Office of Utility Regulation

Fees for

Telecommunications Licences

Report on the Consultation Paper
and Decision Notice

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1. Introduction

In August 2002, the Director General of the Office of Utility Regulation ("the Director General") published a consultation paper, Document OUR 02/31 on proposals for establishing a mechanism for calculating and collecting licence fees for telecommunications licences throughout the lifetime of the relevant licence.

Following the setting of fees for the first year of operation of the Office of Utility Regulation ("OUR"), the Director General reviewed the most appropriate mechanism to be used in setting annual licence fees, given the imminent changes in the market within the Bailiwick such as new entrants and the likelihood of multiple licensees in both the fixed and the mobile markets in the near future.

The OUR received responses to the Consultation Paper from Cable & Wireless Guernsey Limited ("C&WG"), Jersey Telecom ("JT") and Newtel Limited. This report sets out the Director General's conclusions on the issues raised in the Consultation Paper following consideration of the responses received. The Director General wishes to thank these respondents for their contributions in helping to shape the regulatory regime. With the exception of the responses marked as confidential, the written comments are available for inspection at the OUR's office.

Section 2 provides some background information to the report whilst Section 3 considers the responses received to the proposed mechanism described in OUR 02/31. Section 4 addresses respondents' views on the Director General's proposals for rebates for excess fees and the collection of any shortfall. Section 5 deals with the proposed structure and contents of the accompanying guidelines. The Guidelines themselves are published as a separate document (Document OUR 02/39) which is available from the OUR website.

2. Background

The original consultation paper provided detailed background information describing the legislative background, the rationale behind the first year licence fees and the establishment of the Public Utilities Regulation Fund.

2.1 Legislative Background

The Regulation of Utilities (Bailiwick of Guernsey) Law, 2001 ("The Regulation Law") and the Telecommunications (Bailiwick of Guernsey) Law, 2001 ("the Telecommunications Law"), together empower the Director General to regulate the telecommunications market in the Bailiwick of Guernsey.

The Director General's functions[1] include *inter alia*, determining and prescribing the fees and levies payable on an application for, or the grant or renewal of, or over the term of, a licence, and the interest and penalties payable in the event of a default in the due payment of the fees or levies. The Director General is also required to publish fees and the fees or levies charged are expected to meet the costs of the OUR over the term of the licence in connection with the exercise of the Director General's functions and powers.

The Director General is also required to establish a fund known as the "Public Utilities Regulation Fund" in to which licence fees shall be paid and from which costs of the Office of Utility Regulation shall be paid; maintain proper accounts, have the accounts independently audited and submit the audited accounts along with its annual report to the States.

2.2 First Year Licence fees

In advance of the establishment of the OUR, the Director General estimated the cost of regulating the first licensees in the three markets for which she has responsibility (post, telecommunications and electricity) for the first full financial year of operation of the Office and proposed to apportion those costs across the three sectors based on an estimate of the percentage of time and effort that would be required in each sector. Having consulted with each of the three organisations that would be licensed in the first year (Guernsey Post, Guernsey Telecoms and Guernsey Electricity), she set fees for the Office's first financial year based on that apportionment estimate (see document OUR 01/11).

She also stated that following the conclusion of the first full financial year of operation of OUR she would review these amounts and the split between the various sectors and make adjustments as appropriate. That review will be undertaken when a full year of data is available, i.e. after 31st December 2002.

2.3 Public Utilities Regulation Fund

The Director General has established the Public Utilities Regulation Fund in accordance with the legislation and the Fund has been audited up to the end of the first calendar year (i.e. to 31st December 2001), during which OUR operated for three months only.

The 2001 Accounts and Annual Report of the Director General have been submitted to the Board of Industry in accordance with the Laws and will be presented to the States of Guernsey at its meeting in November 2002[2]. The Annual Report and Accounts for the calendar year 2002 will be available as soon as practicable in 2003.

[1] In accordance with section 4(1)(d) of the Regulation Law and section 6 of the Telecommunications Law

[2] The OUR annual report and accounts have been published in Billet d'Etat for November 2002 which will be available from the Guernsey Government website www.gov.gg. Alternatively the annual report is available on the OUR website at: http://www.regutil.gg/docs/annual_report_2001.pdf

3. Telecommunication Fees Over The Term of a Licence

3.1. Mechanism for setting fees

The Director General set out her views in the Consultation Paper that determining annual licence fees on the basis of relevant turnover was a reasonable and objective mechanism for apportioning the costs of regulation across all players in the market, could cope with the uncertainty over the number of licensees in a newly liberalising market, and related the licence fee fairly to the activity of the players in the market. This approach has a proven track record and has been adopted in many jurisdictions. The Director General therefore proposed to adopt the mechanism of setting ongoing fees based on a percentage of turnover of telecom licensees for future years' operation of the OUR.

Views from Respondents

Two respondents, supported the Director General's proposal while the third stated its preference for a mechanism based on a flat fee structure related to the type of licence, justified by reference to OUR costs and apportioning these costs on the basis of regulatory work generated by different types of licensee. The respondent believed that this mechanism could adequately address issues such as uncertainty over numbers of licensees. In response to a later question, this respondent further suggested that a range of relevant turnover thresholds should command a sliding scale of fees.

One party raised some practical considerations for example relating to the definition and verification of relevant turnover and these are addressed in the guidelines set out in document OUR 02/39.

Director General's Position

The Director General welcomes the support from two of the respondents for the proposed mechanism for setting annual licence fees and notes the view of the third respondent.

Having considered the responses, the Director General maintains the view that a percentage of turnover approach is more appropriate than a flat fee structure for the following reasons:

First, in the early stages of liberalisation of the telecommunications market there is no precedent or basis for estimating the exact number of new entrants, and the Director General considers it would be inappropriate to make such estimates and could send inaccurate signals to the market. She does not agree with the dissenting respondent who believes that the setting of a flat fee would in fact be better designed to deal with the uncertainty over numbers of Licensees but notes that the respondent agrees that such uncertainty exists in the early years and will reduce over time.

Second, the Director General believes that the mechanism adopted should relate the fee paid to activity and size of operators in the market. The suggestion that bands or thresholds of turnover be set and a sliding scale of fees applied simply involves a more cumbersome and less precise variation of the application of a percentage of turnover approach and seems to bring no additional benefits.

Third, the setting of flat fees related to "types" of licences would involve even greater administrative overhead, including a redesign of the Guernsey telecommunications licensing regime and could be inequitable as there is no reason to believe that costs incurred by OUR would be related to the type of activity rather than the level of activity in the market.

The Director General has therefore decided to set annual licence fees for telecommunication licensees based on a percentage of relevant turnover.

Decision 3.1

The Director General will apportion the costs of regulation across all telecommunication licensees by setting annual licence fees based on a percentage of relevant turnover.

3.2. Level of Fees

Having decided upon using the percentage of relevant turnover as the appropriate mechanism to use to allocate the OUR's annual operating costs across all of the regulated licensees in the sector, the total level of the income collected remains directly related to the costs of the Regulator's office in regulating that sector

In document OUR 02/31 the Director General set out her proposal to set the ongoing annual license fee for all telecommunications licences at 1% of relevant turnover, including the incumbent operator, C&WG.

In addition, to address the situation of new entrants who may have very low turnover in the initial stages of their business, as well as Licensees operating with a very low level of turnover on an ongoing basis, the Director General proposed that any Licensee with relevant annual turnover of less than £150,000 would pay an annual licence fee of £500 per annum, irrespective of turnover.

Views from Respondents

Two respondents agreed with the Director General's proposals that the licence fee should be based on a percentage of turnover and that there should be a flat fee for licensees below a set turnover. The third respondent disagreed on the basis that there is not a direct relationship between turnover and the demands on OUR's time and resources, and the introduction of a turnover based approach may be premature and would be difficult to amend once introduced. Respondents made a number of other detailed comments which are grouped below.

<u>Level of the Fee</u>

One respondent commented that the actual level (1% of turnover) was excessive and should be capped and quoted the UK and other European countries' fees in support of its argument. The same respondent suggested that the proposed flat annual fee of £500 for licensees with a turnover below £150,000 was too low having regard to the likely work associated with each licensee and also that the proposed turnover level below which a flat fee would apply was too low.

Structure of the Fee.

One respondent suggested that the percentage fee should vary in inverse proportion to the level of turnover – being less for companies with larger turnovers – based on the fact that this approach is adopted in Greece. Another, while acknowledging that the mechanism proposed would ensure the market position of the dominant incumbent operator would be reflected in a higher licence fee, expressed the concern that the definition of relevant turnover means that certain parts of the dominant operator's turnover might be excluded from the fee calculation and suggested that this could be addressed by a specific fee levied on the dominant incumbent

Director General's Position

Level of Fees

The Director General is required by law to raise fees to defray the costs of running her office and carrying out the statutory functions assigned in law. It would be inappropriate and potentially ultra vires the Director General to fetter the functions of the statutory Office by capping the level of fees to be raised. Such an approach could also potentially restrict the Office's ability to carry out the range of functions assigned to it in law, due to insufficient funding. The States of Guernsey has set out the parameters that govern the operation of the Office and the Director General will continue operate within these parameters when exercising her functions, including the function of setting fees.

With regard to the proposed level of the flat fee for licensees with turnovers of less than £150,000, the argument by one respondent that this would not cover the initial costs associated with regulating these licensees is not accepted. In particular, the administrative costs of initial entry into the market (i.e. licence evaluation and award) will be met by the application fee for the licences.

Structure of the Fee

The proposal that a sliding scale of percentage rates, inversely related to relevant turnover is unsupported by any reasons and the Director General sees no benefits in this approach.

In support of its argument for alternative approaches, one respondent suggested that there is no direct relationship between turnover and demands on the regulator's resources. The Director General does not accept this and notes that a clear relationship between turnover and time spent on regulating the market has been established by Oftel[3] in the UK, and many other jurisdictions also use it as it provides a fair and simple mechanism for relating the licence fee to the activities of the regulator.

With regard to the fee paid by the dominant operator, the Director General believes that by relating the fee to the turnover of the operator in the market, its dominance will be taken into account.

In conclusion therefore the Director General considers that the level of fees should be set at 1% of relevant turnover for all licensees with relevant annual turnover in excess of

[3] A Review of Telecommunication Licence Fees in the UK, November 1998

£150,000. The annual licence fee for those operators with relevant turnover below this threshold will be £500.

Decision 3.2

All licensees will pay an annual licence fee to cover the annual operating costs of the OUR. The charge will be 1% of relevant turnover for all licensees whose relevant annual turnover is more than £150,000. Licensees with relevant turnover below this amount will pay a flat fee of £500 per annum.

4. Rebate of Excess Fee and Collection of Shortfalls

In document OUR 01/11 the Director General decided that in the event that the Office of Utility Regulation collects licence fees that are greater than the amount needed to carry out the relevant functions assigned by Law, the Director General will refund the excess to licensees. She proposes to continue with this practice. As a matter of expediency the Director General reserves the right to make rebates by means of a reduction in the amount of the annual licence payable for subsequent years of by offset against any other amount owed by licensees.

She also decided that in the event of any shortfall arising, she will consider making up such a shortfall by:

- imposing an additional fee or levy on the licensees within the calendar year in which the shortfall arises; or
- obtaining short term funding and increasing licence fee or levy in the following calendar year; or
- seeking loans or grants from the States in accordance with section 10 of the Regulation Law if appropriate.

The mechanism to be used will depend on the nature and size of any shortfall and will be decided on a case by case basis.

Views from Respondents

There was general agreement in relation to the mechanism for rebates, and two of the respondents comment on the issue of dealing with shortfalls. Comments included:

- the mechanism for making up shortfalls should be decided in advance along with guidance and criteria for the decision;
- the timing of any action needs to be specified, i.e. when a shortfall would be calculated and when any addition fee might be imposed;
- there is too great a degree of uncertainty with respect to the level of any shortfall that a licensee might fall liable to pay and operators should receive quarterly updates on the expenditure and funding status.

Director General's Position

The Director General notes that the issues raised are matters of detailed implementation and will consider these when managing any shortfall or rebate. However, she considers that the principles outlined in OUR 01/11 are appropriate and she will continue to adopt this approach.

The existence of any shortfall or excess will be finalised in the context of the auditing of the OUR accounts at the end of the calendar year. The Director General believes it is inappropriate and unduly onerous to develop complex guidelines on how rebates or shortfalls will be handled in advance of that calculation and will consider matters of implementation in the light of experience.

Decision 4.1

The Director General will continue the practice set out in OUR 01/11 in relation to shortfalls and excesses and will handle these issues in accordance with the Guidelines.

5. Issues to be Included in Guidelines

In the Consultation Paper the Director General gave notice of her intention to prepare more detailed guidelines on the operation of the mechanism for setting licence fees. The Director General proposed that the guidelines would include as a minimum the following information:

- Persons and Organisations Liable to pay the Fees
- Licence Fee Year
- Relevant Turnover
- Frequency of Payment
- Calculation of Fee: Information to be provided

Respondents were invited to comment on these points and to suggest other issues that might be addressed in the guidelines and how such issues should be addressed.

Views from Respondents

Respondents raised a number of additional questions and highlighted areas that needed to be included within the Guidelines.

One respondent explicitly welcomed the Director General's proposal to change from monthly to quarterly payments. Another suggested that the guidelines could include provisions outlining how a flat rate fee approach for licensees with lower turnovers would be handled and how this could evolve into a turnover based fee.

Director General's Position

The Director General is grateful for the comments received from the respondents to the consultation and their comments have been considered in the preparation of the guidelines.

/ENDS