. For voice services this would be simply based on the number range in question. Non-voice services could be similarly divided by category e.g. reversed bill SMS, Payforit, red button etc;
- This service-based model is supported by the KPMG review (option 4b refers);
- If PhonepayPlus does not accept a service-based funding model then PhonepayPlus should consider an approach based on enforcement activity and that the entire enforcement budget should be recovered by administrative charges. TNUK observes that this proposal is aligned to the KPMG review (option 8 refers). TNUK goes further to support an additional surcharge levy for those subject to PhonepayPlus enforcement activity;
- Finally, TNUK suggest that that it may not also be appropriate for PhonepayPlus to continue to provide industry support and compliance advice for free indefinitely and that instead those who seek such advice should be charged accordingly.

Confidential response: The confidential response supports the case for a review of the funding model and the additional budget provision of £100,000. The responder believes this is necessary to address the unfair levy setting process which results in the effective cross-subsidy of mobile services by the fixed-line industry. In addition, the responder could support the use of bonds and guarantees for certain higher risk services to assist with more reliable fine collections.

PhonepayPlus Response: With the exception of one respondent, there is no appetite for the budget to be increased by £100,000 to fund the resources necessary to undertake a funding review and there is no agreement about an alternative funding model or indeed whether the current model is no longer fit for purpose.

One respondent makes the case for a funding review based on the KPMG review. The review was clear that the current funding model is not broken and enjoys wide stakeholder support. PhonepayPlus still believes this is the case, whilst recognising that the funding model – like all others which support regulatory costs – are never perfect.

PhonepayPlus agrees that insofar as there is a perceived unfairness in the current funding model, it is based on the current volume of complaints and specifically their distribution

between mobile-based services and fixed-line, 0871 and directory enquiries services. Whilst PhonepayPlus would agree that the greatest volume of complaints it receives are related to mobile services this is not the only driver of PhonepayPlus costs. Furthermore, PhonepayPlus has in place an agreed principle that making the polluters pay for the cost of complaints by proportionate fines and administrative charges that should reflect the total cost of investigating the complaint. This principle of making polluters pay for the incremental burden that they cause to legitimate providers is one that therefore should be pursued fully during 2013 and beyond as through this route we have an opportunity to remedy the perceived inequities identified by some respondents in the current funding model.

With respect to alternative funding models, whilst it is noted that KPMG did outline various alternative options, none were clearly recommended as alternatives to a model which they endorsed (as did industry stakeholders). If any of the KPMG options should be considered they would need a further and detailed consideration in light of the changes that have taken place in the market – as well as our regulatory framework, combined with a chargeable Registration Scheme – since 2009. Some of them will clearly have wider ramifications and short-term costs attached to them for implementation. With regards the option of recovering all the costs of enforcement from those who are fined, PhonepayPlus is reviewing its administrative charges model for cost attribution to ensure that it has robust means to cost each investigation and ensure those costs are accurately reflected in the administrative charge set by a Tribunal at the end of a case.

PhonepayPlus also agrees that there is no benefit to be had from committing resources to undertake a funding review in 2013/14 as there is a clear absence of wide support for such a review. Without it and review conclusions are likely to be rejected by respondents as there is no agreement about the structure of a funding model that could secure wide agreement as to its equity. PhonepayPlus has therefore decided to defer a decision on a funding review until such a time that a wider consensus can emerge about the need for change and/or the wider external landscape resulting from, for example, impacts arising from Ofcom's NGCS review, led PhonepayPlus to conclude that the timing a funding review was now imperative, which it is not at present.

Q7: Do you agree with our assessment that the charging model, and exemptions, should remain unchanged during 2013/14? If not, why not?

AIME: AIME agrees that the charging model and exemptions should remain unchanged for 2013/14, though this must be supported by a continual drive for efficiency savings.

BT: BT believes that any non-compliance should make the company eligible for payment of the registration fee. It proposes that charities should continue to be exempt from the registration fee, all other organisations should pay the same registration fee. BT also believes that those organisations generating less than £5,000 in their first year of operation should be exempt.

CCP: The CCP does not have a view on the detail of the charging model, so long as it is ensures sufficient funding for PhonepayPlus to operate effectively and provide a high service standard for consumers.

CWW: CWW is satisfied that the current charging model and exemptions for the Registration Scheme continue to be appropriate.

MBG: The MBG supports the proposed charging model for the Registration Scheme.

TNUK: TNUK is content with the current proposed method of funding the Registration Scheme and have no further comments to make in that regard.

PhonepayPlus Response: PhonepayPlus notes that there is broad support for its proposals on the charging structure and rates for the Registration Scheme and has therefore decided to keep them unchanged for this year.

ANNEX A: PhonepayPlus Budget 2013/14

	Note	Budget 2013/14 excl VAT	Budget 2012/13 excl VAT	Budget Variance (Inc) / Dec excl VAT	% Change	
Staff		2,383,079	2,376,477	(6,601)	0.3%	▲
Communications		103,250	103,850	600	(0.6%)	▼
External expertise		143,000	146,000	3,000	(2.1%)	▼
Legal	1	101,000	123,333	22,333	(18.1%)	▼
Intelligence		150,000	150,000	0	0.0%	▶
External audit & outsourced services		17,091	23,205	6,114	(26.3%)	▼
Overheads		289,229	295,029	5,800	(2.0%)	▼
Premises		314,321	306,914	(7,407)	2.4%	▲
Publications		10,550	10,740	190	(1.8%)	▼
Telecoms	2	52,884	44,030	(8,854)	20.1%	▲
Website		31,150	37,850	6,700	(17.7%)	▼
Depreciation		109,195	124,754	15,559	(12.5%)	▼
Total budget funded by Levy	=	**3,704,749**	**3,742,183**	**37,434**	(1.0%)	▼
		incl VAT	incl VAT	incl VAT		
Estimated irrecoverable VAT 13/14 (12/13 restated for comparison)		232,754	239,661	6,907	(2.9%)	▼
Total Budget funded by Levy – including VAT		**3,937,503**	**3,981,844**	**44,341**	(1.1%)	▼
Registration Scheme		361,883	344,437	(17,446)	5.1%	▲
Cross-charge VAT impact on Registration		2,463	2,463	0	0.0%	
Total including irrecoverable VAT impact		**4,301,849**	**4,328,744**	**26,895**	**(0.6%)**	▼
TOTAL excluding irrecoverable VAT impact		4,066,632	4,086,620	19,988	(0.5%)	▼

This expenditure budget is presented in traditional accounting style to allow stakeholders to compare the proposed spending in 2013/14 with the previous year.

1. This reduction reflects the expected reduction of legal challenges at this stage of the Code lifecycle.
2. The increase in cost for telecoms is due to an over projection of the cost savings in the previous financial year together with set up costs for the migration to a Session Initiation Protocol (SIP) system. The adjustment reflects the actual cost and provides for a £5,000 reduction in costs per annum on the previous telecoms set-up.

ANNEX B: PhonepayPlus Expense Budget 2013/14 – The Registration Scheme

		Budget		Budget		Budget Variance	%
	Note	2013/14		2012/13		(Inc) / Dec	Change
		excl VAT		excl VAT		excl VAT	
Staff		110,413		108,974		(1,439)	1.3%
External expertise	1	10,000		5,000		(5,000)	100.0%
Overheads	2	93,621		85,229		(8,392)	9.8%
Premises		14,490		16,054		1,564	(9.7%)
Website	3	22,721		18,541		(4,180)	22.5%
Depreciation		110,639		110,639		0	(0.0%)
Total excluding VAT		**361,883**		**344,437**		**(17,446)**	**5.1%**
Cross-charge VAT impact on registration		**2,463**		**2,463**		**0**	**0.0%**
Total including irrecoverable VAT impact		**364,346**		**346,900**		**(17,446)**	**5.0%**

Notes:

1. This additional cost is driven by project work related to PhonepayPlus initiated enhancements.
2. This increase is due to uplift on our contract with our supplier, as well as additional data storage costs.
3. The cost of some website changes will now be borne directly by PhonepayPlus core, so the recharge is reduced accordingly.

ANNEX C: Minutes of the ILP (budget) meeting 18th December 2012

NOTES OF THE ILP (BUDGET) MEETING NO 33 HELD ON

TUESDAY 18th DECEMBER 2012

Present:

Graham Pottie – BT (acting as Chair of the ILP)
David Ashman – AIME (attending via conference call)
Tom Cherry – Ofcom
Gavin Daykin – Ofcom
Jeremy Flynn – AIME
Suzanne Gillies – Action4 (attending via conference call)
Jeremy Hallsworth – PP+ Board and BT Agile Media
Justin Hornby – UKCTA
Hamish MacLeod – MBG (attending via conference call)
Chris Pateman – FCS
PhonepayPlus
Andrew Pinder (Chair)
Paul Whiteing (Chief Executive)
Mark Collins
Patrick Guthrie
Jo Prowse
Stephanie Ratcliffe (minutes)
Apologies:
Paul Berney – MMA
Shawn Brown – MDA
Ann Cook – ITV
Hugh Griffiths – PP+ Board and Mobile Services
Rory Maguire – H3G, MBG commercial
Andy Martin – FCS

Welcome:

Graham Pottie, acting as Chair to the ILP, welcomed representatives to the meeting. Apologies were noted and attendees using the conference call facilities.

It was noted that the minutes and actions from the previous meeting, held on 20th November, would be covered at the ILP meeting on 12th February 2013.

1.0 Business Plan and Core Budget 2012/13

Presentation

Paul Whiteing presented an overview of the PhonepayPlus Business Plan and Budget for 2013/14 and explained that the overview sets into context what has already been summarised in the budget consultation document.

Key points addressed focus on:

Outlining the key shifts that have been made as a consequence of a move from a “Rules-based” Code to an “Outcomes” based Code which provides more flexibility for interpretation and application in a fast-changing environment. At the same time the point of enforcement

had shifted from a single point of focus on the “service provider” to a distributed targeted enforcement approach. These changes were in exchange for a greater expectation, supported by the Code, on Due Diligence and Risk Assessment and Control responsibilities being exercised by all providers in particular Level 1s.

Next Paul Whiteing outlined the issues encountered in this shift of regulatory approach. It was never going to be an easy and straight forward shift. Good progress has been made but it is clear that there is more yet to be done, including in tackling the increase in complaint volumes that pre-date the new Code. The Business Plan identifies 5 key issues that are priority issues. These are:

- Continuing due diligence failings by some providers and networks;

- Increasing volume of complaints;

- Growing risk to consumers from malware, misleading digital promotions and affiliate marketing programmes;

- A sub-optimal customer experience journey; and

- A recognition that PRS is competing in a changing payments landscape.

In response to these challenges, strategic themes will run alongside the three-year Strategic Plan namely;

- Strengthening compliance;
- Improving consumer’s experience and protecting vulnerable consumers;
- Preparing for the digital future and tackling increasing risks and threats.

Working programmes in support of the themes will be further developed to address these issues which will be in addition to business as usual operations.

Finally with the Registration Scheme, Paul Whiteing said the Scheme continues to add value both as a due diligence tool and as a feed to the Number Checker. There are currently 3,100 registrants of which 64% are payable and 36% exempt. It was noted that £25K has been set aside for enhancements to the registration budget for 2013/14 with a further £20K for each of the following two years.

Regulatory budget proposals for 2013/14

Paul Whiteing advised at the meeting that the proposed core levy budget is £3,937,503 (inc VAT) which represents a 4.2% reduction in real terms on 2012/13. Some activity cost shifts are proposed in response to short term priorities as complaints, investigations and consumer concerns rise and, with the exception of telecoms expenditure, most cost centres are frozen or reduced. With respect to the Registration Scheme, the budget is proposed at £364,346 (inc VAT) which represents a 5% increase over 2012/13.

Overall budget proposal is £4.3 million (inc VAT) which represents a 3.7% decrease in real terms over 2012/13.

Levy rate and Registration fee proposals for 2013/14

Paul Whiteing advised that based on the current budget and accepting there are certain unknown pieces of financial data that will only be available at the year end, that on this basis the proposed levy rate is likely to fall from 0.48% to between 0.30% and 0.40%. The exact levy rate will only be determined in March 2013 once there is a clearer picture on fine collection and outstanding legal challenges.

Proposed registration fees – the fee for next year is proposed to be held at current 2012/13 rates/exemption categories however, depending on the registration churn over 2013/14, the current assumption is that fees will increase to £150 in 2014/15.

The overall proposal is that the cost of regulation will decrease for 2013/14.

Funding Model review

Paul Whiteing advised the ILP that principles around the proposal to review the funding model are set out in the consultation document. He explained PhonepayPlus' criteria for a model to be fair and efficient; to be collectable and administratively efficient and to command wide industry support. The last review of the model took place in 2009 and it was noted that any change will be costly and complex. Paul Whiteing asked the ILP to provide feedback and an objective assessment on whether to review the model. He advised the ILP that the additional cost of, in the region of £100K, to review the model had not been built into the budget.

Discussion

In discussion, a number of points were raised by the ILP and noted:

- It was agreed that in order to improve the customer journey PhonepayPlus should enhance its relationship with 3rd party consumer bodies and proactively reach these bodies which liaise directly with consumers, rather than solely rely on reaching consumers independently. The Executive is already working closely with a range of organisations to this effect – e.g. Citizen's Advice, Get Safe Online and ChildNet – but it was agreed that it would be helpful to develop a more specific Strategic Plan in this area.
- KPI measures, metrics and performance outcomes, in terms of how effective and efficient we are as a regulator, will be discussed at the ILP, at the next meeting in February. Changes include a new reporting structure to the Board and a refocus on the external stakeholder audience with the production of a bi annual report providing market indicators and key operational performance metrics.
- Chris Pateman from FCS supported the extra expenditure required to review the funding model and agreed that industry stakeholders can provide valuable input into the review and recommended a workshop is initially set up to review the model. In further discussion the ILP agreed that before considering issues around the funding model it was important to improve incentivising compliance and the polluter pays policy early in the year as this could help address the concerns raised around equity. It was proposed that an industry workshop is set up to address issues around the polluter pays policy and the 30 day rule.

3.0 Conclusion

The ILP confirmed their support for the proposed business plan and budget for 2013/14. There was an agreed view around the table that the business plan and budget were very credible and should be supported.

4.0 AoB

- Legal cost recovery – Paul Whiteing to provide update to ILP.
- Chair nominations – to be sent to Hamish Macleod by 31st January 2013.

<u>ILP meetings in 2013 at PhonepayPlus Offices</u>

Tuesday 12th February 10-1pm
Tuesday 23rd April 10-1pm
Tuesday 23rd July 10-1pm
Tuesday 15th October 10-1pm
Tuesday 17th December Budget Meeting 10-11.30am