

**Ofcom Response to Consultation on  
Draft Statement of Charging Principles  
and further consultation**

**Issued: 6<sup>th</sup> December 2004**  
**Closing date for responses: 17<sup>th</sup> January 2005**

# Contents

Section		Page
1	Summary	3
2	Background and Introduction	9
3	General charging principles	12
4	Application of principles to the Television Sector	17
5	Application of principles to the Radio Sector	27
6	Application of principles to the Networks and Services Sector	33
7	Draft Statement of Charging Principles	38
8	Draft Notice of Designation under Section 38 and 34 of the Communications Act 2003	55
9	Draft guidance on Relevant Activity in the Networks and Services sector	57
10	Responding to this Consultation	66
Annex 1	Principles of calculation of Relevant Turnover – Television	68
Annex 2	Principles of calculation of Relevant Turnover – Radio	92
Annex 3	Ofcom’s consultation principles	95
Annex 4	Consultation response cover sheet	96

## Summary

- 1.1 Ofcom assumed its functions from the old regulators on 29 December 2003, which meant that it had a very limited time between publishing its business plan setting out its funding requirements for the first charging year and the setting of tariffs for the 2004/5 charging year on 31<sup>st</sup> March 2004. Therefore, Ofcom undertook a shortened consultation on the Statement of Charging Principles and based its 2004/5 tariff principles largely on those of the old regulators. During its consultation on these, a considerable number of stakeholders raised issues that they did not believe had been effectively addressed in the old regulators' principles. Ofcom agreed that many of these issues deserved a further airing and consulted stakeholders in July 2004 on its proposals.
- 1.2 Having undertaken the promised consultation, Ofcom now presents its proposals and the underlying rationale and sets out a draft Statement of Charging Principles to be applied from the charging year 2005/6 onwards.
- 1.3 In these proposals, Ofcom has addressed five generic issues:
  - the appropriate measure to use as the basis of setting tariffs (e.g. revenue versus audience share or profit);
  - what types of revenue should be included for the purposes of setting tariffs;
  - the structure of tariffs (including the extent to which tariffs should be flat-rate; in line with the operator's respective size; or be progressive, such that larger operators pay proportionately more than small operators/ new entrants);
  - implementation of transitional relief to moderate the impact of significant changes to the structure of tariffs on individual operators;
  - whether individual operators could repay, in one lump sum, their share of the Government loan which funded the outstanding liabilities of the old regulators and the establishment of Ofcom.
- 1.4 Ofcom is required by law to ensure that its revenues fully cover the costs of regulation; and to raise from each of the television, radio and networks and services sectors its best estimate of the cost of regulating each sector for the year ahead with any under-recovery or over-recovery against the end-year outturn being reflected in the following years' fees for the respective sector.

### Principles of Setting Tariffs

- 1.5 Ofcom's objective in setting its tariffs is the effective collection of its funding requirements in a fair and equitable manner and with the minimum administrative burden on stakeholders.
- 1.6 Ofcom's proposals for setting licence fees and administrative charges seek to meet, to the greatest possible extent, the following criteria:
  - **Fairness.** The tariff structure should raise Ofcom's required funding across the regulated sectors in a manner that is equitable;
  - **Cost-reflectiveness.** Charges should broadly reflect the underlying

- cost of regulating each category of stakeholder;
- **Reliability.** The tariff base needs to be stable over time, and not prone to erratic movements. Charges should not move substantially in any one year;
- **Simplicity.** The calculation of charges should be as simple as possible, wherever practicable using data that stakeholders would in any case gather for their own management purposes; and be relatively simple to administer for Ofcom;
- **Be easily verified.** Information required for the setting of charges should be easily verifiable to ensure industry-wide compliance;
- **Adaptable.** Tariff principles and structures should be able to adapt to a changing market environment and be consistent with wider policy; and
- **Relevance.** Charges should cover in full an operator's activities that flow from the licence or authorisation, but only those activities.

## Proposals

- 1.7 Ofcom's proposals are set out in detail in this document and are summarised in the following paragraphs.
- 1.8 Ofcom proposes to retain a revenue measure as the basis of calculating licence fees and administrative charges for the television, radio and networks and services sector. While other methods each have their individual merits, Ofcom believes that revenue most closely matches the criteria set out in paragraph 1.6 above.
- 1.9 Ofcom proposes that the tariff structure should have a modest degree of progression, so that smaller operators and new entrants pay a lower proportion of their revenues than larger established operators.
- 1.10 Ofcom intends to continue to keep radio and television as separate regulatory sectors with separate tariffs to reflect the differences between the sectors in terms of industry structure, size of operator and business models.

## Further consultation

- 1.11 Ofcom is consulting in this document on a new designation in the context of administrative charges set out at Section 8 and on Relevant Activity guidelines which are set out at Section 9.

## Definition of Relevant Turnover in Television

- 1.12 In the television sector, Ofcom proposes to change the definition of Relevant Turnover from being based on Qualifying Revenue, as defined in the 1990 Broadcasting Act, to a new definition as set out in Annex 1 of this document.
- 1.13 The definition of Qualifying Revenue was designed to meet different purposes in the Broadcasting Acts, it is not adaptable and can lead to distortions in the treatment of different operators as their business models evolve.
- 1.14 The proposed new definition of Relevant Turnover will include all revenues which flow from the possession of a broadcasting licence, including those from subscription, advertising, sponsorship and interactive services/applications

(including, for example, revenue deriving from premium rate telephone lines, betting and gaming services and interactive advertising).

- 1.15 Ofcom proposes that, as a general rule, Relevant Turnover should exclude revenue earned by the operator of any television platform in respect of the retailing of television channels (i.e. retail subscription revenue). This is not an Ofcom licensed activity. Instead, all revenue earned by an Ofcom licensee from the wholesaling of a channel to any television platform operator shall be included within Relevant Turnover. However, in certain limited instances where wholesale revenues attributable to a channel cannot be easily ascertained, retail revenues will be used as the starting point for determining the level of subscription revenues which will fall within Relevant Turnover.
- 1.16 One specific exception to the general approach described above relates to shopping channels. Since the main regulatory functions relating to such channels have passed to the Advertising Standards Authority with effect from 1st November 2004, Ofcom proposes to introduce a simple flat fee for such channels in order to cover the cost of Ofcom's residual regulatory duties. It is expected that this flat fee will be equal to the minimum fee. Ofcom also proposes to put teleshopping channels into a new regulatory category, Category E, for this purpose.
- 1.17 The underlying principle in determining Relevant Turnover is that only those revenues deriving from the broadcaster's licensed activities should be included. Accordingly and by way of example, revenues earned pursuant to a Gaming Act Licence will be excluded. However, any revenues earned by the broadcaster from the provision of access to such betting and gaming activities (whether from the broadcast stream or from a stand-alone interactive service) will be included.
- 1.18 Ofcom also proposes that Relevant Turnover should replace Qualifying Revenue as one of the components for assessing obligations under the Code on Television Access Services.

### **Collection of Revenue Data**

- 1.19 Following on from responses received from stakeholders, Ofcom has decided to use revenue data from the last but one calendar year's revenues. Therefore the relevant revenue data for fees payable in 2005/6 will be those for the calendar year ended 31 December 2003.
- 1.20 It is proposed that the changes to the definition of Relevant Turnover will be introduced for the charging year 2005/6 with the exception of the Television Sector, where the inclusion of interactive, betting and gaming revenues will be delayed until tariffs are set for 2006/7 based on 2004 calendar year revenues. Therefore, in general, Ofcom will not require licence holders (or those who pay administrative charges) to resubmit their revenue data for 2003.
- 1.21 However, licensees who are also television platform operators and retail their own channels will be required to resubmit their 2003 subscription revenue data. Since any reduction in revenues by moving from retail to wholesale subscription revenues will tend to reduce the licence fees paid, we do not consider this an undue administrative burden.

## Tariff Structure

### Television

- 1.22 Ofcom proposes to introduce a simpler tariff table for television licensees that removes the distortions caused by the caps set previously by ITC. Ofcom will also introduce a consistent set of tariffs for Public Service Broadcasting (“PSB”) which are platform neutral, rather than having different tariffs which depend on the type of platform the PSB channel is broadcast on.
- 1.23 Ofcom also proposes to modify the tariff structure to reflect market developments. This involves reducing the maximum revenue ceiling beyond which the tariff rate is set to zero, from £400m to £300m and implementing less progressive tariffs than is currently the case.
- 1.24 To ensure consistency across the Broadcasting sector, Ofcom proposes to use transitional relief for the migration of television licence fees onto the new tariff basis, where proposed changes to the tariff structure would produce a significant impact on any individual licensee.

### Radio

- 1.25 In the radio sector, the fees for new licence applications do not currently cover the costs of granting new licences and the difference has hitherto been met by the fees from existing licensees. Ofcom proposes to rebalance this so that income from application fees more closely relates to the cost of granting new licences. Application fees will therefore rise but there will be a corresponding reduction in ongoing licence fees, better reflecting the actual costs of applications.
- 1.26 Ofcom also proposes to change the definition of Relevant Turnover in the Radio sector from being based on Qualifying Revenue, as defined in the 1990 Broadcasting Act, to a new non-statutory definition as set out in Annex 2 of this document. A progressive tariff structure is also proposed. In the interests of simplicity, Ofcom proposes that licensees whose annual fees would be £100 or less, will not be charged (that is, their tariff rate will be set at zero per cent).
- 1.27 Finally, Ofcom proposes to allow a period of transitional relief for the migration of 2004/5 tariffs onto the proposed new tariffs where changes to the tariff structure would produce a major impact in the fees for an individual licensee.

### Networks & Services

- 1.28 In the networks and services sector, Ofcom has analysed the possibility of deducting wholesale costs from Relevant Turnover, but considers that the benefit of this change is outweighed by its complexity, administrative cost and difficulty of verification. Ofcom therefore proposes no alteration to the structure of existing tariffs. Ofcom intends to publish a list of those providers of networks and services whom it considers to be liable to pay administrative charges.

## **Start-up Loan**

1.29 Ofcom has considered whether individual stakeholders should be able to elect to pay their share of the Government loan in a lump sum rather than spread over five years. To do so, however, would require a forecast of that stakeholder's likely Relevant Turnover over the next five years. More important than the administrative complexity is the risk that this forecast could prove to be significantly adrift, which could bear inequitably on other stakeholders. Ofcom does not, therefore, propose to allow elective lump sum repayments of the start-up loan.

## **Notice of Designation under Section 38 and 34 of the Communications Act 2003**

1.30 Under section 38 of the Act, Ofcom can only charge those providers of electronic communication networks, services or associated facilities of a description that have been designated. Ofcom's draft designation is produced as Chapter 8 of this document and Ofcom welcomes comments on this notice of designation.

## **Relevant Activity guidelines**

1.31 Ofcom has taken this opportunity to amend Oftel's guidelines "The definition of "relevant activity" for the purposes of administrative charges" dated 29 July 2003, primarily to clarify how it will interpret public electronic communication services to end-users.

1.32 The guidelines, including Ofcom's amendments are set out at section 9 of this document. Ofcom welcomes comments on the guidelines and Ofcom's amendments in this consultation.

1.33 Without fettering its discretion, Ofcom is proposing to normally expect to follow the guidelines in determining what is a relevant activity for the purposes of administrative charges.

## **Responding to this consultation**

1.34 The consultation seeks views on the draft Statement of Charging Principles that Ofcom will apply to the continued setting of licence fees and administrative charges for 2005/6 and beyond. This is contained within Chapter 7 of this document. In arriving at this draft Statement of Charging Principles, Ofcom has taken the views of its stakeholders into consideration and is therefore seeking comments on matters which have not already been covered by the previous two consultations on this issue, and points on the drafting of the draft Statement of Charging Principles, the definitions contained within Annex 1 and 2 and the draft Designation under sections 38 and 34 of the Act.

1.35 It is now seeking comments on:

- matters which have not already been covered by the previous two consultations on Charging Principles;
- points on the drafting of the draft Statement of Charging Principles;

- the definitions contained within Annex 1 and 2;
- the draft Designation under sections 38 and 34 of the Act at section 8; and
- the draft Relevant Activity guidelines at section 9.

1.36 Views and comments on any of the matters raised in this document should be made in writing by 17 January 2005 to:

Rex Warner  
Head of External Finance  
Ofcom  
Riverside House  
2a Southwark Bridge Road  
London SE1 9HA  
E-mail: [rex.warner@Ofcom.org.uk](mailto:rex.warner@Ofcom.org.uk)  
Tel: 020 7981 3483  
Fax: 020 7981 3630

1.37 Ofcom is allowing six weeks for responses which, although less than the standard period set out in Ofcom's consultation principles, is considered sufficient considering the responses received already regarding this issue.



# Background and Introduction

## Background

- 2.1 Under the Communications Act 2003 (“the Act”), Ofcom is required to consult on and subsequently publish a statement of charging principles before it can set licence fees and administration charges in the broadcasting and networks & services sectors. Ofcom is required to set these charges so as to recover its costs of regulating those sectors within Ofcom’s financial year, which runs from 1st April to 31 March (“Charging year”).
- 2.2 Ofcom published a consultation on its Charging Principles in February 2004 and subsequently published the Statement of Charging Principles on 31 March 2004, setting out its tariffs for Ofcom’s first financial year ending 31 March 2005. Given the necessarily short period of this initial consultation, due to the vesting of Ofcom taking place on 29 December 2003 and the need to publish its Statement of Charging Principles prior to setting tariffs for the financial year, a number of stakeholders raised issues that they felt were not adequately addressed. In response to these issues, Ofcom therefore published a second consultation in July 2004.
- 2.3 Following the responses to this consultation, which we have carefully considered, we are now publishing this document which comprises five elements:
- A description of the rationale underlying the draft Statement of Charging Principles;
  - A draft of the Statement of Charging Principles, setting out the form that Ofcom currently proposes its final statement of charging principles to take;
  - A draft notice of designation under sections 38 and 34 of the Act 2003;
  - Draft guidelines on Relevant Activity for the purposes of administrative charges; and
  - Annexes 1 and 2 setting out Ofcom’s new definition of Relevant Turnover for the Television and Radio sectors.

## Ofcom’s funding

- 2.4 Ofcom is funded from several different sources. Licence fees and administrative charges are used to regulate the TV, radio and network and services sectors. The full range of Ofcom’s funds and use of those funds is provided below:

<b>Source of Funds</b>	<b>Use of funds</b>
Grant in Aid from DTI	Spectrum Management Spectrum Efficiency Scheme The Statutory public interest test for media mergers Competition Act responsibilities
Grant in Aid from the DCMS	Media Literacy Community Radio Fund

Radio Licence Fees	Regulation of radio broadcasting
Television Licence Fees	Regulation of TV broadcasting
Networks & Service Administration Charges	Regulation of electronic communications networks & services sector
Radio Licence Application Fees	Processing applications for radio licences under the Broadcasting Act
Television Licence Application Fees	Processing applications for TV licences under the Broadcasting Act
Electronic Communications Code Charges	Administration of the code
BBC / S4C fees	Regulation of BBC and S4C
Other licence related fees	E.g. fees for applying for renewal of financial terms of Channel 3 and 5 and Teletext licences
Other income (e.g. property rental income)	Apportioned to all sectors above

2.5 The setting of spectrum licence fees falls outside the scope of this draft statement and the process for setting these fees will continue to be determined by the principles set out in the Wireless Telegraphy Acts 1949 and 1998.

2.6 In each financial year, Ofcom is required to balance its expenditure with its income. In doing so, Ofcom is required by the Act to raise income from each of the sectors it regulates to cover the costs of regulating each sector together with a proper apportionment of Ofcom's 'common costs'. Ofcom sets out its principles for cost allocation within the draft Statement of Charging Principles in Chapter 7.

2.7 In addition to the recovery of its ongoing regulatory costs, Ofcom is also required to recover the start-up loan, which it has fairly allocated across each of the sectors it regulates. This is described in more detail in Chapter 7.

## **BBC and S4C**

2.8 Fees paid to Ofcom by the BBC and S4C to cover the relevant cost of regulating these bodies are subject to a different regime set out in the Act and are therefore also outside the scope of this draft statement. However, Ofcom has based its calculation of the amount of fees payable by the BBC and S4C on the same methodology as each of the regulated sectors i.e. by reference to the cost of regulation of that sector together with an apportionment of Ofcom's common costs and start up loan. In calculating the costs attributable to the regulation of the BBC and S4C, they have each been treated as if they are a sector in their own right. However, in general, Ofcom does not calculate the costs of regulation of any one stakeholder separately from other stakeholders in the same sector.

## Document framework

2.9 This rest of this document is set out in the following way:

**Section 3** sets out the general principles that Ofcom will take into account when setting tariffs to recover the costs of regulating each of the relevant sectors. This section also considers the generic issues that apply to all of the relevant sectors, such as payment terms and under/over recovery of fees;

**Sections 4, 5 and 6** consider the application of these general principles to each of the relevant regulatory sectors: Television; Radio; and Networks and Services respectively, and the issues particular to each of these sectors;

**Section 7** provides a draft final statement of charging principles;

**Section 8** provides a draft notice of designation under sections 38 and 34 of the Communications Act 2003;

**Section 9** provides guidance on Relevant Activity in the Networks and Services sector for the purpose of administrative charges; and

**Section 10** provides guidance on responding to this consultation

**Annex 1** provides the definitions of Relevant Turnover for the Television Sector and guidance on how Relevant Turnover is to be calculated by licensees;

**Annex 2** provides the definitions of Relevant Turnover for the Radio Sector and guidance on how Relevant Turnover is to be calculated by licensees;

**Annex 3** provides Ofcom's consultation principles; and

**Annex 4** Consultation response cover sheet

## Key future dates

2.10 The table below sets out the key dates in the process for Ofcom in publishing its final Statement of Charging Principles, which it is intended will remain in place for the foreseeable future. Additionally, the timetable sets out the dates for setting of tariffs for the 2005/6 financial year.

**Table 1 Key dates during tariff setting process**

Date	Action
December 2004	Publish Draft Statement of Charging Principles
January 2005	Publish Draft Ofcom Business Plan
February 2005	Publish Final Statement of Charging Principles
31 <sup>st</sup> March 2005	Publish tariff tables for 2005/6 based upon 2003 calendar year revenues

## General charging principles

- 3.1 This section sets out the general principles that Ofcom will take into account when setting tariffs, taking into consideration responses from stakeholders. This section also considers the generic issues that apply to all of the relevant sectors. Issues particular to one or other of the relevant sectors are considered in more detail in subsequent sections.

### Basic framework and methodology

- 3.2 Ofcom is required to set licence fees and administrative charges in order to support the cost of its regulatory activities. It is further required to split these costs between the sectors it regulates, apportioning the cost of regulation to each of the relevant sectors.
- 3.3 To meet these requirements Ofcom must allocate its regulatory costs to each of the relevant sectors, outline the basis for setting tariffs for each of the relevant sectors and where necessary, identify distinct regulatory categories within each of the regulatory sectors. In doing so Ofcom must ensure that the relationship between the cost of regulation and the level of charges is transparent and that the tariffs are justifiable and proportionate.
- 3.4 In order to calculate the tariff applicable for each sector, in addition to using forecast costs for the Charging Year, Ofcom will estimate the under/over recovery from the previous charging year's licence fees and administrative charges in relation to estimated Ofcom costs for that year. Details of the under/over recovery and the tariffs will be provided in the tariff table published on the 31 March of the preceding charging year.
- 3.5 Once the actual results for the year are known and the level of actual under/over recovery by sector, the amount of money to be collected from each sector will be adjusted where necessary. This will be reflected in the adjustment of under / over recovery at the end of each charging year which will impact the following year's charges.

### Cost allocation

- 3.6 Ofcom is required by the Act to raise income from each of the sectors it regulates to cover the costs incurred in regulating each sector. This means that there needs to be an apportionment of Ofcom's costs between each of the Regulatory Sectors. The process of cost apportionment is described in four key steps below:

Step 1: Ofcom decides its key strategic priorities for the following year.

Step 2: In order to meet the strategy, Ofcom identifies the resources necessary for specific projects and ongoing regulatory activities as part of its budgeting process.

Step 3: The costs of these projects and activities are allocated to regulated sectors and where applicable, categories within those sectors (for example, within television, where Category A represents PSB licences, Category B represents cable and satellite and so forth).

Step 4: Common costs and overheads, not included in specific projects, are allocated to sectors (or categories) on a proportionate basis.

- 3.7 Where particular regulatory activities, functions or overhead costs are common across more than one of the regulatory sectors or categories, Ofcom will apportion costs according to the most suitable cost driver, for example, the time spent by Ofcom staff.

### Broad tariff principles

- 3.8 In setting tariffs Ofcom's prime objective is the effective collection of its funding requirements with the minimum administrative burden on stakeholders in a fair and equitable manner. It is also important that the tariff structure does not create incentives for regulated businesses that conflict with broad objectives of regulatory policy.

- 3.9 To achieve these objectives Ofcom intends to achieve the following criteria when setting administrative charges and licence fees:

- **Fairness.** The tariff structure should raise Ofcom's required funding across the regulated sectors in a manner that is equitable;
- **Cost-reflectiveness.** Charges should broadly reflect the underlying cost of regulating each category of stakeholder;
- **Reliability.** The tariff base needs to be stable over time, and not prone to erratic movements. Charges should not move substantially in any one year;
- **Simplicity.** The calculation of charges should be as simple as possible, wherever practicable using data that stakeholders would anyway gather for their own management purposes; and be relatively simple to administer for Ofcom;
- **Be easily verified.** Information required for the setting of charges should be easily verifiable to ensure industry-wide compliance;
- **Adaptable.** Tariff principles and structures should be able to adapt to a changing market environment and be consistent with wider policy; and
- **Relevance.** Charges should cover in full an operator's activities that flow from the licence or authorisation, but only those activities.

- 3.10 Ofcom asked the question (1) "Are Ofcom's proposed criteria for designing the tariff structure appropriate?"

### Response from stakeholders

- 3.11 Ofcom received 10 responses from stakeholders to this question; all agreed with the criteria set out by Ofcom. However, one respondent (a shopping channel) also suggested considering any recent shifts in "regulatory architecture" to better reflect the extent of Ofcom's regulatory activity in a particular sector.

### Ofcom's response

- 3.12 Ofcom will use the criteria set out above to design tariff structures in order to comply with the Communications Act and provide a predictable and fair basis of setting fees and administrative charges. This is demonstrated by the fact that

as the regulation of teleshopping channels has shifted to the Advertising Standards Authority (“ASA”), Ofcom has adapted its tariff structure, and hence its charges, accordingly.

### **The use of Relevant Turnover for the purpose of setting tariffs.**

- 3.13 Ofcom proposed to use Relevant Turnover as the basis of setting tariffs, because it best complies with Ofcom’s fundamental tariff principle to apportion the costs of regulation across stakeholders in a fair and equitable manner with the minimum administrative burden.
- 3.14 Ofcom asked the question (2) “Do you agree with Ofcom’s view that revenue should be the basis of setting tariffs? If not, which alternatives would you prefer and why?”

### **Response from stakeholders**

- 3.15 The majority of respondents from across all of the regulatory sectors agreed with Ofcom that a revenue measure was the most appropriate basis on which to set tariffs. One respondent suggested however that a minimum fee should apply to all licensees. One respondent noted that a fixed fee should be set for multiplex operators. GMG suggested that a profitability measure should also be factored into the calculation to encourage licensees to invest in programme and service development. GMTV questioned the appropriateness of a revenue measure for broadcasters that have limited periods of broadcasting.
- 3.16 One respondent disagreed with Ofcom, arguing in favour of an audience measure.

### **Ofcom’s response**

- 3.17 Following consultation, Ofcom believes that a revenue basis best meets the criteria set out above because: it can be applied consistently across the three regulated sectors; it is relatively stable over time; it is more easily verifiable than several alternative options and is adaptable to changes in the market. Profitability is not a good measure for the purposes of apportioning Ofcom’s costs amongst stakeholders as inconsistent accounting treatment of stakeholders’ different business models would lead to inequitable licence fees and charges.
- 3.18 Ofcom intends to use the concept of ‘Relevant Turnover’ in determining which revenues should be assessed in setting charges. The application of Relevant Turnover to each of the regulated sectors is described in detail in each of the sector specific sections below. The full definition of Relevant Turnover in respect of each of the regulated sectors is set out in Annexes 1 and 2 to this document.
- 3.19 In most cases, Relevant Turnover is adaptable to different business models, for example, limited periods of broadcasting but in some cases Relevant Turnover might be inappropriate, for example, new applications for a licence or request for communications code powers. In such cases Ofcom intends to set a fixed cash sum in order to recover its associated costs. Additionally, Ofcom charges a minimum fee for most licences, where appropriate and practical, in order to cover its costs in relation to those licences.

## Tariff Structures

- 3.20 In the July consultation document Ofcom analysed the advantages and disadvantages of various tariff characteristics and welcomed comments on its proposed tariff structures.
- 3.21 Ofcom asked the question (3) “Do you agree with Ofcom’s general approach to tariff structures? If not, are there any other tariff structures that Ofcom has not considered? Do you agree that there should be mild progression within Ofcom’s tariff structure?”

## Response from stakeholders

- 3.22 A substantial number of respondents agreed with Ofcom’s general approach. One respondent highlighted some inconsistency in application of general principles across the regulatory sectors. In particular one respondent commented that the level of disaggregation within the regulatory sectors was significantly different with TV being highly segregated but Networks and Service being hardly segregated. This respondent requested that Ofcom consider further disaggregation of the Networks and Services sector, and suggested a split between fixed and mobile operators. The same respondent also suggested that a maximum revenue threshold be set for the Networks and Service sector and proposed removal of the present banding structure which it considered has a distorting effect.
- 3.23 SMG disagreed with the level of progressivity inherent with the tariff structure and suggested that this should be limited. One respondent shared this view and argued that there is no justification for progressive tariffs. In its response another respondent also argued against progressivity, and commented that it is not necessarily true to suggest that larger operators tend to be more profitable and should therefore contribute proportionality more to the cost of regulation than smaller operators. One respondent argued that progressivity penalises successful companies and suggest that Ofcom explore alternative tariff structures. One respondent suggested that a flat rate percentage should be calculated and that the current maximum revenue ceiling for the TV sector should be removed altogether.

## Ofcom’s response

- 3.24 Ofcom considers the networks and services sector to be broadly homogenous in terms of its regulatory activities (in contrast to the television sector), and does not want to sub-divide sectors where it is not strictly necessary.
- 3.25 Ofcom appreciates that there is a tension between strict cost causality and fairness and wider regulatory objectives. Having considered the views put forward by stakeholders, Ofcom considers that a mild degree of progressivity does effectively balance these objectives.

## Regulatory Categories

- 3.26 Separate and identifiable regulatory activities are usually, but not always, defined by different classes of licence or authorisation. Ofcom has identified a number of distinct regulatory categories within each Regulatory Sector, and as

the regulatory costs relating to these services differ it is appropriate that different tariffs also apply (by category). Further explanation of regulatory categories and how they fit within the overall framework is provided in the sector specific sections of this document.

### **Over or Under Recovery of Spend**

3.27 Any estimated over or under recovery of expenditure is carried forward to the next Charging Year on a Regulated Sector basis. The forecast of the under or over recovery by Regulatory Sector within 2004/5 will be updated immediately prior to the setting of the licence fee tariffs for 2005/6 and will be taken into account in the setting of those tariffs. Any under or over recovery of fees in the prior charging year will be published in the tariff table.

### **Payment of Fees**

3.28 It has become apparent to Ofcom that the level at which monthly payment is allowed is inefficient and burdensome for Ofcom resulting in large numbers of relatively small invoices. Therefore, Ofcom proposes to increase the level at which monthly payment is allowed.

3.29 Ofcom's funding requirements are expected to fall fairly evenly over the year. Monthly payment of all licence fees above £75,000 will apply to networks and services and television licensees. Ofcom has decided that a lower limit of £5,000 for monthly payments will apply to radio licensees to match the level of regulatory fees to revenues for smaller licensees.

3.30 Responding to responses received from stakeholders, Ofcom has decided to use revenue data based on the last but one calendar year's revenues to set tariffs so as to collect aggregate amount of fees that are required for the financial year to meet the cost of Ofcom's regulatory functions. The change from the July proposals to using the revenue data from the last but one calendar year was made to reflect the administrative concerns of stakeholders who felt that the limited time period between the end of the calendar year and data collection for that year would make it difficult to supply the information requested. There were also concerns expressed about the supply of unaudited data to Ofcom as the basis for setting tariffs and administrative charges.

### **Transparency**

3.31 Ofcom has a duty under sections 38 and 347 of the Act to publish for each Charging Year statements relating to the income and expenditure for each sector. These statements will be included in Ofcom's annual report and accounts and will be subject to audit by Ofcom's auditors, the National Audit Office. Ofcom will publish data, at the summary levels described in the business plan, on the costs of activities carried out, and on the allocation of these costs by Regulatory Sector. This data will be updated, where appropriate, in the published tariff tables.



# Application of principles to the Television Sector

## Summary of Proposals consulted upon

4.1 The key issues that Ofcom consulted upon were:

- The introduction of a new definition of Relevant Turnover. This included whether to take account of Additional Payments and differences in the cost structure between licensees;
- Changes to the tariff structure;
- Reduction of the degree of progression in Television tariffs;
- Reduction of the maximum revenue ceiling from £400m to £300m;
- Introduction of a flat fee for digital multiplexes; and
- Whether any transitional arrangements should be made to migrate from the existing tariffs to the new tariff structure.

4.2 Additionally, Ofcom has considered the basic principle of setting tariffs based on licensed activity only and, therefore, basing licence fees wherever possible on wholesale rather than retail subscription revenues.

4.3 In view of the complexity of the changes proposed in this area, Ofcom has also considered whether all the changes should be implemented immediately or whether, exceptionally, the inclusion of some new elements of turnover should be deferred until the setting of 2006/07 tariffs – meaning that the relevant turnover data will be collected for the first time in respect of calendar year 2004.

## Relevant Turnover

4.4 Ofcom proposed to introduce a separate definition of “Relevant Turnover” for tariff-setting purposes in order to better reflect the range of services now provided under television licences, and to ensure that only revenue from activities which are licensed is included.

4.5 Ofcom asked the question (5) “Do you agree with Ofcom’s proposal to allow retail revenues to be deducted when calculating subscription revenues where the licensee is also the retailer of the service?”

## Response from stakeholders

4.6 Several respondents sought clarification of what revenues constitute “retail revenues” and requested that Ofcom issue guidance for stakeholders on this issue.

- 4.7 Two respondents disagreed with Ofcom's proposals. In particular one of them argued that the proposal unduly advantages vertically integrated business by allowing a significant portion of their revenues to be omitted from the calculation of relevant turnover.
- 4.8 One respondent considered that this causes distortion between (a) channels that retail their own subscription services, allowing a reduction in their relevant turnover to account for the 'retail' and therefore unlicensed service and (b) shopping channels that have their gross sales revenue with no reduction in the calculation for relevant turnover.

### **Ofcom's response**

- 4.9 It is a basic principle in setting tariffs that the charges should cover activities that flow from the licence or authorisation, but only those activities. Ofcom does not license the activities associated with the provision of a television platform or the retailing of packages of channels to subscribers. Accordingly, as a general rule, licence fees will be based on wholesale rather than retail subscription revenues.
- 4.10 For similar reasons, the definition of Relevant Turnover in Television will for example, exclude betting and gaming revenues earned from gaming activities in respect of which the relevant person has a Gaming Act licence. However, Relevant Turnover will include revenues earned by broadcasters in respect of the granting of access to such betting and gaming activities from the broadcast stream.
- 4.11 Details of the proposed definition of Relevant Turnover together with detailed guidelines are provided in Annex 1 of the document.
- 4.12 Ofcom asked the question (6) "Do you agree with Ofcom's proposed definition of Relevant Turnover in the television sector?"
- 4.13 The majority of respondents agree with the proposed definition. One of the respondents however suggests that Ofcom keeps the revenue measure under review as it may not remain the most appropriate measure going forwards. It also suggests Ofcom monitors tariff levels between PSBs and non-PSBs to ensure ratio between the two remains appropriate and proportionate to the regulatory cost generated by regulating each category. One of the respondents also seeks clarification of exactly what "goods and services" are covered by the proposed definition and how the value should be calculated by the licensee.
- 4.14 Responses from the teleshopping channels noted that with the transfer of regulatory functions to the Advertising Standards Authority ("ASA"), Ofcom's regulatory role vis-à-vis teleshopping channels would diminish and that Ofcom's proposals could lead to teleshopping channels being charged twice for the cost of regulation. Ofcom should ensure that there is no double charging by Ofcom for regulatory activities that have been transferred to the ASA.

## Ofcom's response

- 4.15 Ofcom accepts the arguments advanced by Teleshopping channels that they should not have to pay twice for their regulation. On November 1st 2004, responsibility for the regulation of advertising and teleshopping channels passed from Ofcom to the Advertising Standards Authority ("ASA"). The ASA will fund its activities by a levy raised by the Advertising Standards Board of Finance ("ASBOF") and payable on advertising and teleshopping revenues.
- 4.16 Ofcom retains responsibility for the licensing of teleshopping channels, and for any subsequent licence based issues that may arise, particularly in relation to issues arising out of the Television Without Frontiers Directive. Ofcom may also be called upon by the ASA to impose statutory sanctions on teleshopping channels, in cases of extreme breaches of licence conditions.
- 4.17 Since the entire content of teleshopping channels is treated and regulated as advertising, Ofcom considers that retail revenues should be excluded from the definitions of Relevant Turnover in order to avoid charging teleshopping channels twice. However, Ofcom proposes to charge teleshopping channels a fixed annual licence fee to cover the costs of the backstop and residual powers that Ofcom has retained. This fixed fee will be equal to the minimum applicable television licence fee.
- 4.18 As technology develops and services evolve, the definition of Relevant Turnover can be easily updated so that tariffs do not unfairly discriminate between operators who chose different business models. These business models should be a matter of market choice for the operators and not influenced by Ofcom's tariff structures. Additionally, recent innovations in the provision of services, such as interactive services and premium rate telephone services ("PRTS") to earn revenue are not expressly covered by the statutory definition of Qualifying Revenue but are clearly revenues derived from the possession of a broadcast licence.
- 4.19 Accordingly the definition of Relevant Turnover will include all revenues earned from the possession of a broadcast licence to avoid discriminating between operators' different business models.
- 4.20 Ofcom's proposed definition will include all revenues attributable to the licensed service. This includes advertising revenues, sponsorship revenues, subscription and pay-per-view revenues (based as a general rule on wholesale prices) and interactive revenues attributable to the licence (for example betting and gaming services, PRTS, and interactive advertising). Annex 1 provides Ofcom's proposed definition of Relevant Turnover as it applies to the television sector in greater detail and also includes detailed guidance notes on how the definition is to be applied. Ofcom is seeking licensees' views on both the definition and the detailed guidance notes.

## Additional payments

- 4.21 A key difference between Channel 4 and the other PSB licensees is that Channel 3, Channel 5 and the Public Teletext licensee make Additional Payments to HM Treasury.
- 4.22 During 2005, Ofcom will be setting the terms of the replacement digital licences for all analogue television services. If reviews are requested by licensees,

Ofcom will determine a new cash bid and a new PQR. Ofcom's licence fees will be a deductible cost for the purpose of valuing the licences and setting new Additional Payments.

- 4.23 Ofcom proposed not to allow the deduction of Additional Payments in the assessment of Relevant Turnover for the purpose of setting licence fees as they reflect an economic rent extracted by the government and were set assuming Ofcom's existing licence fees. Ofcom's tariffs are an operating cost for licence holders (i.e. Ofcom's fees are a deductible item in the process of setting Additional Payments). To allow Additional Payments in turn to be a deductible item for the purposes of setting Ofcom's fees would be unfair to other licensees.
- 4.24 Ofcom asked the question (7) "Do you agree with Ofcom's view that Additional Payments should not be subtracted from Relevant Turnover for the purpose of setting television tariffs?"

### **Response from stakeholders**

- 4.25 Ofcom received four responses to this question. Three respondents agreed with Ofcom that additional payments should not be subtracted in the calculation of relevant turnover.
- 4.26 SMG disagreed with the proposals, believing that additional payments should be deducted as they are deducted directly from revenues and represent a commercial disadvantage to the operators that must make these payments.

### **Ofcom's response on additional payments**

- 4.27 For the reasons given above, Additional Payments will not be a deductible item from Relevant Turnover for the purpose of setting television tariffs.

### **Proposed tariff structure**

- 4.28 Ofcom proposed to simplify the tariff structure in the television sector which was inherited from the ITC and which has been rolled forward for two years using a cap on the increase in fees in relation to the previous year's licence fees. If the 2004/5 tariffs were applied in 2004/5 without the cap, Ofcom would raise an amount substantially in excess of Ofcom's funding needs from the television sector. Therefore, to ensure the appropriate level of licence fees is recovered from the sector and that increases across the sector are proportionate, a capped increase of 32% has been applied in 2004/5.
- 4.29 The use of caps on the increases in licence fees has resulted in some anomalies. The profile of growth in revenues for licensees has varied over the period of the licence fee caps, with some faster growing licensees and other slower growing licensees. Furthermore, the migration of analogue revenues to TLCS (formally STS) licences has not been even across Category A licences. This means that after two years of implementing licence fee caps some faster growing licensees are paying proportionally less than slower growing licensees.
- 4.30 In future years it is Ofcom's intention that the tariff table should generate the required level of revenue without the need for such a cap. This will remove the

problems created when using caps and will make the application of the tariff table significantly simpler.

4.31 Furthermore, Ofcom proposed a number of changes to the structure of television tariffs.

- setting separate tariffs for PSB and non-PSB revenues;
- reducing the upper revenue ceiling to £300m beyond which the tariff is set to zero; and
- reducing the degree of progression built into the existing 2004/5 tariffs.

### PSB revenue basis for tariff setting

4.32 Ofcom’s existing categorisation for the purpose of setting tariffs involves three regulatory categories for television, Categories A, B & C. The current categories for each type of television licence are presented below:

**Table 6 Existing television licence categories**

Licence Category Description	Total in Issue	Tariff Category
Channel 3	16	A
Channel 4	1	A
Channel 5	1	A
Commercial Additional Service	3	B
Digital Television Addition Service	21	B
Digital Television Programme Service	33	B
Digital Terrestrial Multiplex Service	5	A
Public Teletext Service	1	A
Restricted Television Services Licence	19	C
Television Licensable Content Service (TLCS)	561	B
Total	661	

**Source: Ofcom**

4.33 Currently TLCS licences held by both PSB and non-PSB broadcasters are included under Category B. However the cost of regulating PSB is very largely platform independent. To reflect these differences Ofcom proposes to split category B between PSB and non-PSB, with different tariffs for each. This means that the PSB licensees (C3, C4, C5, etc) will pay the same tariff rate on their revenues irrespective of the platform that the revenues were generated on. Other Category B licensees will pay the lower tariff for non-PSB revenues to reflect the lower costs of non-PSB regulation.

## Reducing the maximum revenue ceiling

- 4.34 The original television tariff structure was developed by the ITC before the fragmentation of viewing shares between alternative distribution platforms such as analogue terrestrial, DTT, satellite and cable. It contained a £400m maximum revenue ceiling, beyond which the tariff was set to zero. This was designed to mitigate some of the distortion caused when comparing the licence fees of single channel licensees with multiple licensees associated with a single channel. Without the maximum ceiling, single channel licensees would pay significantly higher proportionate licence fees than licensees who share a channel and who collectively gain more from the progressive nature of the tariff.
- 4.35 As a consequence of the migration of television revenues away from analogue licences, falling analogue revenues have rendered this £400m maximum revenue ceiling less effective. Ofcom therefore proposed to reduce the maximum revenue ceiling to £300m.

## Reducing the degree of progression within television tariffs

- 4.36 The original television tariff structure was also developed by the ITC before the significant concentration in licence ownership that has recently occurred. Ofcom therefore reviewed the degree of progression and proposes to implement less progressive tariffs than the existing 2004/5 tariffs (and that are also broadly consistent with the tariff structure proposed for the radio sector).
- 4.37 Ofcom asked the question (8) “Do you agree with Ofcom’s proposed structural changes for television tariffs?”

## Response from stakeholders

- 4.38 Channel 4 agreed with the proposed changes, considers that mild progression in television tariffs is appropriate and welcomes the reduction of the maximum ceiling.
- 4.39 SMG disagreed that the proposed tariff structure is fair and equitable. In particular SMG believe it is unfair effectively to charge all relevant turnover of PSB broadcasters against the Category A tariff. They understand the argument of platform neutrality extended by Ofcom but do not believe this introduces fairness in relation to cost allocation between PSB broadcasters and non-PSB broadcasters.
- 4.40 Several respondents commented that removal of the 32% cap on tariff increases is contrary to Ofcom’s stated principle of fairness and equitability. One respondent also argued that the cap is necessary to ensure continued service development and innovation.
- 4.41 Three respondents questioned the justification for reducing the maximum ceiling above which the tariff is set to zero. Reducing the ceiling is not in accordance with Ofcom’s stated principle of cost-reflectiveness and appears designed to favour a single licensee. One respondent also argued for a minimum £5,000 fee to be introduced to ensure that all licensees contribute to the cost of regulating the sector. One of the respondents noted that PSB broadcasters will meet 75% of cost of regulating the TV sector.

- 4.42 One respondent sought clarity on where digital radio services and TV services on 'Freeview' fit within the tariff structure.

### **Ofcom's response**

- 4.43 The reduction in the £400m ceiling to £300m does benefit only licensees whose revenue from a single licence exceeds £300m, but this has been done to mirror the reduction in revenues in Category A licences. Without this shift the migration of analogue to digital revenues would have a disproportionate impact on different licensees' tariff payments.
- 4.44 Ofcom has decided to apply the same tariff to all PSB revenues, regardless of the platform over which the revenues are generated. A different tariff is applied to non-PSB revenues and this is in line with Ofcom's broad tariff principles to reflect the underlying cost of regulating each category.
- 4.45 The main costs of regulating the television sector under the Communications Act 2003 are related to PSB requirements. As a result, PSB broadcasters meet a larger portion of Ofcom's costs of regulating the television sector.
- 4.46 The revenue from each licence will either attract a PSB-based tariff or a non-PSB based tariff. So, for instance, a non-PSB service on the Freeview platform with a Digital Television Programme service licence will make tariff payments based upon the Category B tariff rate. A PSB service will pay at the Category A tariff rate on revenues earned from each separate licence, currently analogue licences and TLCS and DTPS licences

### **Minimum fees and application fees**

- 4.47 Ofcom has reviewed its costs of administering and processing applications for television licences and has found that applications fees need to increase to fully cover these costs. Additionally, the cost of administering licences has also risen and therefore the minimum fee needs to increase. The suggested minimum fee is £1,000 with effect from 1 April 2005 and will be kept under review thereafter. It is proposed that application fees will also rise to £2,500 with effect from 1 April 2005.

### **Digital multiplexes**

- 4.48 Digital multiplex service licences provide access to a scarce resource on a platform that is central to the future of terrestrial television broadcasting in the UK. However the current revenue definitions are not suited to revenues from the transmission of channels, especially given the variety in business models of multiplex operators (i.e. integrated broadcasters do not record transmission revenue separately). Furthermore, digital multiplex service licences do not attract the content regulation of PSB services. Ofcom therefore proposed an alternative approach for setting tariffs for the digital multiplex service licences which involves moving them out of Category A into a new, separate Category D.
- 4.49 The multiplex service licences are analogous to the national digital radio multiplex licence. Ofcom proposed to set the same £10,000 fee for each

television multiplex service licence but intends to keep this under review as the amount of work in this area increases over the next few years.

- 4.50 Ofcom asked the question (9) “Do you agree with Ofcom’s view that television multiplex service licences should be moved to a new Category of licence? Is £10,000 an appropriate annual fee?”

### **Response from stakeholders**

- 4.51 All respondents to this question agreed with Ofcom’s proposal to re-categorise television multiplex service licences, however two respondents suggest that the annual fee is calculated based on commercial revenue attributable to each multiplex.
- 4.52 Three respondents agreed that proposed £10,000 fixed fee is reasonable, one respondent however considers this to be too low and suggests a figure nearer £250,000 per multiplex. One respondent suggested the introduction of a 2 year deferral on the applicability of fees for new multiplex operators.

### **Ofcom’s response**

- 4.53 It is conceptually problematic to establish the appropriate revenue of multiplex licensees. However, in realising that there is a regulatory cost associated with digital multiplexes, which is largely independent of their business model, for instance a portion of the cost of overseeing digital switchover, Ofcom has decided that the best way to recover this cost is through a flat fee of £10,000. The level of the fee will be kept under review.
- 4.54 As the proposed £10,000 fee is due to a change in category, and multiplex operators typically paid the minimum fee in the past, Ofcom does not propose to allow transitional relief in this case when this new fee results in a large percentage increase in the tariff payable.

### **Shopping Channels**

- 4.55 As the regulation of shopping channels will now fall under the Advertising Standards Authority (“ASA”), Ofcom has decided that a new category of licence is required for shopping channels (Category E). A flat rate fee will be charged for these licences to cover the costs of Ofcom’s residual regulatory duties.

### **Code on Television Access Services**

- 4.56 The Code on Television Access Services uses qualifying revenue as one factor in assessing the ability of licensees to afford to pay for television access services (subtitling, signing and audio description). Ofcom considers that it would be appropriate to replace Qualifying Revenue with Relevant Turnover when this data is available.
- 4.57 Ofcom asked the question (10) “Do you agree with Ofcom’s view that, for the purposes of assessing obligations under the Code on television access services, qualifying revenue should be replaced by relevant turnover?”



## **Response from stakeholders**

4.58 All respondents agreed with Ofcom's proposal, although one commented that affordability should also be used in the assessment of obligations under the Code.

## **Ofcom's response**

4.59 Ofcom intends to use Relevant Turnover as the basis of assessing licensees' ability to pay for television access services.

## **Transitional arrangements**

4.60 Ofcom intends to use transitional arrangements only when they are strictly necessary and where the benefits outweigh the administrative complexity. As a general guideline Ofcom proposes to use transitional arrangements when any individual licence fee increase exceeds 50%.

4.61 Ofcom asked the question (11) "Do you agree with Ofcom's view that transitional arrangements should be used to migrate television tariffs onto a new basis? Is 50% a sensible threshold for licence fee increases to judge when transitional are appropriate?"

## **Response from stakeholders**

4.62 Of the seven responses made to this question, five agreed that transitional arrangements should be put in place to mitigate the transfer to new tariffs in the TV sector. Of these, four argued that 50% was too high a threshold to consider whether transitional arrangements should be applied and the current cap of 32% provided a better proxy figure for this assessment.

4.63 One respondent disagreed that transitional arrangements were required at all, and one respondent considered that there was insufficient data available to properly consider properly whether 50% was an appropriate threshold.

## **Ofcom's response**

4.64 Transitional arrangements will apply to limit increases on a licence by licence basis to 50%.

4.65 Transitional relief will not be available for those licensees currently paying or moving to the minimum tariff, or for licensees whose payments increase significantly because of a re-categorisation of the licence.

## **Timing of the Proposed Changes**

4.66 It is proposed that the changes to the tariffs in the Television sector will be introduced for the charging year 2005/6 with the exception of the inclusion of interactive, betting and gaming revenues.

- 4.67 The reason for the exception is that we do not already have the data for 2003 and therefore licensees will be asked to submit this information for the first time for the 2004 calendar year.
- 4.68 Interactive, betting and gaming revenues will be included in Relevant Turnover with effect from the Charging Year 2006/7 and data on these revenues for calendar year 2004 will be collected in early 2005 to enable the tariffs for 2006/7 to be set in due course.
- 4.69 Platform operators and licensees who retail their own channels will be required to resubmit their 2003 subscription revenue data, but since any reduction in revenues by moving from a retail to a wholesale basis will tend to benefit them, we do not consider this an undue administrative burden.

# Application of principles to the Radio Sector

## Summary of Proposals consulted upon

5.1 The key issues that Ofcom consulted upon were:

- the introduction of a new definition of Relevant Turnover. This included whether to take account of Additional Payments and differences in the cost structure between licensees;
- changes to the tariff structure, particularly whether to introduce a more progressive tariff, akin to the Television and Networks & Services sectors;
- rebalancing of tariffs, particularly raising the cost of licence applications, with a commensurate reduction in licence fees; and
- the impact of the proposed new tariffs, and whether any transitional arrangements should be made to migrate from the existing tariffs (which are already subject to transitional arrangements in 2004/5) to the new tariff structure.

## Definition of Relevant Turnover

5.2 Ofcom proposed to introduce a separate definition of “Relevant Turnover” for tariff-setting purposes in order to better reflect the range of services now provided under radio licences, and to ensure that only revenue from activities which are licensed is included.

5.3 Ofcom asked the question (12) “Do you agree with Ofcom’s proposed definition for relevant turnover in the Radio Sector?”

## Response from stakeholders

5.4 Respondent’s comments on this question were split. Two respondents broadly agreed with Ofcom’s proposed definition, two disagreed and one partially agreed. A number also requested greater clarification on what constitutes “retail revenues”.

5.5 Two respondents disagreed with the proposed inclusion of commercial production, interactive revenues and premium rate services within the definition of relevant turnover, as these are not broadcast services and therefore not revenue connected with broadcasting.

5.6 One respondent argued that the proposals unduly penalised successful radio groups as there was no upper limit on revenue. In addition the proposals do not

apportion costs across all radio operations as community radio, small radio operators and the BBC are excluded from paying tariffs calculated on the basis set out in the consultation. The proposal for de minimis fees means that successful radio groups are further disadvantaged as they contribute to the funding of other parts of the radio sector.

### **Ofcom's response**

- 5.7 Ofcom intends to base the definition of Relevant Turnover on the previous statutory definition of Qualifying Revenue, as defined in the Broadcasting Act, 1990 and 1996. However, the new definition will include new revenue streams associated with the radio broadcasting licence, such as revenue from premium rate telephone services.
- 5.8 The fees payable by the BBC to Ofcom reflect Ofcom's costs of regulation of both TV and Radio broadcasting by the BBC. Additionally, Community Radio channels pay applications fees and licence fees to cover the cost of regulating that sector. The impact of the de minimis threshold on larger radio groups is negligible.
- 5.9 The proposed definition of Relevant Turnover in Radio is set out in Annex 2 of this document.

### **Community Radio**

- 5.10 Our consultation document did not mention Ofcom's proposals for application fees, or ongoing fees, relating to Community Radio. The fees for 2004-05 were set out in our statement, "Licensing Community Radio" available at [http://www.Ofcom.org.uk/consultations/past/comm\\_radio/lcr\\_statement/?a=8710](http://www.Ofcom.org.uk/consultations/past/comm_radio/lcr_statement/?a=8710)  
1Application fees and ongoing annual licence fees were set as a minimum fixed fee, or a fee payable on relevant turnover on the same basis as permanent commercial analogue licences. We have received no comments on these fee proposals following this statement. Ofcom proposes to continue with this fee structure in 2005/6 (subject to a review in 2005, after the first round of licence awards is complete), to ensure that the balance between application fees and ongoing fees is appropriate and that the fees continue to reflect our principles as set out in section 1 of this statement.

### **Rebalancing of radio application fees and radio sector licence fees**

- 5.11 Ofcom undertook an internal review of the relationship between fees and costs for the variety of different regulatory activities in relation to radio.
- 5.12 The principal conclusions of this review were that a substantial proportion of the costs that are incurred in relation to radio regulation are connected to analogue licence applications and awards, but application fees for these licences currently recover only a minority of these costs, with the balance of these costs being recovered from the annual licence fees paid by existing licensees;
- 5.13 Ofcom asked the question (15) "Do you agree with Ofcom's intention to rebalance radio licence application fees and radio sector licence fees towards Ofcom 's underlying activity costs?"

## Response from stakeholders

5.14 All six respondents to this question agreed with the proposals set out by Ofcom. One of these respondents commented, however, on Ofcom's justification for not also reviewing the various other licence fees mentioned in the consultation. Capital Radio and GMG suggest that Ofcom might consider graduating the implementation of its proposed policy so as to limit the impact of this approach.

## Ofcom's response

5.15 Ofcom proposes to partially rebalance radio tariffs to recover more of the cost of the licensing process from application fees, which will result in an increase in the cost of application fees for new analogue radio licences. Ofcom does not intend to fully rebalance charges, as cost alignment is only one factor to be taken into account when judging the detailed structure of fees. The likely level of application charges was set out in the July consultation document.

## Structure of local and national analogue radio licence fees

5.16 Commercial local and national analogue tariffs were altered following the first consultation. The published Ofcom tariff for commercial analogue licences is based upon a proportion of revenue, although the tariff percentage of revenue is rarely applied directly, because of transitional arrangements.

5.17 Ofcom expects that, in part as a consequence of the rebalanced changes discussed above, it should be possible to reduce the tariff charged to commercial licensees for holding an analogue licence.

5.18 The exact size of the change will depend on a number of other factors, including Ofcom's budget for future years and the forecast number of licence applications. The size of the reduction will depend upon three further points considered below:

- a de minimis threshold on radio licence fees;
- the proposed introduction of a progressive tariff instead of the flat percentage rate; and
- the application of transitional relief.

5.19 Ofcom proposes to introduce a de minimis threshold of £100 for the fees that it will collect from radio licensees. This would remove a number of the smallest licensees from the requirement to pay fees, with a corresponding saving in administration costs both to Ofcom and the licensees. Ofcom proposes to set the threshold at this level in recognition also of the fact that the smallest licensees tend to be very marginal businesses.

5.20 Ofcom asked the question (16) "Do you agree with the proposal to introduce a modestly progressive tariff for local commercial analogue radio?"

## Response from stakeholders

- 5.21 The majority of respondents agreed with Ofcom's proposal to introduce moderately progressive tariffs for local commercial radio. One respondent suggested that Ofcom consider index-linking the bands.
- 5.22 Two respondents disagreed, and considered that progressivity was unfair and inequitable. In addition one of them noted that this approach further increased the tariffs payable from the level in 2004/5 and argued that reductions in tariffs should apply across the sector as a whole.

## Ofcom's response

- 5.23 The nature of the radio sector does involve some very small radio licensees, with typically low levels of profitability. Ofcom has satisfied itself that the arguments for progressive tariffs are strong in the radio sector and has therefore proposed tariffs that may be perceived as more progressive.
- 5.24 The decision not to make any major change to the structure of the digital tariffs reflects Ofcom's view that it remains appropriate to charge fees that are less than full cost recovery for DAB licences, given that the sector's commercial revenue remains very low. Ofcom considers that it would also be inappropriate to increase fees for AM applications given that this sector too tends to be characterised by low margins. Fees will be left as fixed sum amounts where revenue data is not available.
- 5.25 Ofcom does not intend to index-link the bands but will review them on a timely basis.

## Additional payments

- 5.26 A key difference between local radio licences and national licences is that national licences pay Additional Payments to HM Treasury.
- 5.27 Ofcom proposes not to allow the deduction of Additional Payments from turnover in the apportionment of Relevant Turnover for the purpose of setting Radio sector licence tariffs.
- 5.28 Ofcom asked the question (13) "Do you agree with Ofcom's view that additional payments should not be subtracted from relevant turnover for the purpose of setting radio tariffs?"

## Response from stakeholders

- 5.29 Three of the four respondents to this question agreed with the proposals set out by Ofcom. One respondent suggested however that Ofcom should review the level of additional payments more generally.
- 5.30 SMG argued that additional payments should be deducted for the same reasons as set out in its response to Question 7, regarding additional payments in the Television sector.

## **Ofcom's response**

5.31 Additional Payments reflect an economic rent extracted by the government and were set assuming Ofcom's existing licence fees. Ofcom's tariffs are an operating cost for licence holders (Ofcom's fees are a deductible item in the process of setting Additional Payments). To allow Additional Payments in turn to be a deductible item for the purposes of setting Ofcom's fees would be unfair to other licensees.

5.32 Therefore, Additional Payments will not be a deductible item from Relevant Turnover for the purpose of setting radio sector tariffs.

## **Cost differences**

5.33 Following the February consultation on charging principles, some of the stakeholders asked us to consider whether to take account of operating characteristics and associated costs for different licences. Ofcom's view was that licence fees should not reflect the underlying operating costs of different licences.

5.34 Ofcom asked the question (14) "Do you agree that operating costs should not be subtracted from relevant turnover for the purpose of setting radio tariffs?"

## **Response from stakeholders**

5.35 All five respondents to this question agreed with Ofcom's proposal.

## **Ofcom's response**

5.36 Ofcom does not intend to assess costs for individual licensees. Licence holders choose the format of the licence for which they apply and must meet the costs associated with the particular format that they choose. This is not a matter for Ofcom to consider when setting tariffs. To the extent, however, that rural licences generate less revenue than urban licences, those with rural licences should benefit from Ofcom's proposal to introduce a modest degree of progressiveness to the radio tariff structure.

## **Transitional arrangements**

5.37 The complete change of tariff setting basis from population (under the Radio Authority) to revenue caused significant variation to licence fee payments made by licensees. This will be to the benefit of some licensees and to the detriment of others. In 2004/5 Ofcom therefore introduced transitional arrangements to avoid large increases in fees. Ofcom proposes to maintain these arrangements.

5.38 Ofcom asked the question (17) "Do you agree that transitional arrangements should be used to migrate radio sector tariffs on to the new basis?"

## **Response from stakeholders**

- 5.39 Most respondents agreed with Ofcom that transitional arrangements should apply to the movement of radio tariffs to a new basis. SMG suggested however that Ofcom may consider implementing a short period for transitional arrangements to apply and queried whether such arrangements should apply to smaller stations owned by a large group.
- 5.40 One respondent disagreed with the proposal for transitional relief beyond the current financial year. One respondent also disagreed with the proposal arguing that it penalised INR services.
- 5.41 One respondent commented that transitional arrangements should be applied consistently between regulatory sectors.

## **Ofcom's response**

- 5.42 Ofcom's tariff principles include a desire to keep the tariff stable over time. As the structural changes imposed by Ofcom in the Radio Sector could involve substantial swings in licence fee payments, Ofcom will maintain the transitional arrangements.
- 5.43 It is Ofcom's intention that the transitional relief would end after the repayment of the DTI loan in 2007/8, when tariffs for all sectors are expected to fall.



# Application of principles to the Networks and Services Sector

## Summary of Proposals consulted upon

6.1 The key issues that Ofcom consulted upon were:

- Whether gross turnover or net turnover should be used for the purposes of calculating Ofcom administration charges;
- The structure of tariffs in the networks and services sector;
- Whether to publish a list of designated persons paying administration charges to Ofcom; and
- Whether to retain the Electronic Communications Code charge.

## Further consultation

6.2 Ofcom is consulting on a new Designation pursuant to section 38 of the Act. Ofcom proposes that the Designation reflects the nature of the designation originally published by the Director General of Telecommunications in 2003 and relied upon by Ofcom in the Statement of Charging Principles published in March 2004. This new Designation is set out in Section 8. Ofcom is proposing that the Designation will designate those providers who had a Relevant Turnover of £5,000,000 or more in the last but one calendar year.

6.3 Ofcom has taken this opportunity to amend Oftel's guidelines "The definition of "relevant activity" for the purposes of administrative charges" dated 29 July 2003, primarily to clarify how it will interpret public electronic communication services to end-users.

6.4 The guidelines, including Ofcom's amendments are set out at section 9 of this document. Ofcom welcomes comments on the guidelines and Ofcom's amendments in this consultation.

6.5 Without fettering its discretion, Ofcom is proposing to normally expect to follow the guidelines in determining what is a relevant activity for the purposes of administrative charges.

## Definition of revenue

6.6 Ofcom consulted upon the option of using either a gross revenue basis for setting administrative charges or a net revenue basis, where wholesale costs could be deducted.

6.7 Ofcom asked the question (18) "Do you agree with Ofcom that a gross revenue basis should be used for setting networks and services tariffs?"

## Response from stakeholders

- 6.8 Respondents' comments on this question were split. Telecommunications operators tended to agree with the proposal, whereas the resellers of capacity largely disagreed.
- 6.9 In particular, one respondent repeated its concerns (raised during Ofcom's earlier consultation on the 2004/5 tariffs) over double-counting of revenues if gross-revenues are to be used. This respondent believes that this approach has discriminatory effects and that Ofcom should consult further with the industry to find a workable alternative. UKCTA also thought that further work should be undertaken to find an alternative solution. Centrica consider that viable alternatives exist, suggesting in its response that wholesale and retail revenues should be separated with fees calculated on each set of revenues.
- 6.10 The ASCP and FSPA argued that calculating fees based on systemless service providers' gross turnover was disproportionate and not consistent with Ofcom's principle of fairness and preferred the alternative approach of calculating fees based on net turnover from which wholesale inputs had been deducted. Uniworld also supported the option of using net turnover. ASCP criticised Ofcom's assessment of the impact of this approach, feeling that it was incomplete. Ofcom had not considered the number of service providers affected nor the increase of regulatory costs on all service providers.

## Ofcom's response

- 6.11 While the net turnover approach may have some merits in principle, Ofcom does not believe it is desirable in practice and therefore does not propose to use a net turnover approach. This is because of:
- the complexity of precisely defining what constitutes a regulated wholesale input. For example, international termination payments represent a wholesale telecommunications cost input, but not one that has attracted UK administrative charges, and hence would not be deductible, like other UK interconnection payments;
  - the additional regulatory burden of compiling and monitoring net revenue data for operators and Ofcom;
  - the additional difficulties in ensuring that operators have calculated and declared Relevant Turnover consistently and fairly;
  - the unfairness perceived by resellers is mitigated by the fact that the bulk of the resellers for whom this may be an issue have revenues less than £5m so administrative charges are not payable; and
  - the tariff as a percentage of revenue is smaller than the television and radio sectors
- 6.12 Ofcom believes the drawbacks of moving to a net turnover basis for setting tariffs for networks and services outweigh the benefits and will therefore continue to use total turnover for the purpose of charging administration fees.

## Structure of network and services tariffs

- 6.13 The structure of networks and services tariffs is different to proposed TV and radio tariffs. In particular:

- the tariffs rely upon 15 bands for Relevant Turnover, whereas television and radio use fewer bands;
- the application of the tariff table rounds down Relevant Turnover to the lowest point within the Relevant Turnover band, whereas there is no rounding down for television and radio tariffs; and
- all relevant persons with a Relevant Turnover lower than £5m do not pay administrative charges. This is a far higher threshold than for television and radio tariffs.

6.14 However, the overall effect of networks and services tariffs is mildly progressive on account of the £5m floor and the rounding down of turnover figures. Ofcom saw little benefit in changing the structure to make it more like the television and radio tariffs and therefore proposed to keep the existing networks and services tariff structure.

6.15 Ofcom asked the question (19) “Do you agree that Ofcom should retain the structure of networks and services tariffs?”

### **Response from stakeholders**

6.16 The majority of respondents agreed with Ofcom’s proposals, although several made additional comments. BT commented that the £5m threshold should only apply for 2 years of a new entrant entering the market – ensuring all operators contribute to regulation. BT also suggested removing the present banding structure as it considered it discriminatory. One respondent also considered that the banding structure be removed.

6.17 One respondent disagreed with the concept of progressivity in the tariff structure, considering it discriminatory. T-Mobile thought that the minimum threshold should be removed.

6.18 Several respondents commented on whether or not the voluntary cap of 0.08% would remain in existence and sought clarification from Ofcom that this was its intention.

### **Ofcom’s response**

6.19 Ofcom proposes to keep the £5m minimum turnover threshold because administration costs would increase significantly if the threshold were lowered, due to the large number of small networks and services providers. Ofcom’s view is that the additional costs of a change would outweigh the benefits to the other networks and services stakeholders.

6.20 The current banding structure is designed to maintain a mild degree of progressivity in the networks and services charges, which is in keeping with Ofcom’s regulatory objectives. Ofcom intends to retain the existing networks & services tariff structures.

6.21 Ofcom is unable to place a formal spending cap on its networks and services charges, due to the requirement in the Communications Act to fully cover its costs. However, Ofcom has an overall spending cap imposed by H.M. Treasury such that increases over the next two years are limited to RPI and Ofcom has

signalled its intention to reduce operating costs by 5% in both the 2004/5 and 2005/6 financial years.

### **Publishing a list of Designated Persons**

- 6.22 Ofcom proposes to publish a list of designated persons paying fees to Ofcom with effect from 1st April 2005. The benefit of publishing this list would be that it would enable Ofcom to ensure that its records are kept more up to date, as circumstances change, for example, electronic communications companies exiting the market or increasing their Relevant Turnover beyond the £5m threshold.
- 6.23 Ofcom asked the question (20) “Do you agree that a list of those operators who are required to pay administrative charges to Ofcom under the Communications Act should be published?”

### **Response from stakeholders**

- 6.24 All respondents agreed that a list of operators who are required to pay administration charges should be published. One respondent suggested that all Network and Services operators should be included and that Ofcom should require all parties to confirm that they fall below the threshold at a particular point in time.

### **Ofcom’s response**

- 6.25 Ofcom intends to publish a list of operators who are required to pay administration charges. Ofcom has fewer formal links with many smaller participants in the networks and services industry and would therefore welcome the assistance of the sector in keeping the list up to date .

### **Section 38 Designations**

- 6.26 Under Section 38(2) of the Act, Ofcom can only charge those providers of electronic communication networks, services or associated facilities of a description that have been designated.
- 6.27 In accordance with good administrative practice, Ofcom intends to publish a fresh designation which will relate to the charging year 2005/6 and will cover subsequent charging years. Ofcom proposes that the Designation reflects the nature of the designation originally published by the Director General of Telecommunications in 2003 and relied upon by Ofcom in the Statement of Charging Principles published in March 2004.
- 6.28 Ofcom therefore proposes that the Designation will designate those providers who have a total turnover from relevant activities of £5 million or more in the last but one calendar year prior to the charging year in question. For example, if the relevant Charging Year commences on 1 April 2007, the relevant turnover will be for the calendar year of 2005.
- 6.29 Ofcom’s draft designation is produced as Chapter 8 of this document and Ofcom welcomes comments on this notice of designation. Ofcom will also

consult with the Secretary of State in accordance with section 34 of the Act once it has received comments on the draft designation pursuant to this consultation.

### **Electronic Communications Code**

- 6.30 Electronic Communication Code fees, (s.106 Communications Act 2003), are related to the costs of dealing with applications for the Code and ongoing administration costs including enforcement of the restrictions and conditions which apply to Code operators.
- 6.31 Ofcom asked the question (21) “Do you agree with maintaining the current electronic communications code tariff?”

### **Response from stakeholders**

- 6.32 All four respondents to this question agreed with Ofcom’s proposals. In its response one respondent suggested a single fee per code operator for recurring administration fees.

### **Ofcom’s response**

- 6.33 Ofcom proposes to maintain the application fee of £10,000 per person granted Code powers. Ofcom also intends to maintain the current system of having the same level of yearly charge for each Code operator for the costs of administration of the Code. This will be calculated by taking those estimated costs and dividing it by the number of Code operators at the time that the charge is calculated.

### **Relevant Activity guidance**

- 6.34 Ofcom has taken this opportunity to amend Oftel’s guidelines “The definition of “relevant activity” for the purposes of administrative charges” dated 29 July 2003, primarily to clarify how it will interpret public electronic communication services to end-users.
- 6.35 The guidelines, including Ofcom’s amendments are set out at section 9 of this document. Ofcom welcomes comments on the guidelines and Ofcom’s amendments in this consultation.
- 6.36 Without fettering its discretion, Ofcom is proposing to normally expect to follow the guidelines in determining what is a relevant activity for the purposes of administrative charges.

# Draft Statement of Principles for Broadcasting Act Licences and Networks & Services Regulation

7.1 This sections sets out the form that Ofcom expects the final published Statement of Charging Principles to take

## Contents

7.2 The contents of the Draft Statement of Charging Principles are as follows:

	Summary
Part 1	Funding of Ofcom
Part 2	Statement of Charging Principles
Part 3	Definitions
Annex A	Approach to Cost Allocation

# Summary

7.3 This statement follows a consultation<sup>1</sup> by the Office of Communications (“Ofcom”) in which Ofcom consulted on the principles that it would apply to fixing administrative charges and licence fees pursuant to the Communications Act 2003 (the “Act”).

7.4 This statement comprises three parts:

**Part 1** Information on the background to Ofcom’s funding and an analysis of the planned allocation of this funding requirement across Ofcom’s stakeholder groups;

**Part 2** The Statement of Charging Principles that Ofcom will apply in determining the amount to be recovered in administrative fees for networks, services and electronic communication code services, and licence fees for broadcasting licences required under sections 38 and 347 of the Act respectively;

**Part 3** Definitions of terms used in this document.

7.5 For the reasons set out in this document, Ofcom has decided as follows:

## Administrative charges

7.6 Administrative charges will be payable by those providers of electronic communications networks, electronic communication services and persons making available associated facilities of a description designated by Ofcom for the purposes of section 38 of the Act, such designation being contained in a notice published by Ofcom on [x date], in accordance with section 38 and section 34 of the Act;

7.7 The tariff applicable will be a percentage of turnover from relevant activities as set out in the tariff tables which will be published on 31st March for the following charging year;

7.8 Fees for the administration of the electronic communication code will be retained at a fixed fee per annum;

7.9 Without fettering its discretion, Ofcom will normally expect to follow its guidance on the definition of relevant activity for the purposes of the administrative charging regime published on [x date].

## Licence fees

### Television

7.10 Licence fees will be payable by those with licences under the Act, the Broadcasting Act 1990 and the Broadcasting Act 1996 (the “Broadcasting Acts”);

---

<sup>1</sup> [http://www.Ofcom.org.uk/consultations/current/licence\\_admin\\_fees/?a=87101](http://www.Ofcom.org.uk/consultations/current/licence_admin_fees/?a=87101)

7.11 The tariffs will be set out in the tariff tables which will be published on 31st March for the following charging year; and

7.12 Ofcom will provide details of transitional relief, where applicable in the tariff table published on 31st March for each charging year.

### **Radio**

7.13 Licence fees will be payable by those with licences under the Act and the Broadcasting Acts;

7.14 The tariffs will be set out in the tariff tables which will be published on 31st March for the following charging year; and

7.15 Ofcom will provide details of transitional relief, where applicable in the tariff table published on 31st March for each charging year.



## Part 1

# Funding of Ofcom

## Background

7.16 This chapter sets out the background to Ofcom's methodology in relation to fixing charges under the Act.

7.17 In summary, Ofcom is partly funded by administrative charges levied on designated providers of electronic communications networks and services (networks and services) and by broadcasting licence fees. Ofcom is required to apportion costs between Regulatory Sectors, and to cover those costs on an annual basis.

## Legislative Framework

7.18 The statutory provisions under which charges are levied on networks and services providers and broadcasting licensees are as follows.

## Networks and services

7.19 The statutory provisions relating to the collection of administrative charges for electronic networks and services and associated facilities are found in sections 38 to 44 of the Act.

7.20 Section 38(3) of the Act states that:

*"Ofcom are not to fix the administrative charge for a charging year unless-*  
*(a) at the time the charge is fixed there is in force a statement by Ofcom of the principles that Ofcom are proposing to apply in fixing charges under this section for that year; and*  
*(b) the charge is fixed in accordance with those charging principles".*

7.21 The principles must be such as appear to Ofcom, to be likely to secure, on the basis of an estimate of costs, on a year by year basis, that the aggregate amount of the charges payable to Ofcom is sufficient to meet the annual cost to Ofcom of carrying out certain functions as specified in the Act<sup>2</sup>.

## Broadcasting licences

7.22 The statutory provisions relating to the collection of broadcasting licence fees are in the Broadcasting Act 1990, the Broadcasting Act 1996<sup>3</sup> and section 347 of the Act.

7.23 Section 347(1) of the Act provides that:

---

<sup>2</sup> Section 38(4) of the Act.

<sup>3</sup> Sections 4(3) and 87(3) of the BA 1990 and sections 4(3) and 43(3) of the BA 1996.

*“Ofcom are not to fix a tariff under section 4(3) or 87(3) of the 1990 Act or under section 4(3) or 43(3) of the 1996 Act ... unless-  
(a) at the time they do so, there is in force a statement of the principles that Ofcom are proposing to apply in fixing that tariff; and  
(b) the tariff is fixed in accordance with those principles”*

7.24 The principles must be such as appear to Ofcom to be likely to secure, on the basis of an estimate of costs, that the aggregate amount of Broadcasting Act licence fees that are required to be paid to Ofcom during a financial year is sufficient to meet the cost of Ofcom’s function relating to the regulation of broadcasting<sup>4</sup>.

## Consultation

7.25 Before making or revising a statement of charging principles, Ofcom must undertake a consultation on the principles<sup>5</sup>.

7.26 The consultation document on this Statement of Charging Principles was published on 6th December 2004 and closed on 17th January 2005.

7.27 The non-confidential responses have been published on the Ofcom website together with a summary of those responses<sup>6</sup>.

## Ofcom’s Funding

7.28 In each financial year, Ofcom is required to balance its expenditure with its income<sup>7</sup>. Ofcom is required by the Act to raise income from each of the sectors it regulates such that it covers the costs to be incurred by Ofcom in regulating that sector together with a proper apportionment of Ofcom’s ‘common costs’ to each of those sectors<sup>8</sup>.

7.29 Ofcom raises its funds from a number of sources including: television broadcasting licence fees; radio broadcasting licence fees; administrative charges for electronic networks and services and associated facilities; and grant-in-aid from Central Government. The grant-in-aid covers the costs of regulating and managing the wireless spectrum. It also covers those statutory functions and duties that Ofcom must discharge under the Act but for which the Act provided no matching revenue stream (e.g. the statutory public interest test for media mergers, media literacy and ex-post Competition Act investigations in relation to networks and services).

7.30 Ofcom operates within an overall financial cap agreed in 2003 with HM Treasury. The current cap, which applies from the 2004/5 Financial Year, runs for three years and is set at RPI plus 0%.

---

<sup>4</sup> Section 347(2) of the Act.

<sup>5</sup> Section 39(5) and 347(3) of the Act.

<sup>6</sup> [www.Ofcom.org.uk](http://www.Ofcom.org.uk)

<sup>7</sup> Paragraph 8(1) of the Schedule to the Office of Communications Act 2002.

<sup>8</sup> Sections 38 and 347 of the Act.

## Ofcom's Overall Budget

7.31 An outline of Ofcom's proposed budget for each financial year will be published in an Annual Plan each year.

## Allocation of Costs by Sector

7.32 The Annual Plan will also include an allocation of planned costs by sector.

7.33 The analysis will be based on the budgeted direct costs of individual projects and programmes, which are allocated to the Regulatory Sector or Regulatory Categories to which they relate. Projects and activities not directly attributable to specific Regulatory Sectors or Regulatory Categories are apportioned across those projects or programmes and hence to Regulatory Sectors.

7.34 Overheads not directly allocated to a particular sector are apportioned to sectors by using the most appropriate cost driver, usually the amount of time spent on any particular activity.

7.35 The final allocation of the planned level of costs by Regulatory Sector represents Ofcom's overall judgement of both the level of expenditure by project or programme and the allocation of the spend on the project as between Regulatory Sectors or Regulatory Categories.

## Ofcom Launch Costs

7.36 The initial costs incurred by Ofcom since its establishment under the Office of Communications Act 2002 have been met through loan funding of £52.3m from the Department for Trade and Industry. These loans, which were made in the period from 31 March 2003 to 2 January 2004, are repayable in the period from March 2004 to March 2008.

7.37 The phasing of repayments is determined under the loan agreement with the DTI. We have apportioned the launch costs for the complete repayment period until March 2008 on a proportionate basis to the amount of expenditure incurred by the legacy regulators in each Regulatory Sector. The result of this apportionment is shown below:

Loan Repayments (inc Interest)	2003/4 £'000	2004/5 £'000	2005/6 £'000	2006/7 £'000	2007/8 £'000	Total £'000
Networks & Services		2,723	2,592	2,672	2560	10,547
TV Broadcasting		2,578	2,454	2,530	2423	9,985
Radio		403	383	395	379	1,560
Other Sectors	7,328	13,948	13,425	-	-	34,701
	7,328	19,652	18,854	5,597	5,362	56,793

7.38 The recovery of these apportioned costs is part of the costs for each Regulatory Category.

## Treatment of The BBC and S4C

- 7.39 The Act makes separate provision for the funding of Ofcom's costs in respect of carrying out its regulatory functions for both the BBC<sup>9</sup> and S4C<sup>10</sup> (the Welsh Fourth Channel). For the avoidance of doubt the fees payable by these organisations are not determined in accordance with the Statement of Charging Principles issued under section 347 of the Act, or determined in accordance with the same tariff to that of Television or Radio licensees. Instead both the BBC and S4C are to pay Ofcom such sums in respect of the carrying out by Ofcom of its functions in relation to the BBC and S4C as may be agreed between each of them and Ofcom respectively from time to time, or in default of agreement fixed by the Secretary of State.
- 7.40 Ofcom's approach to this separate treatment of funding for the BBC and S4C has been to identify its costs in respect of the regulatory functions under sections 198 and 207 of the Act and include an allocation of loan repayment and overheads. These costs are excluded from the totals for Television and Radio licence fees.

---

<sup>9</sup> Section 198(4).

<sup>10</sup> Section 207(6).

## Part 2

# Statement of Charging Principles

## Ofcom Approach to Setting Administrative Charges and Licence Fee Tariffs

### Common Principles

7.41 Ofcom has identified a number of common principles to apply in setting tariffs for licence fees and administrative charges. These are:

- Use of Relevant Turnover as a common tariff basis across all sectors or the setting of fixed tariffs where applicable. Turnover data is readily obtainable from all licensees and network and services providers and provides a basis for ensuring that the specific fees charged are proportional to ability to pay;
- Collection of turnover data for the last but one calendar year (rather than using licensees' and network and services providers' accounting periods). Collecting data for a fixed time period will be necessary to support Ofcom's database of cross-industry data that can be used for market analysis; and
- Administrative charges and licence fees will be calculated for each Regulatory Sector and for each Regulatory Category within the Regulatory Sector. This ensures reduced fees for Regulatory Categories with lower regulatory costs.

7.42 Ofcom has identified a number of distinct Regulatory Categories (set out at paragraph 7.45 below) within each Regulatory Sector. Because the regulatory costs relating to these categories are different separate tariffs will be set for each category.

7.43 For the purposes of sections 38 and 347 of the Act in any Charging Year Ofcom is proposing to adopt a common basis of tariff, usually based on turnover across the network and services and broadcasting sectors. Separate percentages may be set in respect of different Regulatory Categories, and for different bandings of turnover. Tariffs for some categories where turnover data is inappropriate (for example, under the Electronic Communications Code) or unavailable (for example, for digital sound programme service licences) may be set as fixed cash sums.

7.44 The definition of Relevant Turnover for the networks and services and broadcasting sectors relates directly to the activity regulated in that Regulatory Sector or Regulatory Category. Turnover for a relevant person who derives revenue from more than one Relevant Activity (for example for multiple broadcast licences) should be allocated across each of the Relevant Activities by the relevant person. Where Turnover is not able to be determined separately for each Relevant Activity an apportionment should be made on a basis that is proportionate to the underlying direct costs of each activity.

## Identification of Regulatory Categories

7.45 Ofcom has identified different levels of costs applying to the following groups of licences or activities:

- Relevant Activities for persons falling within section 38 of the Communications Act 2003 (Networks and Services);
- Electronic Communications Code administration;.
- Television – Category A – Channel 3, Channel 4, Channel 5 and the Public Teletext Service Licence;
- Television – Category B – Television Licensable Content Service Licences, Digital Television Programme Service Licences, Commercial Additional Services Licences and Digital Additional Service Licences;
- Television – Category C – Restricted Television Service Licences (long-term and short-term);
- Television – Category D – Multiplex Licences
- Television – Category E – Teleshopping Channels
- Radio - National and Local Sound Broadcasting Service Licences;
- Radio – Radio Licensable Content Service Licences, Additional Services Licences, Restricted Service Licences (long-term and short-term), Digital Radio Multiplex Service Licences, Digital Sound Programme Service Licences and Digital Additional Sound Service Licences.
- Radio – Community radio licences

7.46 Separate tariffs will be set for each of these Regulatory Categories.

## Payment of Fees

7.47 Ofcom's funding requirements are expected to fall fairly evenly over the year. Monthly payment of all licence fees above £75,000 will apply to networks and services and television licensees. Ofcom has decided that a lower limit of £5,000 for monthly payments will apply to radio licensees. The new administrative charges and licence fee tariffs will apply from 1 April in that charging year. Where existing fees are payable by monthly instalment, the new fee tariff will apply to payments from that date.

## Networks and Services

### Tariff calculation

7.48 Ofcom will charge designated providers a percentage of their relevant turnover:

- Where the fees payable exceed £75,000 p.a. they will be payable in monthly instalments;
- Ofcom has decided to use revenue data based on the last but one calendar year's revenues;
- A tariff table setting out the percentage to be applied will be published annually in March;
- There will be no distinction between charges for a network operator and a service provider;
- Ofcom will raise charges for the administration of the electronic communications code and the fees payable will be set annually; and
- Ofcom will publish a list of network and service providers who pay administrative fees.

7.49 Without fettering its discretion, Ofcom will normally expect to follow its guidelines in determining what is a relevant activity for the purposes of administrative charges published on [x date].

### Basis of Tariff Calculation

7.50 Ofcom shall set the tariff for each Charging Year as a percentage of the Relevant Turnover of each Relevant Person. Where turnover falls within a banding within the tariff table, the lower figure of the turnover band will be used to calculate the administrative charge. The percentage applied will be published in the tariff table for the Charging Year.

7.51 To determine the percentage, Ofcom shall determine the planned level of expenditure to be recovered in accordance with the principles set down in this document. Any over or under recovery of costs, through variations in the expenditure or the number or turnover of Relevant Persons will be adjusted in the following charging period.

7.52 Ofcom will then determine a percentage tariff that it expects will recover this amount based on the known Relevant Turnover of each Relevant Person. Turnover bands will be published in the tariff table for each Charging Year.

7.53 Charges for the administration of the electronic communications code will be determined by assessing the forecast expenditure and allocating it equally between the expected number of Relevant Persons. Any over or under recovery of costs, through variations in the expenditure or the number of Relevant Persons will be adjusted in the following charging period.

### Designation under section 38 of the Act

7.54 Under section 38 of the Act, Ofcom can only charge those providers of electronic communication networks, services or associated facilities of a

description that have been designated. Ofcom's designation (See Chapter 8) dated [x] will apply for each Charging Year.

### **Collection of Relevant Turnover information**

7.55 Ofcom will publish a general demand for information under section 135 of the Act in respect of each Charging Year in the early part of each calendar year.

### **Broadcasting**

7.56 Within Ofcom, costs related to the regulation of broadcasting are generally directly attributable to either television or radio. Ofcom has therefore set separate tariffs for radio and television licensees.

### **Television Broadcasting**

#### **Tariff Calculation**

7.57 Ofcom will charge Category A and B licensees a percentage of their relevant turnover. The definition of Relevant Turnover is included in Part 3. Ofcom will charge Category C, D and E licensees a fixed sum:

- Where the fees payable exceed £75,000 p.a. for Television they will be payable in monthly instalments;
- Ofcom has decided to use revenue data based on the last but one calendar year's revenues;
- A tariff table setting out the percentage or fixed annual sums to be applied will be published annually in March;

7.58 Ofcom shall set the tariff for each Charging Year for each category of licence and the percentage or percentages applied or fixed annual sums and any upper limit on relevant turnover will be published in the tariff table for the Charging Year published annually in March.

### **Transitional Relief**

7.59 Ofcom recognises that the changes to the bases of licence fees for some Television licensees may result in significant percentage variation in the licence fees. To limit the impact of this Ofcom proposes to limit the maximum percentage change in fees by way of a transitional relief policy.

### **Collection of Relevant Turnover Information**

7.60 To assess the Relevant Turnover of licensees Ofcom will request, under Broadcasting Act licence conditions, details of the Relevant Turnover for the calendar year to be provided within 28 days of the request. The returns must be certified by a Director of the Relevant Person.



## **Radio Broadcasting**

### **Radio Fee Tariff**

7.61 For national and local analogue radio licences, Ofcom will set fees as a percentage of Relevant Turnover. The definition of Relevant Turnover is included in Part 3 of this document. For all other types of radio licences, Ofcom will charge a fixed annual sum.

### **Tariff Calculation**

7.62 Ofcom will charge licensees a percentage of their relevant turnover or a fixed annual sum where applicable:

- Where the fees payable exceed £5,000 p.a. they will be payable in monthly instalments;
- Where fees are calculated as a percentage of relevant turnover, Ofcom has decided to use revenue data based on the last but one calendar year's revenues;
- A tariff table setting out the percentage or fixed annual sums to be applied will be published annually in March;

### **Transitional Relief**

7.63 Ofcom recognises that the changes to the bases of licence fees for Radio licensees resulted in significant percentage variation in the licence fees. To limit the impact of this Ofcom has introduced a limit to the maximum percentage change in fees by way of a transitional relief policy.

### **Collection of Relevant Turnover Information**

7.64 To assess the Relevant Turnover of licensees Ofcom will request, under broadcasting licence conditions, details of Relevant Turnover to be provided within 28 days of the request. The returns must be certified by a Director of the Relevant Person.

7.65 Ofcom will seek Relevant Turnover information for the calendar year on a consistent basis across all licensees (and providers of networks and services).

## Definitions

7.66 For the purposes of interpreting this document the following definitions shall apply unless otherwise stated:

'Act' means the Communications Act 2003;

'Connected Person' shall be interpreted in accordance with Paragraph 3 of Part 1, Schedule 2 to the Broadcasting Act 1990 (as amended);

'Charging Year' means the twelve month period commencing on 1 April in a year and ending on 31 March in the immediately following year;

'Licensed Service' means a service licensed under the Broadcasting Act 1990 or the Broadcasting Act 1996;

'Relevant Calendar Year' means, in respect of a Charging Year, the twelve month period commencing on 1 January in the last but one calendar year prior to the charging year in question so that if, for example, the Charging Year commences on 1 April 2007, the Relevant Calendar Year will be the calendar year of 2005;

'Regulatory Sector' are the categories of broadcasting and networks and services to which this Statement of Charging Principles applies (pursuant to Section 38 and Section 347 of the Act), together with Ofcom's spectrum management activities and other specific grant funded activities such as ex-post competition enquiries relating to networks and services, media literacy and newspaper mergers;

'Regulatory Category' means those groups of licences or activities described at paragraph 7.45 of this document;

'Relevant Activity' means any of the following:

- the provision of Public Electronic Communications Services to end-users;
- the provision of Electronic Communications Networks, Electronic Communications Services and Network Access to Communications Providers; and/or
- the making available of Associated Facilities to Communications Providers;

'Relevant Person' means a person liable to pay the administrative charge under Section 38 of the Act or a person liable to pay a Broadcasting Act licence fee as set out in section 347 of the Act;

'Relevant Turnover' means

- Relevant Turnover (Networks and Services); or
- Relevant Turnover (Radio); or

- Relevant Turnover (Television),

as applicable depending upon the type of service which that Relevant Person is providing;

'Relevant Turnover (Networks & Services)' means the turnover generated by the Relevant Person during the Relevant Calendar Year from carrying on any Relevant Activity after the deduction of value added tax and any other applicable sales taxes;

'Relevant Turnover (Radio)' means, in respect of each Licensed Service of a Relevant Person, all revenues (exclusive of value added tax) in respect of each Relevant Calendar Year derived from the provision of the Licensed Service, which shall be determined in accordance with the principles set out in Annex 2.

'Relevant Turnover (Television)' means, in respect of each Licensed Service of a Relevant Person, the revenues (exclusive of value added tax) in respect of each Relevant Calendar Year derived from the provision of the Licensed Service, which shall be determined in accordance with the principles set out in Annex 1.

# Annex to Statement of Charging Principles

## Approach to cost allocation

### Why Costs Need to be Allocated

7.67 Ofcom is required by the Act to raise income from each of the sectors it regulates such that it covers the costs to be incurred in regulating that sector. This means that there needs to be an apportionment of Ofcom's costs between each of the Regulatory Sectors. It may also be necessary to apportion costs between groups of services within the networks and services and broadcasting sectors which have different regulatory needs (for example, where one group of services has different regulatory requirements and hence different regulatory costs). Therefore Ofcom has identified different Regulatory Categories (see paragraph 7.45) within the networks and services and broadcasting sectors.

### Identification of Costs

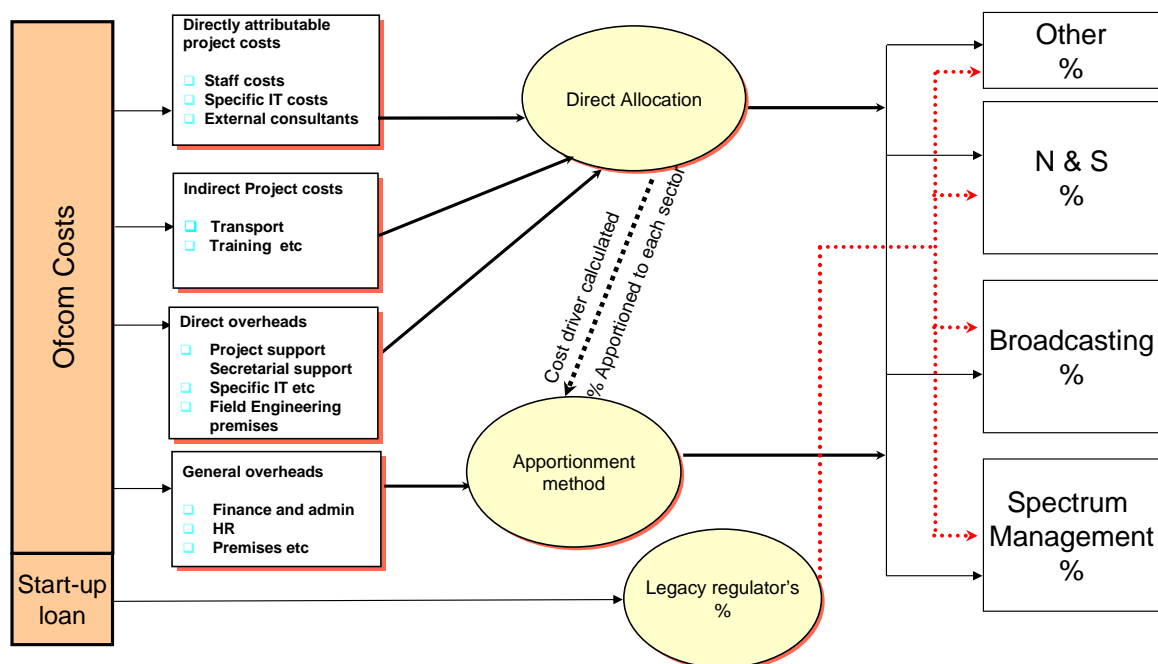
7.68 Ofcom divides its activities into projects, programmes of ongoing work and overheads. These are described in Ofcom's annual plan, and may vary each year.

7.69 Projects are one-off, separately identifiable projects that have been agreed upon for any particular year's activity. For example, during the financial year 2004/5, Ofcom undertook the Telecommunications Strategic Review, the Public Service Television Broadcasting Review and undertook projects associated with Spectrum Trading and Pricing.

7.70 Programmes are work that is ongoing in nature forming part of Ofcom's day-to-day regulatory activities. For example, Ofcom has a duty to deal with complaints regarding standards of television and radio content and a duty to investigate complaints relating to activity in the telecommunications market and Spectrum Interference.

7.71 Overheads are items identified as being the costs that facilitate Ofcom's performance of those duties described above, and include Human Resources, IT Infrastructure, Finance and Building Facilities.

7.72 Ofcom's approach to cost allocation is summarised in the diagram below.



7.73 The allocation of costs is intended to fulfil the following criteria:

### Objectivity

7.74 Cost allocations are not intended to benefit any particular sector or activity.

### Consistency

7.75 There will be consistency in approach between budget and actual costs, and from year to year

### Transparency

7.76 There will be:

- A clear distinction between direct and apportioned costs
- Identification of appropriate cost drivers
- Clear links to Ofcom's corporate plan

7.77 Ofcom's approach to cost attribution is to identify the appropriate cost drivers for each type of activity (as described in the consultation document on Ofcom's annual plan) and to use objective operational and/or financial data relevant to that cost driver to apportion the costs across the Regulatory Sectors.

## Concepts of Attribution

- 7.78 The fundamental feature of this approach to attribution is adherence to the key principle of causality. Each item of cost recorded in Ofcom's accounts is attributed to the activities within each sector.
- 7.79 Direct costs of activities are recorded directly and indirect costs are added by either allocation or apportionment. Allocated costs represent items of operating costs or capital expenditure which can be assigned wholly to a particular sector or activity by virtue of information in the accounting records. Apportioned costs represent overheads which are spread over each of the activities on a fair and equitable basis using standard cost apportionment methods.

## How transparency for Stakeholders is achieved

- 7.80 Ofcom has a duty under sections 38 and 347 of the Act to publish for each Charging Year statements relating to the income and expenditure for the sector in the year. These statements will be included in Ofcom's annual report and accounts which are audited by Ofcom's auditors, the National Audit Office.
- 7.81 The underlying methodology and computer models used for cost allocation statements will be subject to an internal audit review. As part of this internal audit process, Ofcom will make available data, at the summary levels described in the business plan, on the costs of activities carried out, and on the allocation of these costs by Regulatory Sector and Regulatory Category.

## Over or Under Recovery of Spend

- 7.82 Any over or under recovery of expenditure is carried forward to the next Charging Year. In that year, the allocation of the planned spend by Regulatory Sector is adjusted to reflect the over or under recovery carried forward from that Regulatory Sector from the previous year.
- 7.83 In each year when Ofcom publishes its Tariff Tables, it will provide a forecast of the over or under recovery for the preceding year. In addition, it will provide an allocation of the planned spend in the following year by sector. The forecast of the under or over recovery by Regulatory Sector within the preceding year will be updated immediately prior to the setting of the licence fee tariffs for the following charging year and will be taken into account in the setting of those tariffs.

## **Draft Notice of Designation under Section 38 and 34 of the Communications Act 2003**

- 8.1 The Office of Communications (“Ofcom”) in accordance with section 38 and section 34 of the Communications Act 2003 ('the Act') hereby gives notice of a designation, set out below, that it has made by way of publication of the notice on [x date] for the purposes of section 38 of the Communications Act 2003 (Fixing of charges).
- 8.2 The designation follows “Ofcom Response to Consultation on Draft Statement of Charging Principles” dated 6th December 2004 and the consultation with the Secretary of State for Trade and Industry.

### **Designation for the purposes of section 38 of the Act**

#### **Definitions**

- 8.3 For the purpose of interpreting this Designation the following definitions shall apply:-
- ‘Act’ means the Communications Act 2003;
- ‘Charging Year’ means a twelve month period ending 31 March;
- ‘Relevant Activity’ means any of the following:
- a. the provision of Public Electronic Communications Services to End-Users;
  - b. the provision of Electronic Communications Networks, Electronic Communications Services and Network Access to Communications Providers; or
  - c. the making available of Associated Facilities to Communications Providers.
- ‘Relevant Turnover’ means turnover made from carrying on any Relevant Activity after the deduction of sales rebates, value added tax and other taxes directly related to turnover.
- 8.4 Except in so far as the context otherwise requires, words or expressions shall have the meaning assigned to them and otherwise any word or expression shall have the same meaning as it has in the Act.

#### **Designation**

- 8.5 During each Charging Year, the Electronic Communications Network, Electronic Communications Service or Associated Facility which is designated for the purposes of section 38 of the Act is any Electronic Communications

Network, Electronic Communications Service or Associated Facility where the person providing that Network or Service, or making available that Associated Facility had a total turnover from relevant activities of £5 million or more in the last but one calendar year prior to the charging year in question. (For example, if the relevant Charging Year commences on 1 April 2007, the relevant turnover will be for the calendar year of 2005).

**[signed]**



## **The definition of ‘relevant activity’ for the purposes of administrative charging**

### **Guidelines issued by Ofcom**

#### **Summary**

- 9.1 This Guidance is intended to help those persons liable to pay administrative charges under section 38 of the Communications Act 2003 (“the Act”) to establish their gross turnover from relevant activities for the purposes of administrative charging.
- 9.2 It is hoped that operators will be able, with the help of this Guidance, to provide the information specified in any general demand for information more quickly. A number of activities they carry out will clearly fall under the definition of ‘relevant activity’ in the charging principles, without the need to refer to the Guidance.

### **Chapter 1**

#### **The Definition of Relevant Activity**

- 9.3 In the charging principles the term ‘relevant activity’ means:-
- a) the provision of public electronic communication services to end users;
  - b) the provision of electronic communication networks, electronic communication services and network access to communication providers;
  - or
  - c) the making available of associated facilities to communication providers.
- 9.4 The following section sets out Ofcom’s Guidance on the interpretation of this definition. The words and expressions used in the definition of ‘relevant activity’ have the same meaning as they have in the Act and they are included in Part D of this Section. They derive from but are not identical to the definitions contained in the EC Framework Directive<sup>11</sup>. Where appropriate, reference is made to this Directive for guidance on interpretation.

#### **Guidance on the definition of relevant activity.**

- 9.5 The purpose of this Guidance is to assist those persons liable to pay fees to estimate their gross turnover from relevant activities for the purposes of administrative charging. Ofcom cannot fetter its discretion as to any future decision. Accordingly, this Guidance will not be binding upon Ofcom in the future. However, Ofcom would normally expect to follow this Guidance in determining what is a relevant activity for the purposes of the administrative charging regime. Should Ofcom choose to depart from this Guidance in respect of any future decision it would set out its reasons for doing so. This Guidance may be subject to revision from time to time.

---

<sup>11</sup> Article 2 Framework Directive

- 9.6 For the avoidance of doubt, the guidelines are specific to determining what is a Relevant Activity for the purposes of administrative charging under the Act.

## Part A

### What does the provision of public ECSs to end users mean?

#### What is an ECS?

- 9.7 The definition of ECS in the Act is very broad. A service will be an ECS where:
- following removal of the content aspect of the service; then
  - the service has as its principal feature the conveyance of signals by means of an ECN.

This would include, for example, telephone calls. Where however, the principle feature of the service is what is *comprised* in the signals as opposed to the *conveyance* of signals, then it will constitute a content service and not an ECS.

- 9.8 Ofcom recognises that a broad range of services fall within the definition of ECS and that in some cases it may not be easy to decide whether an ECS is being provided. One method of viewing the range of ECSs is to classify them as either basic, advanced or enhanced services (value-added services) depending on the level of additional network resources and associated facilities that they require as well as whether there is any interaction, manipulation, or storage of content. The terms 'basic', 'advanced' and 'enhanced' services do not derive from the Act or from any of the EC Directives and are used here purely to help provide a framework for identifying activities which are ECSs.

#### Basic services

- 9.9 Where services are provided over an ECN without the support of databases or servers they can be regarded as basic services. Such services would include, but are not limited to, straightforward conveyance services such as: telephone calls; telex; IP conveyance using a 4 digit IP address; leased lines; video conferencing; ATM; frame relay; X25 data; radio and television transmission.

#### Advanced services

- 9.10 Where services are provided over an ECN but require the support of an associated facility they can be regarded as advanced services. Such services would include IP conveyance supported by the domain name system, non-geographic number services supported by IN translation databases, instant messaging supported by a 'presence' database, mobile telephony supported by home location registers, television transmissions supported by conditional access systems and electronic programme guides.

#### Enhanced services

- 9.11 Where services are provided over an ECN but either they interact with content, manipulate content or store content with the support of an associated facility such services can be regarded as enhanced or value-added services. In all of these cases even though the service does involve doing something with 'content' the service is still an ECS as it consists wholly or mainly in the conveyance of signals as opposed to the provision of a content service. Examples of such enhanced services include telephone calls completed

through interactive voice response boxes, TV transmission with MPEG compression supported by compression systems, 3-way conference calls supported by conference bridges, e-mail supported by e-mail servers and voice mail supported by voice mail servers.

9.12 Although the boundary lines between the suggested hierarchy of services is not always clear cut, any overlap will not impact on the question of whether an activity is a relevant one for the purposes of administrative charging.

9.13 The following diagram attempts to illustrate more clearly the features of basic, advanced and enhanced services.

	<b>Electronic Communication Networks</b>	<b>Associated Facilities</b>	<b>Output</b>
<b>Basic Services</b>	Provided over an ECN	None needed	Conveyance of signals e.g. telephone calls
<b>Advanced Services</b>	Provided over an ECN	Certain elements of the service require the support of associated facilities	Conveyance of signals e.g. mobile calls
<b>Enhanced Services</b>	Provided over an ECN	Certain elements of the service require the support of associated facilities	Conveyance of signals and either interaction with content, manipulation of content or storage of content e.g. email.

9.14 These principles are in line with the definition of ECS in the EC Framework Directive, which states that information society services are not ECSs unless they consist wholly or mainly in the conveyance of signals. Taking examples such as internet banking or on-line betting, in both cases the key characteristic lies more in the provision of information than in the conveyance of signals which is a purely incidental aspect of the service. However, even where a service does not consist mainly in the conveyance of signals the expectation will be that there is an underlying conveyance service associated with it that is an ECS and which will be caught. In many cases, for example home shopping, the provider of the content service will be different from the provider of the ECS.

### **What is the provision of a public ECS to end users?**

9.15 Part (a) of the definition of relevant activity comprises the provision of public electronic communication services to end-users. Ofcom considers that some guidance can usefully be provided in relation to two aspects of this definition:

- Who are end-users?
- What is a public ECS?

9.16 'End-user' is a term defined in section 151 of the Act, and in relation to a public ECS means:

- a) a person who, otherwise than as a communications provider is a customer of the provider of that service;
- b) a person who makes use of the service otherwise than as a communications provider; or
- c) a person who may be authorised, by a person falling within paragraph (a) so to make use of the service.

9.17 Ofcom's view is that an end-user will therefore comprise any customer of a public ECS who is not himself a communications provider. This would include residential customers who are provided with public electronic communication services.

9.18 It would also include business customers, of a wide variety of types where they are provided with public electronic communication services. Depending on the precise circumstances, providers of these services are likely to constitute end-users in relation to their status as customers of electronic communications services. Ofcom considers that business customers who are provided with public electronic communication services may be end-users even if they provide services themselves to either residential or business customers where the provision of the public electronic communication services is used as an input to those services.

9.19 The term 'public electronic communication service' is also defined in section 151 of the Act, as any electronic communications service that is so provided as to be available for use by members of the public.

9.20 Ofcom considers that 'available for use by members of the public' is to be interpreted broadly. It should in general encompass all services that are made available commercially, whether the potential customers for those services comprise (at one extreme) millions of residential consumers or (at the other) a very small number of businesses with complex and unusual communications requirements. A member of the public could in this context therefore comprise a single corporate customer.

9.21 Ofcom would not expect 'available for use by members of the public' to include the following two types of relationship:

- Supply of service to groups such as inmates of a prison, or the tenants of a landlord. This is because membership of these groups is not 'available to members of the public'.
- Self-supply of services, or the supply of services by one company in a group to others, where the same service is not genuinely available on a commercial bases to third parties.

## Part B

### The provision of ECNs, ECSs, and network access to communications Providers

#### What does the provision of ECNs to communication providers mean?

##### What is an ECN?

9.22 The definition of ECN in the Act is very broad. All that is required for an ECN to be viewed as an ECN by Ofcom is a 'transmission system'. This term is itself undefined. Although it may be inferred that a transmission system requires the conveyance of signals between the following elements: a transmitter, a medium and a receiver, the Act makes it clear that a transmission system may consist of no more than a transmitter used for the conveyance of signals<sup>12</sup>. Other resources which permit the conveyance of signals, such as apparatus used for switching or routing of signals, or stored data are not central to the definition although if they are present they will form part of the ECN.

9.23 Section 32(4) of the Act makes it clear that references to the 'provision of an ECN' include references to its establishment, maintenance or operation. Thus provision is not the same as ownership. There is no requirement for a communications provider to enjoy exclusive rights over the elements that combine to form the ECN.

9.24 There are many similarities between the definition of an ECN and the definition of 'telecommunication system' in section 4 of the Telecommunications Act 1984. Therefore it is highly likely that telecommunication systems which have been run under licences will be viewed as ECNs. The main difference between the old licensing regime and the new regime is that under the old licensing regime only one person could be authorised to run a system. Under the new regime a system that was being run by one licensee could form part of several persons' ECN. Furthermore, instead of regulating the running of the system, as was the case under licensing, it is the provision of the ECNs, ECSs and the making available of AFs that will be regulated under the new regime.

9.25 Communications providers are the providers of ECSs and ECNs and therefore would not include members of the public. An example of the provision of an ECN to a communications provider is where a provider operates and maintains a network on behalf of another communications provider i.e. the outsourcing of network provision. Another example is the grant of property rights which cannot be withdrawn (indefeasible rights of use) i.e. in international sub-marine cables.

#### What does the provision of electronic communication services to communication providers mean?

9.26 The meaning of an ECS has already been considered above. Examples of the provision of ECSs to communication providers would include the wholesale provision of any of the services mentioned above, to other communication providers as opposed to members of the public. It would also include the provision of an ECS to enable access to another ECS or ECN or the provision of an ECS to enable the interconnection of Public ECNs.

---

<sup>12</sup> Section 32(6)

## **What does provision of network access to communication providers mean?**

9.27 Section 151(3) of the Act sets out the definition of 'network access'. The term is all embracing and encompasses the interconnection of Public ECNs, and any services, facilities or arrangements which are not interconnection but which enable a Communications Provider, for the purpose of providing an ECS (whether his own or someone else's,) to make use of, for example any ECN or ECS provided by another Communications Provider.

Examples include:

- the provision of access to specified network elements and/ or facilities, including unbundled access to the local loop;
- the provision of specified services on a wholesale basis for resale by third parties;
- the provision of access to technical interfaces, protocols or other key technologies that are indispensable for the interoperability of services or virtual network services;
- the provision of access to operational support systems or similar software systems necessary to ensure fair competition in the provision of services; and
- the provision of interconnection services to networks or network facilities.

## **Part C**

### **The making available of Associated Facilities to communication providers**

#### **What are Associated Facilities?**

9.28 The definition of AFs in the Act catches all those AFs which are made available to enable the provision of an ECN or ECS or to support the provision of other services, such as any form of information society services or content services, e.g. broadcast television, which are provided by means of a network or service. A defining characteristic is that the AF is provided to make the provision of the ECN or ECS possible. In relation to 'other services' provided by means of an ECN or ECS an AF is caught if it makes possible or supports the provision of those other services. Therefore the definition catches AFs which are essential in the provision of an ECN or ECS and AFs which enable or support the provision of 'other services' provided by means of that network or service. Examples include telephone calls completed through interactive voice response boxes, TV transmission with MPEG compression supported by compression systems and e-mail supported by e-mail servers.

9.29 It is important to note that the AFs caught in this part of the definition of relevant activity do not include AFs, which are provided by the same person providing the ECS, which the AF supports or enables.

9.30 As has already been stated references to the 'provision of an ECN' is a reference to the network's establishment, maintenance or operation. Therefore this section could include the provision of a wide range of facilities including ducts, buildings masts and poles.

## Part D

### Annex to the definition of 'relevant activity' for the purposes of administrative charging

#### Definitions of the terms used in the definition of 'relevant activity'

9.31 These definitions have been taken from the Communications Act 2003 (the 'Act'):

- **Electronic communications network** means<sup>13</sup>:
  - a) a transmission system for the conveyance by the use of electrical, magnetic or electro-magnetic energy, of signals of any description; and
  - b) such of the following as are used, by the person providing the system and in association with it, for the conveyance of the signals:
    - i. apparatus comprised in the system;
    - ii. apparatus used for the switching or routing of the signals; and
    - iii. software and stored data.
- **Electronic communications service** means<sup>14</sup>:  
a service consisting in, or having as its principal feature, the conveyance by means of an electronic communications network of signals, except in so far as it is a content service.
- **Content service** means<sup>15</sup> so much of any service as consists in one or both of the following:-
  - a) the provision of material with a view to its being comprised in signals conveyed by a means of an electronic communications network;
  - b) the exercise of editorial control over the contents of signals conveyed by means of such a network
- **Conveyance of signals**<sup>16</sup> includes references to the transmission or routing of signals or of parts of signals and to the broadcasting of signals for general reception.
- **Signals** includes<sup>17</sup>:
  - a) anything comprising speech, music, sounds, visual images or communications or data of any description; and
  - b) signals serving for the impartation of anything between persons, between a person and a thing or between things, or for the actuation or control of apparatus.

---

<sup>13</sup> Section 32(1) of the Act

<sup>14</sup> Section 32(2) of the Act

<sup>15</sup> Section 32(7) of the Act

<sup>16</sup> Section 32(8) of the Act

<sup>17</sup> Section 32(10) of the Act

- **Associated facility** means<sup>18</sup> a facility which:
  - a) is available for use in association with the use of an electronic communications network or electronic communications service (whether or not one provided by the person making the facility available;) and
  - b) is so available for the purpose of
    - i. making the provision of that network or service possible;
    - ii. making possible the provision of other services provided by means of that network or service; or
    - iii. supporting the provision of such other services.
  
- **Communication provider** means<sup>19</sup>:  
a person who (within the meaning of section 32(4) of the Communications Act) provides an electronic communications network or an electronic communications service
  
- References to **Network Access** in Chapter 1 of the Communications Act<sup>20</sup> are references to:
  - a) interconnection of public electronic communication networks; or
  - b) any services, facilities or arrangements which
    - i. are not comprised in interconnection; but
    - ii. are services, facilities or arrangements by means of which a communications provider or person making available associated facilities is able, for the purposes of the provision of an electronic communications service (whether by him or by another), to make use of anything mentioned in section c) below

and references to providing network access include references to providing any such services, making available any such facilities or entering into any such arrangements.

- c) The things referred in ii) above are
  1. any electronic communications network or electronic communications service provided by another communications provider
  2. any apparatus comprised in such a network or used for the purposes of such a network or service
  3. any facilities made available by another that are associated facilities by reference to any network or service (whether one provided by that provider or by another); and
  4. any other services or facilities which are provided or made available by another person and are capable of being used for the provision of an electronic communications service.

---

<sup>18</sup> Section 32(3) of the Act

<sup>19</sup> Section 405 of the Act

<sup>20</sup> Section 151(3) of the Act



- **Public electronic communications service** means<sup>21</sup>:  
any electronic communications service that is provided so as to be available for use by members of the public
  
- **End-user** means in relation to a public electronic communications service<sup>22</sup>:
  - a) a person who, otherwise than as a communications provider is a customer of the provider of that service
  - b) a person who makes use of the service otherwise than as a communications provider; or
  - c) a person who may be authorised, by a person falling within paragraph (a) so to make use of the service

---

<sup>21</sup> Section 151 of the Act

<sup>22</sup> Section 151 of the Act

## Section 10

# Responding to this consultation

### How to respond

Ofcom invites written views and comments on the issues raised in this document, to be made by **5pm on Monday 17<sup>th</sup> January 2005**.

Ofcom strongly prefers to receive responses as e-mail attachments, in Microsoft Word format, as this helps us to process the responses quickly and efficiently. We would also be grateful if you could assist us by completing a response cover sheet (see Annex 4), among other things to indicate whether or not there are confidentiality issues. The cover sheet can be downloaded from the 'Consultations' section of our website.

Please can you send your response to [rex.warner@Ofcom.org.uk](mailto:rex.warner@Ofcom.org.uk).

Responses may alternatively be posted or faxed to the address below, marked with the title of the consultation.

Rex Warner  
Head of External Finance  
Ofcom  
Riverside House  
2A Southwark Bridge Road  
London SE1 9HA

Fax: 020 7981 3630

Note that we do not need a hard copy in addition to an electronic version. Also note that Ofcom will not routinely acknowledge receipt of responses.

### Further information

If you have any want to discuss the issues and questions raised in this consultation, or need advice on the appropriate form of response, please contact Rex Warner on 020 7981 3483.

### Confidentiality

Ofcom thinks it is important for everyone interested in an issue to see the views expressed by consultation respondents. We will therefore usually publish all responses on our website, [www.Ofcom.org.uk](http://www.Ofcom.org.uk), ideally on receipt (when respondents confirm on their response cover sheer that this is acceptable).

All comments will be treated as non-confidential unless respondents specify that part or all of the response is confidential and should not be disclosed. Please place any confidential parts of a response in a separate annex, so that non-confidential parts may be published along with the respondent's identity.

Ofcom reserves its power to disclose certain confidential information where this is necessary to fulfil its functions, although in practice it would do so only in limited circumstances.

Please also note that copyright and all other intellectual property in responses will be assumed to be assigned to Ofcom unless specifically retained.

### **Next steps**

Following the end of the consultation period, Ofcom intends publish its final Statement of Charging Principles in early February 2005.

Please note that you can register to get automatic notifications of when Ofcom documents are published, at

[http://www.Ofcom.org.uk/static/subscribe/select\\_list.htm](http://www.Ofcom.org.uk/static/subscribe/select_list.htm).

### **Ofcom's consultation processes**

Ofcom is keen to make responding to consultations easy, and has published some consultation principles (see Annex 3) which it seeks to follow, including on the length of consultations.

This consultation is shorter than Ofcom's standard 10 week period because of the responses received already regarding this issue.

If you have any comments or suggestions on how Ofcom conducts its consultations, please call our consultation helpdesk on 020 7981 3003 or e-mail us at [consult@Ofcom.org.uk](mailto:consult@Ofcom.org.uk). We would particularly welcome thoughts on how Ofcom could more effectively seek the views of those groups or individuals, such as small businesses or particular types of residential consumers, whose views are less likely to be obtained in a formal consultation.

If you would like to discuss these issues, or Ofcom's consultation processes more generally, you can alternatively contact Philip Rutnam, Partner, Competition and Strategic Resources, who is Ofcom's consultation champion:

Philip Rutnam  
Ofcom  
Riverside House  
2A Southwark Bridge Road  
London SE1 9HA  
Tel: 020 7981 3585  
Fax: 020 7981 3333  
E-mail: [philip.rutnam@Ofcom.org.uk](mailto:philip.rutnam@Ofcom.org.uk)

# Definition of Relevant Turnover in the Television Sector

## SUBSCRIPTION, INTERACTIVE AND ADVERTISING/SPONSORSHIP REVENUE – STATEMENT OF PRINCIPLES

### PART 1

#### Advertising & Sponsorship Revenues - Principles

1. Set out below are the principles which Ofcom considers should continue to apply in determining whether revenue deriving from the sale of advertising and sponsorship (other than interactive advertising and sponsorship which will fall within interactive revenues) should be treated as Relevant Turnover. Licensees will note that this is almost identical to the existing regime. Accordingly, given there are very few changes, Ofcom sees no need to attach to this document an Annex comprising detailed definitions and example scenarios in relation to advertising and sponsorship revenues.
2. Advertising revenue will be included within Relevant Turnover to the extent that it represents the net advertising revenue (i.e. net of commission paid to advertising agents) derived from independent television services regulated by Ofcom under Section 211 of the Communications Act 2003 as recorded in the profit and loss account(s) for the relevant calendar year computed on a normal accruals basis. For the purpose of calculating advertising revenue, all revenue which results from the normal trading terms and conditions for the insertion of advertisements into and around the programmes or information on the services, will be taken into account. For example, late payment surcharges and cancellation penalties will be included as Relevant Turnover, and early payment or volume discounts will be deducted when calculating Relevant Turnover.
3. Specific provisions for bad debts that are made in relation to advertising revenue in the audited accounts of licensees may be deducted. However, costs related to the selling of airtime are not allowable as a deduction when calculating Relevant Turnover.
4. Where airtime is provided to an advertiser, and where all or part of the consideration for an advertisement is received or is receivable other than in cash (for example, by barter or other exchange or contra-deal), the advertising revenue in respect of that advertisement will be deemed to be the amount that Ofcom determines would have been receivable in cash having regard to the factors that affect the price of analogue or digital television advertising for the licence in question.
5. Any amount received or receivable by the licensee in respect of an advertisement or other programme to meet his liability for additional payments (excluding the cash bid) will be regarded as advertising revenue.
6. Apart from commission paid to advertising agents, advertising revenue may not be

reduced under arrangements where all or part of the consideration for the advertisement is receivable by any person other than the licensee or his Connected Person. Commission paid to an advertising agent in excess of 15 per cent of the amount payable by the advertiser will be disregarded when computing advertising revenue.

### **Sponsorship Income**

7. A programme is sponsored if any payment is made, or if any part of its costs of production or transmission is met, by an organisation or person other than a licensee, with a view to promoting that organisation or person's own or another's name, trademark, image, activities, products, or other direct or indirect commercial interests. This would include any programme which is to any extent funded or supplied by an advertiser.
8. Sponsorship income of a licensee will be calculated on the same basis as advertising revenue in paragraph 1 above so far as applicable. That is, normal trading terms and conditions will be taken into account in determining the amount of sponsorship income which will be included within Relevant Turnover.
9. As a general principle, sponsorship income may not be reduced under arrangements where all or part of the consideration for the sponsorship is receivable by any person other than the licensee or his Connected Person. Similarly, the costs or commission paid to any agent, organisation, or person appointed to sell sponsorship on behalf of the licensee cannot be deducted when calculating Relevant Turnover.
10. Where a licensee secures sponsorship income on behalf of one or more licensees in connection with programmes to be transmitted on his own and/or their licensed services, any fee received by that licensee (for example, a finder's fee), will form part of his Relevant Turnover.
11. Where all or part of the financial benefit (direct or indirect) for including a programme in a licensed service, by way of sponsorship, is receivable by a licensee, but is receivable other than in cash, the Relevant Turnover of the Licensee will include the value, as determined by Ofcom, of the financial benefit received by the licensee. For example, where programme material is purchased on behalf of, or provided to a licensee, the Relevant Turnover of the licensee will be deemed to include the cost of the programme material to the supplier. Where transactions of this sort occur the licensee must endeavour to obtain true and fair records of the cost of the programme to the programme supplier.
12. However, if sponsorship appears in a programme but the sponsorship was arranged and sold not by the licensee but by an independent programme maker, other organisation, or by the organiser of an event or occasion which features in the programme (such as a sporting fixture, concert or theatrical performance) and the licensee neither received any part of the sponsorship payments nor played any part in determining the commercial terms on which the sponsorship was negotiated or sold, then such sponsorship income will not be included in Relevant Turnover. It is important, however, that there should be no specific arithmetical or quantitative relationship between the amounts paid for the sponsorship and the amount paid by the licensee for the programme or programme rights. Sponsorship of this kind may well have some impact on the price which the licensee pays for broadcast rights in the programme, but that alone will not bring the sponsorship within the scope of Relevant Turnover.

13. Off-air and support material, including books, videos, tapes, conferences, exhibitions, help lines and information lines, such as any premium rate telephone service, may be sponsored. Where the sponsor is given screen credits, the value of this sponsorship will count as Relevant Turnover.
14. Any amount received or receivable by the licensee, in respect of the inclusion of a programme in the service, to meet his liability for additional payments (excluding the cash bid) will be regarded as sponsorship income.

### **Advertising and Sponsorship Revenue of the Independent Analogue Broadcasters: Channels 3, 4, 5 and the Public Teletext licensee.**

15. Where advertising and sponsorship revenue is derived from the inclusion of advertisements or sponsorship on both the analogue and digital services of Channels 3, 4, 5 and the public teletext licensee, it is necessary to apportion the revenue between that attributable to the analogue service for which the relevant licensee holds a licence and the digital service(s) for which the relevant licensee holds a licence unless the advertiser or sponsor is sold and invoiced for the analogue and digital services separately. Ofcom will apportion the revenue on the basis of the audience share of the digital service(s) as a proportion of the total audience share for the analogue and digital services of the licensee in question, measured over the relevant calendar year. Digital cable viewers are to be treated as digital terrestrial viewers and analogue cable viewers are to be treated as analogue terrestrial viewers for the apportionment of revenue. Until the measurement of digital audience share is sufficiently reliable on all platforms, the amount to be apportioned to the digital services will be based on the percentage of ITV homes that are digital homes. The basis of apportionment may, however, be subject to review.
16. The apportionment will be applied retrospectively, i.e., after the end of each calendar year. Licensees may apply the latest apportionment percentage to their advertising and sponsorship revenue falling within Relevant Turnover until the next retrospective adjustment is made.
17. Where advertising or sponsorship agreements on the digital service(s) are invoiced separately, no apportionment will be required. It is expected that the invoiced amount will represent the value of a separate, arm's length transaction. If, in Ofcom's view, the invoiced amount misstates that value, Ofcom will adjust the amount so that it is equal to a separate arms length price.
18. Channel 3 licensees may apply to Ofcom for advertising to be sold jointly over more than one Channel 3 regional licence area where the Channel 3 licences are in common ownership. The apportionment of jointly sold revenues between licence areas will normally be based on net ITV homes in each regional area or whatever other basis Ofcom considers appropriate in the circumstances.

## PART 2

### Subscription Revenue Principles

#### Wholesale Revenues For Channels Retailed By Third Party Retailers

19. This will be the normal situation as the majority of pay TV channels will not be retailed by the Ofcom licensee (or one of its connected persons) but will be wholesaled by the Ofcom licensee to one or more third party retailers.
20. In that situation the wholesale revenues which would fall into "Relevant Turnover" would be determined as follows:
  - (a) The general rule will be that wholesale revenues for a channel will be the actual wholesale revenue received from third party retailers in respect of that channel in the relevant calendar year.
  - (b) The only exception to that general rule will be where a licensee wholesales a package of two or more channels to a retailer for a single wholesale charge. In that case, the wholesale revenues received in respect of that package of channels will be allocated among the channels in that package. That allocation will be based on the respective viewing shares of the channels in that package and the viewing share of each such channel will be the percentage of the total viewing figure achieved by that channel in each month, as published by BARB. The only circumstance in which the foregoing approach would not be employed is if the licensee can demonstrate to Ofcom's satisfaction that an alternative basis for such allocation or measurement of viewing share would be more appropriate and/or practicable (e.g. where the necessary BARB viewing data is not available). In that circumstance, the allocation or measurement of viewing share would be carried out in a manner agreed between Ofcom and the relevant licensee or, failing agreement, determined by Ofcom.

#### Wholesale Revenues For Channels Retailed By The Licensee

21. This will be an exceptional situation as only a small number of licensees are likely to retail their own channels.
22. For each channel of a licensee which is retailed by that licensee or a connected person of that licensee (a "**Relevant Channel**") on a particular platform (the "**Relevant Platform**"), then (unless the licensee can demonstrate to Ofcom's satisfaction that an alternative basis would be more equitable or more practicable) the wholesale revenues in respect of the distribution of that Relevant Channel on the Relevant Platform which would fall into "Relevant Turnover" would be determined as follows:
  - (a) The general rule would be to use the total amount of wholesale revenues received from third party distributors of that Relevant Channel on platforms other than the Relevant Platform in the relevant calendar year, to divide that total amount of wholesale revenues by the total number of subscribers to that Relevant Channel on platforms other than the Relevant Platform in the relevant calendar year and then to multiply the resulting amount by the total number of subscribers to that Relevant Channel on the Relevant Platform in the relevant calendar year.

In order to assist licensees, a worked example of how this general rule would work in practice is set out in Annex 1a (in the section relating to subscription revenues).

- (b) However, the following exceptions would apply in the following circumstances:
- (i) **Where a Relevant Channel is wholesaled by a licensee as part of a package of channels for distribution on a platform other than the Relevant Platform**, the total wholesale revenues received from the relevant third party distributor for that package of channels in the relevant calendar year will be allocated among the channels within that package. That allocation will be based on the respective viewing shares of the channels in that package (see paragraph 2(b) above as to how each channel's viewing share will be determined) unless the licensee can demonstrate to Ofcom's satisfaction that an alternative basis for such allocation would be more equitable or more practicable. In that case, the allocation would be carried out in a manner agreed between Ofcom and the licensee or, failing agreement, determined by Ofcom. The amount of the wholesale revenues allocated to each Relevant Channel will then be divided and multiplied as per 4(a) above.
  - (ii) **Where a Relevant Channel is not wholesaled for distribution on any platform other than the Relevant Platform**, the wholesale revenues for that Relevant Channel in the relevant calendar year would be deemed to be 70% of the total retail revenues from the distribution of that Relevant Channel on the Relevant Platform in the relevant calendar year (i.e. in each month a sum equal to the retail price of that Relevant Channel on the Relevant Platform multiplied by the number of subscribers to that Relevant Channel on the Relevant Platform, which monthly sums would then be aggregated across all twelve months in the relevant calendar year).
  - (iii) **Where a Relevant Channel is retailed only on the Relevant Platform and is retailed on the Relevant Platform as part of a package of channels**, the retail price of that package would be allocated among the channels in that package. That allocation will be based on the respective viewing shares of the channels in that package (see paragraph 2(b) above as to how each channel's viewing share will be determined) unless the licensee can demonstrate to Ofcom's satisfaction that an alternative basis for such allocation would be more equitable or more practicable. In that case, the allocation would be carried out in a manner agreed between Ofcom and the licensee or, failing agreement, determined by Ofcom. In each month, the amount of the retail price of that package so allocated to each Relevant Channel would then be multiplied by the number of subscribers to that package on the Relevant Platform, those monthly amounts would then be aggregated across all twelve months in the relevant calendar year and the wholesale revenues for that Relevant Channel in the



relevant calendar year would be deemed to be 70% of the aggregate of those monthly amounts.

### **Wholesale Revenues For Pay-Per-View Services Retailed By The Licensee**

23. This will be the usual situation as pay-per-view services are likely to be retailed by the licensee in most cases.
24. For each pay-per-view service of a licensee which is retailed by that licensee or a connected person of that licensee (a "**Relevant Service**") on a particular platform (the "**Relevant Platform**"), then (unless the licensee can demonstrate to Ofcom's satisfaction that an alternative basis would be more equitable or practicable) the wholesale revenues in respect of the distribution of that Relevant Service on the Relevant Platform which would fall into "Relevant Turnover" would be deemed to be 70% of the total retail revenues from the distribution of that Relevant Service on the Relevant Platform in the relevant calendar year.
25. For the purposes of calculating such total retail revenues, in each month the retail price of each programme or event offered, or each number or series of programmes or events offered for a single retail price (a "**Multiple PPV Offering**"), on the Relevant Service in that month would be multiplied by the total number of "buys" of each such programme, event or Multiple PPV Offering in the relevant month and the amount of retail revenues from all buys of each programme, event and Multiple PPV Offering offered on that Relevant Service in that month would be aggregated in order to determine the total amount of retail revenues for that month. The total amount of retail revenues for each month in the relevant calendar year would then be aggregated across all twelve months in the relevant calendar year.

### **Wholesale Revenues For Pay-Per-View Services Retailed By Third Party Retailers**

26. The wholesale revenues from the distribution of a pay-per-view service by a third party retailer which would fall into "Relevant Turnover" will be the actual wholesale revenue received from third party retailers in respect of the distribution of that pay-per-view service in the relevant calendar year.

## PART 3

### Interactive Revenue Principles

27. As a general rule, all sources of revenue deriving from a licensee's interactive services/applications (other than revenue deriving from retailing activity carried out via interactive services/applications – see below) will be included within that licensee's "Relevant Turnover".
28. **All** forms of interactivity resulting from a licensee's interactive services/applications will be taken into account irrespective of whether or not the viewer responds via the set-top box or any other means (for example, the display of a premium rate phone number in an interactive application leading to telephony revenue from viewer calls via that premium rate phone line).
29. Interactive applications/services will include those which are broadcast as part of, or accessed by any viewer from, the broadcast stream of a channel or pay-per-view service as well as any interactive application/service accessed independently e.g. via a separate menu of "stand-alone" interactive services.
30. For the purposes of these explanatory notes, interactive applications/services are also deemed to include:
  - i) any "call-to-action" displayed on-screen during any television programme or advertising break on any licensed service (including, for example, a call to viewers to vote or participate in a competition via a premium rate phone line, web site or text message) even if no interactive application is launched; and
  - ii) any digital text service(s) launched from within, or accessed via, the broadcast stream of any licensed service (including, for example, any on-screen display, as part of the relevant digital text service, inviting or prompting viewers to call a premium rate telephone line in order to place a bet with a bookmaker).
31. The principles relating to interactive revenue are set out below in three sections:
  - (a) **Sources of Interactive Revenue:** This section outlines the sources of interactive revenue which fall within "Relevant Turnover".
  - (b) **Chargeable Interactive Revenue:** This section explains how to determine the level of interactive revenue which will be subject to the percentage of "Relevant Turnover" payable to Ofcom.
  - (c) **Trigger for Inclusion within Relevant Turnover:** This section explains which viewer transactions and interactions trigger the inclusion of any resulting revenue within "Relevant Turnover".

### Sources of Interactive Revenue

32. All forms of revenue derived by a licensee and its connected persons from interactive applications/services will (subject to paragraph 36 below) fall within Relevant Turnover other than revenue deriving from the retailing of:

- goods; and
- services such as holidays (but excluding revenue deriving from the provision or offering of betting and gaming services via interactive services/applications which will be included within Relevant Turnover).

Interactive revenues are not limited to amounts expressed to be payable as shares of revenue and would, for example, include registration fees and "hosting" fees paid to any licensee in consideration for the "hosting" of/provision of access to an interactive application/service behind/from the broadcast stream of a licensed channel.

33. Interactive advertising and sponsorship revenue will fall within "Relevant Turnover". Therefore, in the case of an interactive advertisement which, for example, advertises a particular model of car, any payment by the advertiser for the inclusion within the broadcast stream of that advertisement or a related on-screen prompt or icon (e.g. any advertiser "impact" payment which is triggered by any click through into the advertisement) shall be included within "Relevant Turnover" whereas the revenue from any resulting purchase of the model of car being advertised shall be disregarded.
34. Accordingly, the following principal sources of interactive revenue are included within the calculation of "Relevant Turnover":
- Telephony charges (for example, resulting from viewer responses of any description (including but not limited to voting and competition entries) via premium rate phone lines and text messaging);
  - Betting and Gaming services and activities of any description (including, for example, fixed odds betting, pool betting, spread betting, lotteries, bingo, football pools, casino games, prize draws, scratch cards and pay-to-play games) irrespective of whether or not a licence or permit to provide such services or engage in such activities is required by law (whether by statute or otherwise); and
  - Interactive Advertising (including sponsorship of any interactive service/application).
35. This is not, however, an exhaustive list. Subject to the exclusion for retailing activities described above, all sources of revenue derived by a licensee from interactive services/applications are included within the calculation of "Relevant Turnover".

### **Chargeable Interactive Revenue**

36. All amounts of interactive revenue payable to, and retainable by, the licensee and its connected persons which fall within the sources of revenue described in Section 1 above will be included within "Relevant Turnover" subject to the permissible deductions/exclusions outlined at (a) to (e) below:

#### **(a) Revenue Share Arrangements**

The licensee may exclude or deduct from interactive revenues any amount which is "in the nature of" a share of those interactive revenues and which:

- (i) never comes into the hands of the licensee (i.e. is taken off the top) because a relevant third party is contractually entitled to retain such amount; or
- (ii) is received by the licensee but which the licensee is then contractually required to pay to a relevant third party.

For these purposes, the relevant third parties are:

- any telephony provider/operator by means of whose network (whether fixed or mobile) viewer responses are conveyed;
- any operator of a television platform on which the licensee broadcasts/provides interactive applications/services;
- any provider of interactive "back end" services to the licensee in relation to the processing and authentication of viewer responses and the provision of a "return path";
- providers of interactive betting/gaming services (e.g. bookmakers) via the licensee's interactive services/applications. The "provider" of an interactive betting/gaming service will be, typically, the person who is liable to pay out any winnings or prizes (e.g. any winnings deriving from any bet placed by a viewer or any prizes deriving from any pay-to-play game played by a viewer) and not the producer or provider of the content or functionality of the relevant interactive application/service. In order to assist licensees, a further detailed example scenario is set out in Annex 1a below; and
- advertising agencies in respect of interactive advertising and/or sponsorship broadcast or provided by the licensee but subject to (d) below.

Any person who falls within any of the above categories shall be treated as a "relevant third party" irrespective of whether or not that person is a connected person of a licensee.

Ofcom's current view is to regard this as an exhaustive list of relevant third parties.

**(b) Non-Broadcaster Revenues:**

A licensee may deduct/disregard any interactive revenues receivable by it in any capacity other than its capacity as an Ofcom licensee or as a provider of a service licensed by Ofcom. Accordingly, to the extent that interactive revenues are receivable by a licensee or any of its connected persons in its capacity as a platform operator or, for example, as a provider of interactive betting or gaming services (see the fourth bullet in (a) above in respect of the meaning of "provider" in this context), such revenues may be disregarded in computing Relevant Turnover.

**(c) Cost Deductions:**

Pursuant to (a) above the licensee may deduct from gross interactive revenues sums payable to platform operators or other relevant third parties which are in the nature of a revenue share. Costs which are not in the nature of a revenue share and are effectively business costs associated with the provision of interactive services would not be deductible.

Ofcom proposes that the following contractual payments to relevant third parties would be deductible as being "in the nature of" revenue sharing payments:

- (i) any percentage of interactive revenue which falls within (a) above; and
- (ii) any per call/response fee which is effectively a share of telephony revenue.

There would then be a presumption that all other payments to third parties would be non-deductible business costs. By way of example, these would include:

- (i) insurance premiums relating to the broadcast of interactive applications;
- (ii) set-up fees in respect of the integration of interactive applications with set-top box software/hardware;
- (iii) signing fees relating to the broadcast of interactive applications;
- (iv) "production/functionality" costs i.e. the cost(s) of designing, building, producing and/or providing the content and/or functionality of interactive applications and services (whether as part of any initial "set-up" phase or on an ongoing basis);
- (v) technical support fees in respect of any online network, online communications module, browser or other software;
- (vi) software licence fees e.g. for the use of a browser to navigate through an interactive application; and
- (vii) fees in return for contact information and viewer data.

**(d) Interactive Advertising Commissions:**

In the case of sales of interactive advertising involving an advertising agent, the licensee shall be entitled to deduct any commission which is actually retained by or paid to the relevant advertising agent provided that the maximum amount which may be so deducted shall be 15% of the amount payable by the relevant advertiser.

**(e) Betting/Gaming Returns/Winnings and Prizes etc:**

The licensee may also deduct or exclude from gross interactive revenues any returns/winnings paid out to viewers pursuant to betting and gaming activities (where such activities give rise to gross interactive revenues) and/or the cost to the licensee of any prize(s) provided to viewers as part of any competition but only to the extent that such prizes are paid for directly by the licensee itself.

**Trigger for Inclusion of Interactive Revenue within Relevant Turnover**

37. Any interactive revenue deriving from a viewer transaction or interaction (whether that transaction or interaction is carried out via a set-top box, telephone call, website or otherwise e.g. voting via text message) shall fall within Relevant Turnover if that transaction or interaction is in response to or with, or results from:
- an interactive application launched from within, or accessed from, the broadcast stream of a channel or other licensed service operated by the relevant licensee; and/or
  - a call-to-action during any programme or advertisement broadcast on a channel or other licensed service operated by the relevant licensee which invites viewers to carry out a transaction or respond to an invitation or prompt (e.g. by voting or entering a competition or game of any description) and, where required, contains the necessary contact information; and/or
  - an interactive service which is not launched from the broadcast stream of a channel but is accessed via a separate menu of interactive services (e.g. by pressing the "Interactive" button on any remote control) in circumstances where that interactive service is licensed by Ofcom.
38. Ofcom may decide to review the methodology described above for setting licence fees based on interactive revenues and the way in which licensees have implemented that methodology.

## **CALCULATION OF SUBSCRIPTION REVENUE – EXAMPLE SCENARIOS AND DEFINITIONS**

1. This part of the Annex provides broadcasters with further detail as to how the principles set out in Section 4 of this document would operate in practice in the context of various scenarios applicable to the wholesaling and retailing of subscription channels and pay-per-view services.
2. The scenarios listed below are designed to be read in conjunction with the definitions which are set out at the end of this Annex.

### **Example Scenarios**

3. Most broadcasters will fall within Scenario 1 or, if not, Scenario 2. Only in a limited number of cases will a broadcaster fall within Scenario 3.

#### **(i) Scenario 1**

**A Licensed Channel is distributed on one or more Third Party Platform(s) where the wholesale revenues in respect of that Licensed Channel can be separately determined:**

In this scenario, the amount of wholesale revenues included in the Relevant Turnover in respect of that Licensed Channel would in each month be the Third Party Monthly Subscription Revenue in respect of the distribution of that Licensed Channel on the relevant Third Party Platform(s) and would in each year be the amount of the Third Party Monthly Subscription Revenue in respect of that Licensed Channel aggregated across all twelve months during that year.

This will apply in circumstances where the wholesale revenues payable in respect of the relevant Licensed Channel are separable from those payable in respect of any other Licensed Channel i.e. where the relevant distribution arrangement is in respect of one Licensed Channel only or, in the event that the relevant distribution arrangement relates to two or more Licensed Channels, the amount of wholesale revenues attributable to the relevant Licensed Channel can be separately determined by reference to the terms of that distribution arrangement from those payable in respect of the other Licensed Channels covered by that distribution arrangement.

#### **(ii) Scenario 2**

**A Licensed Channel is distributed on one or more Third Party Platform(s) as part of a group of Licensed Channels in circumstances where the wholesale revenues in respect of that Licensed Channel cannot be separately determined:**

In this scenario, the amount of wholesale revenues included in the Relevant Turnover in respect of that Licensed Channel would in each month be the Third Party Monthly Subscription Revenue in respect of the distribution of that Licensed Channel on the relevant Third Party Platform(s) and would be determined in accordance with the proviso to the definition of "Third Party Monthly Subscription Revenue". To determine the annual amount of such wholesale revenues, the Third Party Monthly

Subscription Revenue in respect of each month would be aggregated across all twelve months during that year.

Therefore, where there is a single wholesale price paid for a group of Licensed Channels by any third party platform operator in respect of the distribution of two or more Licensed Channels on that operator's Third Party Platform and a separate wholesale price for each of those Licensed Channels cannot be separately determined, the Viewing Share Principle will be used to allocate that wholesale price among the relevant Licensed Channels unless the licensee can demonstrate to Ofcom's satisfaction that an alternative basis for such allocation would be more equitable or more practicable (in which case, the allocation would be carried out in a manner agreed between Ofcom and the relevant licensee or, failing agreement, determined by Ofcom).

**(iii) Scenarios 3a, 3b 3c and 3d**

**A Licensed Channel is distributed on the Own Platform of the Relevant Person who holds the Ofcom licence for that Licensed Channel (including where a Relevant Person retails its own Licensed Channel on such Own Platform):**

In this scenario, there will be no arm's length carriage agreement in respect of the distribution of the Licensed Channel on the Relevant Person's Own Platform. In such circumstances, the amount of subscription revenue included in the Relevant Turnover in respect of that Licensed Channel shall be the Deemed Monthly Subscription Revenue in respect of that Licensed Channel which shall in each month be determined as follows:

- a) **in any month in which that Licensed Channel is also distributed on one or more Third Party Platform(s) and a separate wholesale fee for that Licensed Channel is capable of being determined:** the Deemed Monthly Subscription Revenue is determined by reference to the average wholesale per subscriber rate payable in respect of that Licensed Channel across all Third Party Platform(s) multiplied by the number of subscribers to that Licensed Channel on the Relevant Person's Own Platform - see the opening section of the Deemed Monthly Subscription Revenue definition,

i.e.  $\frac{A}{B} \times C$

Where

A = the total amount of wholesale revenues received from the distribution of that Licensed Channel on all Third Party Platforms in the relevant month;

B = the total number of subscribers to that Licensed Channel on all Third Party Platforms in the relevant month;

C = the total number of subscribers to that Licensed Channel on the Own Platform of the Relevant Person in the relevant month.

- b) **in any month in which that Licensed Channel is also distributed on any Third Party Platform(s) but as part of a group of Licensed Channels for which a single wholesale price is payable:** unless a



separate wholesale fee for that Licensed Channel is capable of determination by reference to the terms of the relevant distribution arrangement, the Deemed Monthly Subscription Revenue shall be the proportion of the total wholesale revenues payable in respect of that group of Licensed Channels which is allocated to that Licensed Channel. That proportion shall be determined in accordance with the Viewing Share Principle (see the proviso to the opening section of the Deemed Monthly Subscription Revenue definition) unless the licensee can demonstrate to Ofcom's satisfaction that an alternative basis for such allocation would be more equitable or more practicable (in which case, the allocation would be carried out in a manner agreed between Ofcom and the relevant licensee or, failing agreement, determined by Ofcom); or

- c) **in any month in which that Licensed Channel is not distributed on any platform other than the Own Platform of the Relevant Person:** wholesale revenues cannot be determined by reference to the distribution of that Licensed Channel on any Third Party Platform. Accordingly, unless paragraph (d) below applies, the Deemed Monthly Subscription Revenue shall be deemed to be 70% of the retail price payable for that Licensed Channel by subscribers to that Licensed Channel on the Own Platform of the Relevant Person (see subparagraph (a) of the Deemed Monthly Subscription Revenue definition); or
- d) **in any month in which that Licensed Channel is not distributed on any platform other than the Own Platform of the Relevant Person and the retail price for that Licensed Channel on the Own Platform cannot be separately determined:** where the Licensed Channel is retailed as part of a package of channels on the Own Platform for a single retail price, the Deemed Monthly Subscription Revenue shall be deemed to be 70% of the proportion of the total retail revenues payable by subscribers in respect of that package of Licensed Channels which is allocated to that Licensed Channel. That proportion (i.e. against which the 70% shall be applied) shall be determined in accordance with the Viewing Share Principle (see subparagraph (b) of the Deemed Monthly Subscription Revenue definition) unless the licensee can demonstrate to Ofcom's satisfaction that an alternative basis for such allocation would be more equitable or more practicable (in which case, the allocation would be carried out in a manner agreed between Ofcom and the relevant licensee or, failing agreement, determined by Ofcom).

To determine the annual amount of subscription revenues included within the Relevant Turnover of that Licensed Channel, the Deemed Monthly Subscription Revenue in respect of each month would be aggregated across all twelve months during that year.

#### **(iv) Scenario 4**

**A Licensed PPV Service is distributed on the Own Platform of a Relevant Person only:** The amount of revenues included within Relevant Turnover in respect of that Licensed PPV Service shall be the Own PPV Service Revenue relating to that

Licensed PPV Service and shall be deemed to be 70% of the total retail revenues deriving from PPV Buys during the relevant calendar year (see the definition of Own PPV Service Revenue).

#### (v) Scenario 5

##### **A Licensed PPV Service is distributed on one or more Third Party Platform(s):**

The amount of revenues included within Relevant Turnover in respect of that Licensed PPV Service shall be the Third Party Monthly PPV Revenue relating to that Licensed PPV Service and shall be the actual wholesale revenues from distribution of that Licensed PPV Service on the relevant Third Party Platform(s) (see the Third Party Monthly PPV Revenue definition).

Note: For the avoidance of doubt, the above scenarios will not necessarily be exclusive of each other throughout a particular year or on all platforms i.e. different scenarios can apply to the same channel or service in different months or on different platforms. For example, in a month where a Licensed Channel is licensed for distribution on only one Third Party Platform, Scenario 1 would apply to such distribution and in a month where that Licensed Channel is licensed for a single wholesale price as part of a group of channels for distribution on two separate Third Party Platforms, Scenario 2 would apply to such distribution.

### **Applicable Definitions**

4. Applicable definitions are:

- **"Deemed Monthly Subscription Revenue"**, in respect of a Licensed Channel distributed on the Own Platform of the Relevant Person who holds the Ofcom licence for that Licensed Channel, means, in each calendar month, the sum represented by "x" in the following equation:

$$x = \left(\frac{a}{b}\right) \times c$$

where:

- a = the total amount of wholesale revenue received by the Relevant Person (or a Connected Person of that Relevant Person) from the distribution of the Licensed Channel on all Third Party Platforms in the relevant month
- b = the total number of subscribers to the Licensed Channel on all Third Party Platforms in the relevant month
- c = the total number of subscribers to the Licensed Channel on the Own Platform of the Relevant Person in the relevant month

PROVIDED THAT in any month in which the Licensed Channel is wholesaled to a third party together with at least one (1) other Licensed Channel for distribution on a Third Party Platform and a single wholesale price, charge or fee is payable in respect of those Licensed Channels, the figure at "a" above shall (in respect of the Licensed Channel) be a proportion of that single wholesale price, charge or fee calculated in accordance with the Viewing Share Principle unless the licensee can demonstrate to Ofcom's satisfaction that an alternative basis for such allocation would be more equitable or more practicable (in which case, the allocation would be carried out in a manner agreed between Ofcom and the relevant licensee or, failing agreement, determined by Ofcom).

**Notwithstanding the foregoing provisions of this definition:**

- in any month in which the Licensed Channel is not wholesaled for distribution on any television platform other than the Own Platform of the Relevant Person, the formula set out above shall be disregarded and (unless paragraph (b) below applies) the "**Deemed Monthly Subscription Revenue**" in respect of such Licensed Channel shall be deemed to be seventy per cent (70%) of all payments received by the Relevant Person (or any Connected Person of the Relevant Person) from any subscriber(s) to the Licensed Channel on such Own Platform for the right to view the Licensed Channel (i.e. the retail price payable by subscribers in respect of the Licensed Channel) in the relevant month.

Therefore, in each such month, the Deemed Monthly Subscription Revenue shall be calculated as follows:

**(Standalone Retail Price of Licensed Channel x Total No of Subscribers) x 0.7**

- unless otherwise agreed between Ofcom and the Relevant Person, in any month in which the Licensed Channel is not wholesaled for distribution on any television platform other than the Own Platform of the Relevant Person **and** is retailed on that Own Platform for a single retail price as part of a package of channels (whether basic or premium), the formulae set out above shall be disregarded and the "**Deemed Monthly Subscription Revenue**" in respect of such Licensed Channel shall be an amount equal to the proportion of the retail revenues payable by subscribers in respect of such package of channels which is allocated to that Licensed Channel. Such proportion shall be calculated in accordance with the Viewing Share Principle unless the licensee can demonstrate to Ofcom's satisfaction that an alternative basis for such allocation would be more equitable or more practicable (in which case, the allocation would be carried out in a manner agreed between Ofcom and the relevant licensee or, failing agreement, determined by Ofcom). The amount equal to the proportion of retail revenues so allocated shall, for the purposes of this sub-paragraph (b), be referred to as the "**Retail Proportion**".

Therefore, in each such month, the Deemed Monthly Subscription Revenue shall be calculated as follows:

**(Retail Proportion x Number of subscribers to the Licensed Channel) x 0.7**

- "**Licensed Channel**" means any linear television channel for which a licence under the Broadcasting Acts 1990 and 1996 or the Communications Act 2003 is required;
- "**Licensed PPV Service**" means any licensed service which offers programmes, events and/or Multiple PPV Offering(s) for purchase on a pay-per-view basis;

- **"Multiple PPV Offering"** means two (2) or more programmes and/or events which are offered for purchase by viewers on a pay-per-view basis for a single retail price;
- **"Ofcom licence"** means a licence under the Broadcasting Acts 1990 and 1996 or the Communications Act 2003 (whether granted by Ofcom or the Independent Television Commission);
- **"Own PPV Service Revenue"** in respect of a Licensed PPV Service means seventy per cent (70%) of the total retail revenue from PPV Buys received by the Relevant Person (or any Connected Person of the Relevant Person) from viewers during the relevant calendar year in respect of single programmes, single events or any Multiple PPV Offering(s) offered by the Relevant Person as part of that Licensed PPV Service on the Own Platform of that Relevant Person;
- **"Own Platform"** means, in respect of any Relevant Person, means any television platform which is owned and/or operated by that Relevant Person (or any Connected Person of that Relevant Person) or on which that Relevant Person retails any Licensed Channel or Licensed PPV Service;
- **"PPV Buy"** means a payment made by a viewer for the right to view a single programme, single event or Multiple PPV Offering on a pay-per-view basis;
- **"Television Platform"** means any delivery system used to distribute any Licensed Channel on a subscription basis and/or any Licensed PPV Service including, without limitation, any cable, DTH, DSL and/or DTT system(s);
- **"Third Party Platform"** means, in respect of a Relevant Person, any television platform other than the Own Platform of that Relevant Person;
- **"Third Party Monthly Subscription Revenue"** in respect of a Licensed Channel means, in each month, the total sum of all revenues received from any television platform operator(s) (or any Connected Person of any television platform operator(s)) in respect of the carriage or distribution of the relevant Licensed Channel on Third Party Platform(s) PROVIDED THAT, in the event that the Licensed Channel is wholesaled for distribution on any Third Party Platform together with one or more other Licensed Channel(s) in consideration for a single monthly wholesale price, charge or fee, a proportion of such single monthly wholesale price, charge or fee shall be allocated to the relevant Licensed Channel on the basis of the Viewing Share Principle unless the licensee can demonstrate to Ofcom's satisfaction that an alternative basis for such allocation would be more equitable or more practicable (in which case, the allocation would be carried out in a manner agreed between Ofcom and the relevant licensee or, failing agreement, determined by Ofcom);
- **"Third Party Monthly PPV Revenue"** in respect of a Licensed PPV Service means, in each month, the total sum of all payments received by the Relevant Person from any television platform operator(s) (or any Connected Person of any television platform operator(s)) in respect of PPV Buys of programmes, events and PPV Multiple Offerings offered as part of the relevant Licensed PPV Service on Third Party Platform(s);

- **"Third Party Revenue"** means the total sum of Third Party Monthly Subscription Revenue and Third Party Monthly PPV Revenue aggregated across the twelve (12) months in the relevant calendar year;
- **"Viewing Share Principle"** means, in respect of each month in which a Licensed Channel is wholesaled for a single wholesale price, or retailed for a single retail price, as part of a package of two or more channels, the allocation to such Licensed Channel of a proportion of such wholesale or retail price on the basis of the monthly average viewing share figures of that Licensed Channel (as determined by BARB or by the use of such other methodology or viewing data as may be agreed between the relevant licensee and Ofcom or, failing that, as Ofcom may determine) expressed as a percentage of the total monthly average viewing share figures of all of the Licensed Channels which form part of the relevant package.

**By way of example:**

in the context of wholesale revenues, if Licensed Channel A and Licensed Channel B are wholesale to the operator of a Third Party Platform for a single wholesale price and Licensed Channel A has 2% of the total monthly viewing share and Licensed Channel B has 1% of the total monthly viewing share, the single wholesale price shall be allocated in a ratio of 2:1 in favour of Channel A; and

in the context of retail revenues, if Licensed Channel A and Licensed Channel B are retailed by the operator of an Own Platform for a single retail price as part of a two (2) channel tier and Licensed Channel A has 2% of the total monthly viewing share and Licensed Channel B has 4% of the total monthly viewing share, the retail price payable by subscribers for that package of channels shall be allocated in a ratio of 2:1 in favour of Channel B.

## Calculation Of Interactive Net Revenue – Example Scenarios And Definitions

5. This Annex provides broadcasters with further detail as to how the principles set out in Section 4 of this document would operate in practice in the context of some examples of different interactive applications and services.
6. Those example scenarios are listed below and are designed to be read in conjunction with the definitions which are set out at the end of this Annex.
7. All Interactive Net Revenue received by a Relevant Person and its Connected Persons shall be included in the Relevant Turnover of that Relevant Person.

### 8. Example Scenarios

#### (i) Scenario 1

**An interactive application is accessed from a Licensed Channel by a viewer pressing the "red button" on his or her remote control. The interactive application is sponsored by Company X and contains advertisements for Company Y. The interactive application provides viewers with the opportunity to place bets on the outcome of an event depicted in the programme being broadcast on the relevant Licensed Channel.**

In this scenario, the relevant revenues which will fall within Interactive Net Revenue (and, therefore, within Relevant Turnover) will be:

- a) payments made to the Relevant Person (or any Connected Person) by Company X in respect of the sponsorship of the Interactive Application and by Company Y in respect of the advertisements contained in the application would fall within Gross Interactive Revenue because this is revenue deriving from Interactive Advertising. However, Permitted Deductions would then be deducted from Gross Interactive Revenue in computing Interactive Net Revenue;
- b) bets placed on the outcome of such event would fall within Gross Interactive Revenue as revenue deriving from an Interactive Transaction prompted by an Interactive Application which is a Betting/Gaming/Lottery Service. However, Permitted Deductions would then be deducted or excluded. Therefore, any Third Party Revenue Share of, for example, a betting service provider would be deducted or excluded from Gross Interactive Revenue in computing Interactive Net Revenue and the amount of winnings from winning bets (including stakes returned) would be excluded from Gross Interactive Revenue as a Permitted Deduction. Finally, for the avoidance of doubt, any revenue received by the Relevant Person in any capacity other than as the broadcaster or provider of the relevant Licensed Service (e.g. pursuant to a Betting and Gaming Act Licence) would not fall within Gross Interactive Revenue.

**(ii) Scenario 2**

**An interactive advertisement for certain goods is broadcast on a Licensed Channel and, by "clicking through" that interactive advertisement, the viewer may purchase those goods.**

In this scenario, paragraph (a) above (in Scenario 1) would apply in respect of the revenues deriving from the Interactive Advertising. However, any revenue which derives from the purchase of any advertised goods by the viewer would be disregarded since this derives from Retail Activity (see Paragraph (d) of the Permitted Deductions definition).

**(iii) Scenario 3**

**Two separate on-screen messages during the broadcast of a television programme prompt viewers firstly to vote in order to determine the outcome of that programme and secondly to enter a viewer competition. Votes and entries are to be submitted by text message or premium rate phone line and the necessary contact information is displayed in the on-screen message.**

In this scenario, the on-screen prompt would be a Call-To-Action and, therefore, each resulting vote and entry would constitute an Interactive Transaction. Any resulting revenue from telephony charges (calls and texts) would then fall within Gross Interactive Revenue (see paragraph (a) of that definition). Any Permitted Deductions would then be deducted in computing Interactive Net Revenue including, for example, any Third Party Revenue Share paid to or retained by any telephony operator (see paragraph (a) of the Relevant Third Party definition) and any competition prizes paid for by the Relevant Person (see paragraph (c) of the Permitted Deductions definition).

**(iv) Scenario 4**

**A viewer presses his or her "interactive" button on the remote control and accesses an interactive service via an interactive menu. He or she then registers with the provider of that interactive service to enable him or her to play pay-to-play games.**

Each payment by the viewer to play a game will constitute Gross Interactive Revenue from an Interactive Transaction in response to the content of an Interactive Service which is a Betting/Gaming/Lottery Service. Any registration fee would also be included in Gross Interactive Revenue. Any Permitted Deductions would then be deducted from Gross Interactive Revenue (including, for example, any Third Party Revenue Share) in computing Interactive Net Revenue.

**(v) Scenario 5**

**On Grand National day, a viewer presses his or her "red button" or "text" button on the remote control and accesses a digital text service which contains a "page" devoted to a bookmaker.** The bookmaker is the entity who will ultimately pay out any winnings on any winning bet placed by a viewer and is, therefore, the "provider" of the interactive service/application for these purposes. The page lists the odds on the various horses running in the race and sets out the details as to how a viewer can place a bet. This can be achieved via (i) the interactive application itself (using the return path/set top box), (ii) a premium rate phone line and (iii) a related web site of the bookmaker. All bets placed via each of (i), (ii) and (iii) will fall within Gross Interactive Revenue (subject to any Permitted Deductions e.g. any Third Party Revenue Share). However, if such contact details were not supplied on the relevant page of the digital text service and bets could not be placed

via the return path, none of the bets placed on the race would fall within Gross Interactive Revenue.

## 9. Definitions

- **"Advertising Agency Commission"** means, in the case of sales of any Interactive Advertising involving an advertising agency, any commission which is actually retained by or paid to an advertising agent provided that any such commission in excess of fifteen per cent (15%) of the amount payable by the relevant advertiser will be disregarded when computing Interactive Net Revenue.
- **"Betting/Gaming/Lottery Service"** means any Interactive Application or Interactive Service which allows or enables (for example, by the display of the necessary contact information) a viewer to carry out or engage in an Interactive Transaction which involves:
  - placing a bet of any description upon the outcome of an uncertain or unascertained event;
  - playing or taking part in gaming (for this purpose, "gaming" shall have the meaning set out in Section 52 of the Gaming Act 1968) or any game (including, for example, pay-to-play games), competition or quiz; or
  - playing or taking part in a lottery (meaning a distribution of prizes by chance where players make a payment or provide other consideration in return for their chance of winning a prize including, without limitation, lotteries falling within Sections 3, 4, 5 and/or 6 of the Lotteries and Amusements Act 1976 and the National Lottery (as defined in Part I of the National Lottery etc. Act 1993));  
  
and may include, without limitation, fixed odds betting, pool betting, spread betting, bingo, football pools, casino games (such as roulette, blackjack and pontoon), prize draws, scratch cards and pay-to-play games;
- **"Call-To-Action"** means any visual or oral prompt, invitation, on-screen message, on-air announcement and/or interactive television e-mail or message which is visible or audible during any programme, on-air promotion or advertisement broadcast on, or contained in an Interactive Application accessed via, a Licensed Service. For the avoidance of doubt, there shall be no requirement for an Interactive Application to have been launched or accessed in order for such a call-to-action to have occurred, e.g. a call-to-action may be comprised within the broadcast of a programme on a Licensed Channel;
- **"Gross Interactive Revenue"** in respect of a Licensed Service means all sources of revenue deriving from any Interactive Transaction undertaken in relation to that Licensed Service including, without limitation, revenues arising from:
  - any and all telephony charges (for example, resulting from viewer responses to any Call-To-Action (including, but not limited to,



voting and competition entries) sent via any premium rate phone lines and text messaging);

- Betting/Gaming/Lottery Services;
  - Interactive Advertising; and/or
  - any other Interactive Transaction;
- **"Interactive Advertising"** means:
    - any advertisement during which viewers are provided with a visual or oral invitation or any other prompt to launch or access an Interactive Application or Interactive Service and which provides further details of the product(s) or service(s) which is or are the subject of that advertisement; or
    - any sponsorship of any Interactive Application or Interactive Service (for example, the sponsorship of a Betting/Gaming/Lottery Service);
  - **"Interactive Application"** means any interactive application which is launched from within, or accessed from, the broadcast stream of a Licensed Service including without limitation a digital text service;
  - **"Interactive Net Revenue"** in respect of a Licensed Service means all Gross Interactive Revenue in respect of that Licensed Service less any and all Permitted Deductions from that Gross Interactive Revenue;
  - **"Interactive Service"** means any interactive service which may be accessed by a viewer via a separate menu of interactive services (for example, by pressing the "Interactive" button on any remote control or set-top box) and is licensed by Ofcom;
  - **"Interactive Transaction"** in relation to a Licensed Service means any transaction, interaction or other response by a viewer (excluding Retail Activity) which is in response to, or with, or results from or is prompted by:
    - any Interactive Application accessed via or launched from that Licensed Service; or
    - any Call-To-Action on that Licensed Service; or
    - the content or subject matter of that Licensed Service if it is an Interactive Service;

- **"Licensed Channel"** means any linear television channel or any pay-per-view service for which a licence under the Broadcasting Acts 1990 and 1996 or the Communications Act 2003 is required;
- **"Licensed Service"** of a Relevant Person means a Licensed Channel or Interactive Service for which that Relevant Person holds a licence under the Broadcasting Acts 1990 and 1996 or the Communications Act 2003;
- **"Permitted Deductions"** from an amount of Gross Interactive Revenue means each of the following categories of deductions or exclusions from that Gross Interactive Revenue:
  - any Third Party Revenue Share in relation to that Gross Interactive Revenue (but excluding, for the avoidance of doubt, any costs associated with the broadcast, design, production, building or provision of Interactive Applications or Interactive Services - for examples of such costs, see the list set out at Paragraph 36 of this Annex);
  - any revenue received by a person in any capacity other than its capacity as a Relevant Person including, without limitation, as licensed bookmaker, platform operator, provider of conditional access, access control, customer management, transmission, transponder, uplink, facilities or other technological services;
  - any stakes returned and winnings paid to viewers out of that Gross Interactive Revenue pursuant to any Betting/Gaming/Lottery Service and/or the cost to the Relevant Person of any prizes provided to viewers as part of any competition but only to the extent that such prizes are paid for directly by the Relevant Person itself;
  - any revenues from any Retail Activity;
- **"Relevant Third Party"** in respect of a Relevant Person means any of the following:
  - any telephony provider/operator by means of whose network (whether fixed or mobile) viewer responses are conveyed to that Relevant Person or any Connected Person, agent or contractor of that Relevant Person;
  - any operator of a television platform on which that Relevant Person broadcasts any Interactive Applications or provides any Interactive Service;
  - any provider of interactive "back end" services to that Relevant Person in relation to the processing and authentication of viewer responses and the provision of a "return path";
  - providers of Betting/Gaming/Lottery Services (i.e. typically, the person who is liable to pay out any winnings or prizes to participants in the relevant Betting/Gaming/Lottery Service and not the producer or provider of the content or functionality of the relevant Betting/Gaming/Lottery Service) on or via any Licensed Service broadcast or provided by that Relevant Person; and

- advertising agencies who are entitled to receive an Advertising Agency Commission in respect of sales of Interactive Advertising broadcast by that Relevant Person, and no other person;
- **"Retail Activity"** means the retailing of goods and/or services (such as holidays), but excluding Betting/Gaming/Lottery Services;
- **"Third Party Revenue Share"** in relation to an amount of Gross Interactive Revenue means any sum which is in the nature of a share of that Gross Interactive Revenue, which is earned in consideration for the provision of a service referred to in the definition of "Relevant Third Party" and which is either:
  - deducted by a Relevant Third Party from that Gross Interactive Revenue before being paid to the Relevant Person or any of its Connected Persons pursuant to a contractual entitlement including any Advertising Agency Commission; and/or
  - received by the Relevant Person but which is then paid out by the Relevant Person to a Relevant Third Party pursuant to a contractual obligation to do so including any Advertising Agency Commission.

For these purposes, any fee payable to any third party in respect of each telephone call, text message or other viewer response and which is effectively a share of telephony revenue included within Gross Interactive Revenue shall be deemed to be a Third Party Revenue Share.

# Definition of Relevant Turnover in the Radio Sector

## ASSESSMENT OF RELEVANT TURNOVER (RADIO)

### Principles Followed by Ofcom

1. Ofcom considers that the overriding principle that should be applied with regard to the computation of Relevant Turnover (Radio) is that the payment due when the appropriate percentage is applied to this computation should represent as far as possible a charge against all revenue to the extent that it derives from the licensee's possession of a radio broadcasting licence. It is this principle that should be applied when determining the Relevant Turnover (Radio) of the licensee.
2. In this document, any reference to revenues/benefits earned or received by a licensee shall also be deemed to include a reference to revenues/benefits earned or received by any Connected Person (as defined in Part 3 of Section 7) of that licensee. Accordingly, any and all revenues/benefits earned or received by any such Connected Person shall be deemed to have been earned or received by the licensee (and the charge shall be applied against the aggregate of all such revenues/benefits).
3. Where revenues are earned by a licensee from a radio service simulcast by means of an analogue signal and a digital signal (irrespective of the platform(s) on which such radio service(s) is/are distributed), Ofcom will treat all such revenues as having been earned from the analogue version of the service.
4. This is because (a) consistent and reliable audience data across all services and platforms (analogue and digital) is not currently available, (b) the revenue which is attributable to simultaneously transmitted digital services is currently insignificant (in comparison with the equivalent analogue services) and (c) it will be simpler for licensees to use and for Ofcom to administer.
5. However, in the event that there are either (i) significant developments in the measurement of audience share across all platforms (analogue and digital) meaning it is possible to apportion revenue between analogue and digital versions of services or (ii) revenues attributable to digital versions of services substantially increase (meaning it would be inequitable to continue to apportion all revenue to the analogue version of the service), Ofcom may elect to review this approach.
6. The assessment of Relevant Turnover (Radio) is based upon the statutory accounts as audited and laid before the licensee's shareholders in general meeting. If the licensee's accounting period is different from the relevant calendar year used by Ofcom the Licensee should apportion the relevant revenue from each such accounting period so as to compute the figures for the relevant calendar year. Such accounts, if accompanied by an unqualified report by the licensee's auditors, provide prima facie evidence that income is correctly recorded and expenditure properly chargeable to the revenue account.

7. Set out below are various forms of revenue and the manner in which Ofcom proposes they should be treated:

### **Broadcasting and Advertising Revenues**

8. Any amount that is received by the licensee in consideration for the inclusion of advertisements in the licensed service, shall be included within the computation of Relevant Turnover (Radio) and will be taken to be the amount paid over by the advertiser. In the case of advertisements included under an arrangement between the licence holder and a person acting as an advertising agent the amount included in the Relevant Turnover (Radio) computation shall be the amount paid over by the advertiser after the deduction of the advertising agent's commission. The maximum amount that may be deducted in respect of the advertising agent's commission shall be 15% of the payment by the advertiser.
9. Where the amount paid over by the advertiser includes a payment in respect of any costs incurred by the licensee in producing the advertisements included in the radio service, then this amount shall be included when computing the Relevant Turnover (Radio) of the licensee.
10. For the avoidance of doubt, in circumstances where the entirety of (or any part of) the advertising airtime of a licensee is sold by a licensee to a third party (for onward sale to advertisers), the revenue to be included in Relevant Turnover (Radio) shall be that received by the licensee from the third party in respect of that sale of airtime.

### **Sponsorship and Co-Funding**

11. Any payment received directly or indirectly by the licensee in relation to any programme to be included in the licensed service, shall be included within the computation of the licensee's Relevant Turnover (Radio). This will include all income derived from sponsorship and co-funding, together with any financial benefit derived by virtue of any person making payments for the purpose of defraying, or contributing towards the costs incurred, or to be incurred, in connection with the programme. In determining the licensee's Relevant Turnover (Radio), the amount included in the computation shall be the amount paid over by the sponsor or co-funding organisation, after the deduction of any advertising agent's or other intermediary's commission. The maximum amount that may be deducted in respect of any commission shall be 15% of the payment made by the sponsor or co-funder.

### **Sale or Assignment of Programme Rights**

12. Any income or benefit that accrues to the licensee in respect of any sale or assignment of programme rights to other broadcasters will not constitute Relevant Turnover (Radio) and therefore can be excluded in the assessment of the payment due to Ofcom.

### **Interactive Revenue**

13. Any income or benefit that accrues to the licensee as a result of a "Call-to-Action" broadcast on a radio service operated by the relevant licensee which invites listeners to carry out a transaction or respond to that Call-to-Action (e.g. by the submission of a vote or competition entry via a premium rate phone line or text message) will be included within Relevant Turnover (Radio). This would also include any online payment which flows from any Call-to-Action (e.g. the downloading of a song from an associated website (e.g. [www.radiolicensee.co.uk/radiopromotion](http://www.radiolicensee.co.uk/radiopromotion)))

whose URL is referred to in a Call-to-Action).

14. A "Call-to-Action", for this purpose only, means any oral prompt, invitation, on-air announcement, on-air promotion or advertisement broadcast on a radio service operated by the licensee.

### **Broadcast Airtime Sales**

15. Any income or benefit that accrues to the licensee in respect of any sale or other disposal to any third party of any airtime on the radio service (other than that falling within (a) and/or (b) above) would be included within Relevant Turnover (Radio). For example, this would catch any revenue received by a licensee from the sale of a 2 hour block of airtime to a third party in circumstances where that third party provides its own content for broadcast during that 2 hour block.

### **Subscription Revenue**

16. At this stage, given there is little or no subscription revenue earned by licensees in respect of radio services, Ofcom does not propose this form of revenue should fall within Relevant Turnover (Radio). However, should subscription-based business models evolve in due course in the radio environment, Ofcom reserves the right to revisit this form of revenue and to consider whether it should be included in Relevant Turnover (Radio).

### **Non-Broadcasting Related Revenues**

17. Income from events, promotions, the provision of services or other activities which have no direct or indirect link to the licensed service, will not be counted in the computation of Relevant Turnover (Radio).

### **Investment Income and Income from Asset Disposals**

18. Investment income from interest and dividends would be excluded, together with the proceeds of asset sales (other than airtime sales).

### **Merchandising and Hire of Facilities**

19. Income derived from merchandising activities (the sale, for example, of promotional goods or services with the intention of making a profit), together with income derived from the hiring out of facilities to third parties, would not be included within the computation of Relevant Turnover (Radio).

## Annex 3

# Ofcom's consultation principles

Ofcom has published the following seven principles that it will follow for each public written consultation:

### Before the consultation

1. Where possible, we will hold informal talks with people and organisations before announcing a big consultation to find out whether we are thinking in the right direction. If we do not have enough time to do this, we will hold an open meeting to explain our proposals shortly after announcing the consultation.

### During the consultation

2. We will be clear about who we are consulting, why, on what questions and for how long.
3. We will make the consultation document as short and simple as possible with a summary of no more than two pages. We will try to make it as easy as possible to give us a written response. If the consultation is complicated, we may provide a shortened version for smaller organisations or individuals who would otherwise not be able to spare the time to share their views.
4. We will normally allow ten weeks for responses, other than on dispute resolution.
5. There will be a person within Ofcom who will be in charge of making sure we follow our own guidelines and reach out to the largest number of people and organisations interested in the outcome of our decisions. This individual (who we call the consultation champion) will also be the main person to contact with views on the way we run our consultations.
6. If we are not able to follow one of these principles, we will explain why. This may be because a particular issue is urgent. If we need to reduce the amount of time we have set aside for a consultation, we will let those concerned know beforehand that this is a 'red flag consultation' which needs their urgent attention.

### After the consultation

7. We will look at each response carefully and with an open mind. We will give reasons for our decisions and will give an account of how the views of those concerned helped shape those decisions.

## Annex 4

# Consultation response cover sheet

1. In the interests of transparency, we will publish all consultation responses in full on our website, [www.Ofcom.org.uk](http://www.Ofcom.org.uk), unless a respondent specifies that all or part of their response is confidential. We will also refer to the contents of a response when explaining our decision, unless we are asked not to.
2. We have produced a cover sheet for responses (see below) and would be very grateful if you could send one with your response. This will speed up our processing of responses, and help to maintain confidentiality by allowing you to state very clearly what you don't want to be published. We will keep your completed cover sheets confidential.
3. The quality of consultation can be enhanced by publishing responses before the consultation period closes. In particular, this can help those individuals and organisations with limited resources or familiarity with the issues to respond in a more informed way. Therefore Ofcom would encourage respondents to confirm on the response cover sheet that Ofcom can publish their responses upon receipt.
4. We strongly prefer to receive responses in the form of a Microsoft Word attachment to an email. Our website therefore includes an electronic copy of this cover sheet, which you can download from the 'Consultations' section of our website.
5. Please put any confidential parts of your response in a separate annex to your response, so that they are clearly identified. This can include information such as your personal background and experience. If you want your name, contact details, or job title to remain confidential, please provide them in your cover sheet only so that we don't have to edit your response.



## Cover sheet for response to an Ofcom consultation

### BASIC DETAILS

Consultation title:

To (Ofcom contact):

Name of respondent:

Representing (self or organisation/s):

Address (if not received by email):

### CONFIDENTIALITY

What do you want Ofcom to keep confidential?

Nothing

Name/contact details/  
job title

Whole response

Organisation

Part of the response

If there is no separate annex, which parts?

If you want part of your response, your name or your organisation to be confidential, can Ofcom still publish a reference to the contents of your response (including, for any confidential parts, a general summary that does not disclose the specific information or enable you to be identified)?

Yes

No

### DECLARATION

I confirm that the correspondence supplied with this cover sheet is a formal consultation response. It can be published in full on Ofcom's website, unless otherwise specified on this cover sheet, and all intellectual property rights in the response vest with Ofcom. If I have sent my response by email, Ofcom can disregard any standard email text about not disclosing email contents and attachments.

Ofcom can publish my response: on receipt

once the consultation ends

Name

Signed (if hard copy)