Oaseirys Çhellinsh
Communications Commission

Licensed activities:

Guidelines for calculating the licence fee

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Background

The IOM telecommunications licences provide for a licence fee to be paid by all licensed operators. The legal background is set out in Annex 1. The structure and level of the fee differ according to the type of licence held, but the underlying premise is that an initial fixed sum is followed by an annual payment representing a percentage of turnover. 'Turnover' is defined as the 'total revenue generated by the provision of Electronic Communications Networks and Services under this Licence for the financial year ending immediately before the due date for payment of the fee'. The licences provide that the percentage of turnover may be modified by the Commission with the consent of the Treasury, in order to reflect current regulatory costs.

The Commission's decision to review the licence fee process was prompted by change in telecommunications technologies, and in the market. As telecommunications technologies evolve and converge with previously distinct technologies such as broadcasting, it is necessary to clarify where the boundaries lie in what may be considered to be electronic communications networks and services, because the licence fee is directly related to the definition of electronic communications. At the same time, telecoms operators are increasingly expanding their areas of activity – for example, by running data centres – and their geographical reach. In addition, telecoms services are increasingly sold as bundled services, with some elements of the bundles (for example, the provision of mobile handsets) potentially falling outside the definition of licensed services.

The Commission initiated its review by seeking input from operators on their current activities. Follow-up discussions have been undertaken with all operators, in person or by email and the Commission wishes to thank operators for their constructive engagement. The purpose of these guidelines is to propose a set of clear rules that determine the revenues to which the licence fee applies, how revenues are reported to the Communications Commission, and whether or not revenues earned from specific products and services are included or excluded. The Communications Commission's aim is to clarify the revenue reporting process resulting in the calculation of a licence fee, with a view to establishing a consistent and fair approach which will be followed by all operators. The Commission will then assess the implications of proposed changes on licence fee payments, with a view to ensuring that licence fee payments cover regulatory costs.

Approach

The Commission's proposals are derived from the legal context in the Isle of Man, as set out in the Telecommunications Act 1984 and the operator licences. The Commission has also considered practice elsewhere, in order to ensure that the Isle of Man follows best international practice. In particular, the Commission has taken into account the approaches of the International Telecommunications Union (ITU), and the European Union (EU). The ITU publishes guidelines on the definition and collection of administrative data, which reflect agreed international best practice.[1] Many of the EU National Regulatory Authorities (NRAs) have published guidelines and methodologies for the collection and reporting of administrative data. In addition, BEREC[2] has published guidance on various aspects of regulatory accounting which are relevant.

Geographical scope

The Operator are licensed to run "…telecommunication systems (as) specified in (the licence) within the Isle of Man…". In the Commission's view, this means that some part (but not necessarily all) of the telecommunications service should take place in the Isle of Man. For example, revenue from any service which involves origination in the Isle of Man would be included, even if termination is off-island. So for example, a retail leased line which is "A" ended in the Isle of Man would be included, even if the line terminates outside the Isle of Man. Conversely, pure transit, where there is no origination, switching or termination in the Isle of Man, would not be included. Similarly, where an earth station is being used only for telemetry, tracking and control (TT&C), or to provide services for off-island customers, revenue from such services would not form part of the eligible revenue for the purposes of calculating the licence fee.

The Commission believes that there is a case for allowing operators to deduct wholesale off-island costs from their retail revenues. This would mean that, for example, the operator would include for the purposes of calculating the licence fee all the revenue from an "A" ended retail leased line going from the Isle of Man to another jurisdiction, but would then deduct the wholesale costs associated with off-island connectivity. Similarly, off-island wholesale circuit costs used for retail internet connectivity could be deducted from the retail revenue associated with internet provision. This recognises that part of the revenue is for activity off-island, and removes the anomaly of paying a licence fee based on high revenue without recognising the potentially high (and possibly very high) costs incurred for off-island activity. The rationale for this is that part of the activity is off-island, and it should be clear that this approach does not apply to on-island connectivity.

The ownership of the operator is immaterial – it is the location of the telecommunications service that is significant. So, for example, an Isle of Man company which had invested in mobile networks in several countries would only count its annual gross turnover in the Isle of Man for this purpose. Similarly, an externally-owned company which holds a licence in the Isle of Man would only count its turnover in the Isle of Man.

Conclusion: revenue is that associated with telecommunications services provided in whole or in part the Isle of Man

[1] ITU, *Handbook for the collection of administrative data on telecommunications/ICT*, updated note on the methodology for the collection of revenue and investment data on telecommunications, Geneva 17 February 2014

[2] Body Of European Regulators of Electronic Communications

How is turnover defined?

The definition of turnover considered to be eligible for the application of a licence fee is set out in the operator licences[3] as follows:

> *"**Turnover**" means the total revenue generated by the provision of Electronic Communications Networks and Services under this Licence.*

The starting point is therefore that gross revenue from **all** electronic communications networks and services provided in the Isle of Man should be considered eligible when calculating the licence fee.

This issue has been addressed by other agencies. The ITU has set out a definition[4] of what should be considered as constituting revenue from telecommunications services, and the key points for the financial year under review are:

- Revenue should include that from fixed, mobile, internet and data services;
- Revenue from the transmission of TV signals should be included, but from TV content creation excluded;
- Revenue from device sales should be excluded;
- VAT and excise taxes should be excluded.

In the UK, Ofcom is currently consulting on a revision to its principles for setting licence fees.[5] Ofcom has defined a "relevant activity" for the purposes of setting a licence fee as constituting the provision of electronic communications services (ECS) to third parties and to communications providers, and the making available of associated facilities to communications providers.

This definition is derived from the UK Communications Act. The point to note from the Ofcom example is that the definition of a telecommunications activity is based on the conveyance of signals over a network, and includes facilities that are necessary to enable that conveyance. Equipment, such as handsets and other customer premises equipment (CPE), is not included, and neither are services that are not specifically to do with the conveyance of signals over an electronic communications network.

A second EU example is that of the Netherlands. Its definition of licensed activities includes the following:

[3] See Annex 1 for the legal background

[4] The ITU approach excludes wholesale revenue. However, the ITU's methodology is one based on net turnover.

[5] Ofcom, *Principles for setting licence fees and administrative charges,* Preliminary consultation, 27 March 2014

"…***electronic communication network:*** *transmission systems, which are deemed to include switching or routing equipment and other resources that render it possible to transmit signals by means of cables, radio waves, fibre optic or other electromagnetic means, including satellite networks, fixed and mobile terrestrial networks, electricity networks in so far as they are used to transmit signals, networks for radio and television broadcasting, and cable television networks irrespective of the information transmitted;*

- ***electronic communication service:*** *usually provided for a fee, this service consists entirely or predominantly of transmitting signals through electronic communication networks, including telecommunication services and transmission services on networks used for broadcasting purposes, though not the service that entails the supply or editorial verification of content transmitted with the aid of electronic communication networks and services. This does not include any services from the Knowledge Economy …..which does not consist entirely or predominantly of transmission of signals through electronic communications networks;*

…….

- ***providing an electronic communication network:*** *building, exploiting, managing or making an electronic communication network available;*
- ***related facilities:*** *any facilities relating to an electronic communication network or service which facilitates or supports the provision of services through that network or by means of that service, as well as any conditional access systems and electronic programme guides…*"[6].

As with the UK example, the focus is on the transmission of signals over an electronic communications network, and there is an explicit exclusion of the provision of content. The approach taken by the ACM in the Netherlands also emphasises technological neutrality – it makes no difference whether turnover is achieved by fixed, mobile, cable or satellite networks and services, and it makes no difference whether the signals are to do with transmitting speech, data or imaging.

The Netherlands regulator includes in its relevant turnover definition any fees payable for activities that are undertaken for the purpose of supplying public electronic communications services, public electronic communications networks and related facilities. In the ACM's view, these constitute part of the (telecommunications) services agreed upon by the customer and the provider. Such services include disconnection fees, income from help desk activities, relocation, lapsed call credit, connection and reconnection fees and income from subscription changes.

The Commission's view is that the legal basis in the Isle of Man is sufficiently similar to that of the EU to propose that the IOM approach should be derived from the provision of electronic communications networks and services. The approach should be technologically neutral.

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[6] ACM, *Instructions for submitting turnover details*.

Conclusion: all operator turnover generated by the provision of electronic communications networks and services in the Isle of Man is eligible for the calculation of the licence fee.

Should revenue from wholesale and retail sales be included?

There are different ways of accounting for wholesale and retail revenue. In the Isle of Man, separated accounting information is required of some operators (generally those with SMP obligations) in some markets, so that there is a clear distinction between wholesale and retail revenues. This may include a real or notional transfer charge between the wholesale and retail arms of the operator in question. In these cases, wholesale revenue could include both the wholesale merchant market supply (where the operator sells wholesale services to another communications provider) and the vertically-integrated operator's self-supply (where the operator supplies its own downstream retail arm).

The ITU suggests that reported turnover for the calculation of a licence fee should not include wholesale revenue, because wholesale sales revenue would be captured in the retail market. This would be the case where an operator buys a wholesale input from another operator (usually the incumbent) to include in its own retail offer. So, for example, an OLO could buy a wholesale leased line which it then sells to a retail customer, either as a retail leased line or as part of a VPN. It could be considered that from a revenue reporting perspective, this revenue would be double counted, because the wholesale price would be passed on to the retail customer, and the associated revenue would be realized in the retail market data.

The main areas of wholesale revenue generation in the Isle of Man are likely to be wholesale supply by the incumbent in the fixed market, on the foot of SMP regulation, and wholesale termination by MT and Sure in the mobile market. The Commission recognises that there will be some "double-counting" where a wholesale product is directly related to retail revenue. However, this is not the case with all wholesale products. For example, an OLO could buy a wholesale leased line as mobile backhaul, which would effectively be the extension of its own network rather than a retail offering, and would have no direct retail revenue implications. Also, a mobile operator could generate wholesale revenue from terminating calls in the Isle of Man which originated off-island, and where there would be no direct retail charge on-island.

The Commission notes that the ITU approach of relying only on retail revenue and not considering wholesale revenue may be appropriate where the calculation is of net revenue – that is, where costs are factored in as well as revenues. In such a circumstance, the operator supplying the retail revenue deducts the wholesale cost. This is not the case in the Isle of Man.

The Commission has two main options. It could ask operators to identify wholesale revenue which is associated directly with retail revenue in the Isle of Man, and to exclude this from the total revenue figures, leaving only wholesale revenue which does not have a direct retail value. This would avoid double counting wholesale input revenue which forms part of a retail product or service, while capturing wholesale revenue which does not have associated retail revenue. However, it is likely to be a cumbersome process for operators, because it is unlikely that this data is currently collected in a suitable form. Alternatively, the Commission could follow Ofcom's approach[7], which considers "relevant activity" for the purposes of administrative charging to mean the following:

a) the provision of electronic communication services to third parties;
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

The Ofcom definition therefore includes electronic communications services provided to third parties, that is, retail customers, and to communications providers, who are wholesale customers. It is considered that the Isle of Man telecommunications licences define conditions which include wholesale and retail supply (i.e. supply to end users and to OLOs) and so total revenue should include both wholesale and retail revenue. However, the Commission proposes that the inclusion of wholesale revenue should be restricted to the merchant market (that is, in sales to other operators), and that self-supply (whether actual or notional revenue) should not be included. This is a practical means of mitigating the effect of "double counting".

The Commission also proposes, as outlined earlier, to allow operators to exclude off-island wholesale input costs when reporting on retail revenues, to avoid a situation where operators might be obliged to report high retail revenues earned on products that incur a correspondingly high wholesale cost that relates to putting in place off-island connectivity.

The Commission notes also that the benefits of wholesale regulation accrue primarily to OLOs, and eventually to end-users. It therefore seems reasonable that some of the cost of wholesale regulation is shared by OLOs in their contribution to the licence fee.

Conclusion: wholesale and retail revenues should be included as relevant turnover.

Are there products and services which should be excluded?

As telecommunications services evolve and converge, and as operators extend their activities, it is necessary to clarify any service types which may not be considered to be electronic communications, and so would not be part of the turnover which is eligible for the calculation of the licence fee. Experience elsewhere suggests that there are two key areas to be considered:

- Content
- Equipment

[7] Ofcom, *Designation and relevant activity guidelines for the purposes of administrative charging*, 31 March 2005

These areas are discussed in turn below.

Content

The ability of electronic communications networks to carry different types of signal means that previously distinct media are converging. Of particular relevance is the increasing convergence of previously distinct broadcast and telecommunications technologies, where TV programming can now be delivered over a telecommunications network (for instance cable TV or IPTV) as well as by traditional broadcast.

In the Commission's view, the guiding principle is that, where a telecommunications operator offers a service which includes content (for example TV programming), the eligible turnover would be the conveyance over the communications network, but not any creation of content. This means that any revenue from content creation should not be included in the operators' turnover for the calculation of the licence fee. However, the transmission of content over an electronic communications network should be included. This is consistent with best practice elsewhere.

The ITU has summarised the status of different types of content-based services as shown in the table below.

Table 1: ITU classification of content-based services

	Included	**Excluded**
Free to air TV	No	Yes
Pay DTT channels	No	Yes
IPTV	Yes	No
Cable TV	Internet/PSTN access Multi-channel distribution	Content creation
Satellite	Internet/PSTN access Multi-channel distribution	Content creation

Source: ITU ibid

Conclusion: reported revenue should not include the creation of content, but should include the transmission of content over an electronic communications network

Equipment

International best practice indicates that Customer Premises Equipment (CPE) should not be considered part of the turnover which is eligible for calculating the licence fee. This would include, for example, fixed and mobile handsets, mobile dongles, broadband routers and business end-user equipment.

The exclusion of CPE from the reported turnover raises particular issues when CPE is bundled with services where the revenue is included within the relevant turnover. For example, an operator which sold a mobile handset on its own would not include the associated revenue in its reported turnover. However, how would it account for revenue from a bundle which includes a mobile handset?

Bundles are usually sold at a price that includes a discount that is attributed across the products and services in the bundle. This creates an issue for attributing revenues to the individual bundle components, in particular where the individual services are not sold on a stand-alone basis.

The attribution of value to the elements of a bundle has been the focus of much attention by regulators, not just in the calculation of relevant turnover, but also in SMP regulation – for example in ensuring that there is no cross-subsidy between services provided in markets subject to SMP regulation and markets which are not. There are therefore many examples of attempts to clarify how bundles should be valued, and the selected approach is mainly dependent on how prescriptive the regulator wishes to be. Some regulators ask that operators explain and justify their methodology for identifying excluded revenue associated with equipment. However, while this places the onus on the operator, it runs the risk of every operator choosing a different methodology. Other regulators have very detailed and prescriptive methods for identifying and valuing bundle elements.

The Commission notes that guidance from the International Financial Reporting Standards (IFRS) body on recognition of revenue from contracts with customers provides a useful approach, and one which corresponds to international best practice. In particular, IFRS 15, when applied to, for example, mobile contracts requires a company to allocate the transaction price - which would be the amount that the customer pays on entering into the contract and the monthly payments for the network services - to the mobile phone and the network services on the basis of the relative stand-alone selling prices of each item. Consequently, some revenue will be recognised when the handset transfers to the customer (even if the handset is marketed as 'free') and the remaining revenue will be recognised when the network services are provided. IFRS 15 will be a required reporting standard form January 2017, and in the Commission's view, it provides guidance for how operators may exclude revenue associated with the unlicensed elements of a bundle.

Conclusion: reported revenue should exclude CPE, including customer handsets, mobile dongles, broadband routers. Where CPE is sold as part of a bundle, the operator may deduct the value of the CPE from the revenue associated with the bundle. The Commission proposes that this is done in line with accounting standard IFRS15.

Reporting process

At present, operators report headline revenue figures to the Commission and are responsible for calculating the associated licence fee. The Commission aims to put in place a process which is transparent and consistent, and which ensures that the data provided are reliable and verifiable. However, the process should not constitute an undue burden on operators.

To assist operators in submitting their revenue reports, a template is provided in Annex 2 as an illustration of the level of information required.

It is expected that the revenue figures from which the licence fee derives are aligned, where relevant, with figures reported in the company accounts. The Commission does not intend that revenue reporting for the purposes of calculating the licence fee should be subject to any delay associated with the preparation of accounts, and proposes therefore that the revenue figures should be certified by a responsible person within the company, for example the CFO and/or CEO. Should there be any subsequent variation between revenue figures submitted and those in the accounts, the Commission would expect an explanation.

The Commission reserves the right to require revenue figures to be certified by an auditor. The Commission also reserves the right to examine submitted data, and to request further detail, including audited accounts and/or other information, to verify the licence fee calculation. Operators' licences and the Telecommunications Act 1984 contain provisions on the powers of the Commission to secure information.

Conclusion: revenue information and licence fee calculation should be certified by a responsible officer of the operator's company.

Annex 1: Legal background

The 1984 Telecommunications Act provides that an Isle of Man licence may include the requirement to make a payment to the Treasury on the granting of the licence, and/or payments during the lifetime of the licence:

Para 5.5 (b)

A licence granted under this section may include….
(b) conditions requiring the rendering to the Treasury of a payment on the grant of the licence or payments during the currency of the licence or both of such amount or amounts as may be determined by or under the licence; and
[Para (b) amended by Treasury Act 1985 Sch 2.]

Paragraph 1 of operator licences sets out the granting of the licence:

*The Council of Ministers, in exercise of the powers conferred on them by section 5 of the Telecommunications 1984 (the "**Act**"), hereby grants to [the operator] (a company incorporated in the Isle of Man) (the "**Communications Provider**") a licence, for the period specified in paragraph 3, subject to the conditions set out in Schedule 1 and to revocation as provided for in Schedule 2 to run telecommunication systems specified in Schedule 3 within the Isle of Man (the "**Communications Provider's Network**") and authorises the Communications Provider to do all or any of the acts specified in Schedule 4.*

The "Communications Provider's network" is defined[8] as:

*For the purposes of this Licence "**Communications Provider's Network**" means any or all of the telecommunication systems run by the Communications Provider unless the context otherwise requires.*

The operator licences specify[9] the payment of fees as follows:

PAYMENT OF FEES
The Communications Provider shall pay, or cause to be paid, to the Treasury:
On [licence date], the [fixed sum]; and
On [anniversary of licence date], and annually thereafter:
(a) on the first £1,000,000 (one million pounds) of Turnover, a fixed sum of £5,000 (five thousand pounds); and

(b) 0.5 per cent of any Turnover in excess of £1,000,000 (one million pounds).

[8] For example, MT licence para 7; Sure licence para 6.

[9] For example, MT licence para 26; Sure licence para 23; Wi-Manx licence para 24.

The percentage of Turnover specified in paragraph [above] may be modified by the Commission with the consent of the Treasury, in order to reflect current regulatory costs, at any time after the end of the fifth year after the grant of this Licence.

The operator licences define turnover as follows:

*For the purposes of this Condition "**Turnover**" means the total revenue generated by the provision of Electronic Communications Networks and Services under this Licence for the financial year ending immediately before the due date for payment of the fee.*

ISP licence

The ISP licences state that:

The Communications Provider shall pay, or cause to be paid, to the Treasury on [licence date], the [fixed sum]; and

[annually on anniversary of licence date]

on the first £100,000 (one hundred thousand pounds) of Turnover, a fixed sum of £500 (five hundred pounds); and

0.5 per cent of any Turnover in excess of £100,000 (one hundred thousand pounds).

The percentage of Turnover specified in paragraph [above] may be modified by the Commission with the consent of the Treasury, in order to reflect current regulatory costs, at any time after the grant of this Licence.

*For the purposes of this Condition "**Turnover**" means the total revenue generated by the provision of Electronic Communications Networks and Services under this Licence for the financial year ending immediately before the due date for payment of the fee.*

Earth station licence

The earth station licences state that:

The Communications Provider shall pay, or cause to be paid, to the Treasury on [date], the sum of £500 (five hundred pounds); and

on [date], and annually thereafter:

(a) on the first £100,000 (one hundred thousand pounds) of Turnover, a fixed sum of £500 (five hundred pounds); and

(b) 0.5 per cent of any Turnover in excess of £100,000 (one hundred thousand pounds).

The percentage of Turnover specified in paragraph [above] may be modified by the Commission with the consent of the Treasury, in order to reflect current regulatory costs, *at any time after the grant of this Licence.*

*For the purposes of this Condition "**Turnover**" means the total revenue generated by the provision of Electronic Communications Networks and Services under this Licence for the financial year ending immediately before the due date for payment of the fee.*

Annex 2: Revenue reporting template

Annual gross revenue	
Fixed services	
Retail	
Access & calls	
Broadband	
Leased lines	
Data centres/hosting	
CPE sales	
Managed services	
Other	
Wholesale	
Access & calls	
Broadband	
Leased lines	
Interconnection	
Other	
subtotal	

Mobile services	
Retail	
Access & usage (including outbound roaming)	
CPE sales	
SIM cards	
Other	
Wholesale	
Wholesale termination	
In-bound roaming	
Other	
subtotal	
Total revenue	

Deduction of non-licensed activities	
Fixed services	
Retail	
Data centres/hosting	
CPE	
Other	
Wholesale	
Payments for off-island circuits used to provide retail on-island services	
Other	
subtotal	

Mobile services	
CPE	
Other	
subtotal	

Total deductions	

Eligible revenue (total revenue minus deductions)	
Licence fee @0.5%	