CABLE & WIRELESS
JAMAICA

C&WJ's Response to the Office of Utilities Regulation (OUR.'s) Supplementary Consultative Document on Accounting Separation for Cable and Wireless Jamaica

Introduction

Cable & Wireless, Jamaica (C&WJ) welcomes the opportunity to respond to the Office of Utilities Regulation (OUR.'s) Supplementary Consultative Document on Accounting Separation for Cable and Wireless Jamaica dated June 30, 2005.

C&WJ will respond to each question posed by the OUR as well as comment on areas of major concern to C&WJ. These major areas of concern include the appropriate level of public disclosure, implementation of reporting requirements, appropriate documentation and the costs associated with Accounting Separation.

Objectives of Separated Accounts

C&WJ believes the telecommunications landscape has changed dramatically since the O.U.R. issued its first consultative document on Accounting separation in March 2000. The telecommunications market is now more developed and the level of competition much more intense than five (5) years ago. C&WJ's influence over the survival and profitability of new entrants to the market has been significantly reduced by the advent of alternatives to traditional wholesale fixed inputs. C&WJ's importance in this market has therefore been greatly attenuated.

In the early years of liberalization C&WJ was the major supplier of wholesale inputs for new entrants. New entrants have used a combination of new infrastructure solutions coupled with purchased wholesale components to satisfy their customer's needs, thereby reducing their dependence on C&WJ. In 2000 C&WJ supplied the entire wholesale market with international outgoing minutes. With the liberalization of the international market C&WJ lost approximately 90% of that market with the majority of new entrants having their own equipment to convey international traffic- both incoming and outgoing. A similar situation obtains in the market for Internet services where new entrants have used alternative technologies to provide their Internet services.

The OUR has set out four regulatory objectives that separated accounts are intended to support:

1. Ensuring non-discrimination
2. Identifying unfair cross-subsidies
3. Setting or assessing interconnection charges
4. Retail price control

C&WJ has concerns that some requirements proposed in this consultation will:

- Be costly, without commensurate benefits, and
- In many cases the requirement to publish commercially sensitive information will place C&WJ at a competitive disadvantage. C&WJ believes that accounting separation can achieve the objectives set out above without excessive publication requirements.

C&WJ's Current Interconnection Rates

Internationally the broad aim of accounting separation is to achieve market outcomes that promote competition. More specifically, accounting separation is used to promote an effective competitive environment and contribute to a level playing field for all competitors. C&WJ appreciates the relevance of accounting separation in safeguarding against discriminatory behaviour, providing a basis for retail price control as well as identifying unfair cross-subsidies.

The OUR. has on occasion exercised due diligence by examining C&WJ's cost model as it relates to relevant costs for interconnection and has subsequently approved the Reference Interconnect Offers (RIO). In C&WJ's view this process of examination already provides an adequate safeguard mechanism for setting and assessing interconnection charges. C&WJ recognizes the importance of having interconnection rates that fairly reflect the associated costs and the Company has consistently applied the prescribed regulatory and accounting principles to ensure that interconnect rates are cost-based. C&WJ has openly shared with the OUR the costing information and methodologies used in determining interconnect rates.

Only after examining and finding comfort in C&WJ accounting and costing information did the OUR approve these interconnect rates. Having examined this costing information the OUR should be aware that the publication of commercially sensitive information is not necessary in order to satisfy users of the separated accounts that interconnection rates have been calculated fairly. It is the duty of the auditor and regulator to examine the accounts to ensure that the rates properly reflect the relevant cost and to provide this assurance to the market.

Cost of Accounting Separation

The OUR has suggested that the welfare loss resulting from the absence of a system of regulatory accounts will be significant. The regulator must be fully aware of the economic implications of the measures adopted in a policy aimed at non-discriminatory access pricing. An incorrect assessment of the effect of accounting separation will lead to higher consumer prices and lower welfare through the mechanism outlined above. C&WJ is concerned that the OUR has not provided a quantitative justification for this "significant welfare loss" consistent with the absence of a system of regulatory accounts.

Additional costs incurred by C&WJ for the implementation and annual submission of regulated accounts will be borne by wholesale and interconnected customers (). As per the *Telecommunications Act 2000, Part 2 Section 4-(2),* "*In making a decision in the exercise of its functions under this Act the Office shall observe reasonable standards of procedural fairness*". C&WJ notes that the OUR has not demonstrated that the cost to be borne by the telecommunication industry will be surpassed by the anticipated benefit from accounting separation. C&WJ believes that there needs to be this type of quantitative analysis before the implementation of a costly regulatory accounts system which is to be audited. C&WJ, and the telecommunication sector as a whole, needs the OUR to provide a detailed cost-benefit analysis showing the welfare loss that would be involved if a system of regulatory accounts was not developed.

To make C&WJ's position clear, C&WJ agrees that the OUR needs to have sufficient accounting separation information available to ensure that a level playing field exists in the Jamaican (fixed) market. However, directions to produce information on areas of business where competitors are not reliant on wholesale inputs from C&WJ, or directions to publish excessive or confidential information regarding the operation of C&WJ individual services will cause C&WJ and the industry to incur significant cost and place C&WJ at a competitive disadvantage. C&WJ trust that this is not what the OUR is intending to do through this consultation.

Level of Accounting Separation

Question 3.1: Do you agree that for the purposes of regulatory accounts C&WJ should split its activities into four Main Business Activities, namely: Fixed Access, Fixed Network, Fixed Retail Services and Mobile Business. The definitions of each main business are set out in Annex I to this Document.

C&WJ recognizes that within the supplementary consultative document the OUR has requested Accounting Separation (A/S) information at a more aggregated level. While C&WJ is generally in agreement with the degree of disaggregation for the main business areas proposed, the Company believes that any reporting on the Mobile business should not go beyond that which is required of any other mobile operator in the market. C&WJ firmly believes that the publication of sensitive information on the "mobile business" will place C&WJ mobile operations at a competitive disadvantage unless a similar demand is made on all mobile operators. According to the *Telecommunications Act 2000, Part 2 Section 4-(1) (c) and (f),* the OUR shall promote the interests of customers, carriers and service providers and promote competition among carriers and service providers. The OUR cannot justifiably argue that in its attempt to achieve its outlined objectives for accounting separation as well as operate as per the Act, it has grounds to request that C&WJ provide commercially sensitive data for the mobile business that will be placed in the public domain. Placing one operator at a competitive disadvantage in a fiercely competitive market does not promote competition. C&WJ notes that Mobile reporting has often been required during the implementation of A/S in other jurisdictions to which the OUR refers. It must be appreciated however that these markets exhibited very distinct characteristics from Jamaica i.e. the incumbent fixed operator was also dominant in the Mobile market. This is not the case in Jamaica.

Internationally, a primary objective of A/S is to devise an access and usage directive that is specific to business areas where an operator has significant market power (SMP). The OUR.'s recent consultation "*Assessment of Dominance in Mobile Call Termination*" indicated that each mobile operator is dominant on its network for mobile call termination With regards to mobile call origination, it could reasonably be argued that Digicel is dominant given its market share of more than 70% of total mobile active accounts. As previously stated, international best practice has been to limit accounting separation to areas of operation in which the service provider has SMP, an example is Kingston Communications in the United Kingdom who report only on dominant services as opposed to the full suite of services offered.

Given that C&WJ do not have SMP in the mobile market, and in fact have less than 50% of market share, coupled with the fact that the mobile market is competitive, C&WJ believes that unless a similar demand is made of all mobile operators then the provision and publication of separated, and potentially commercially sensitive, information will place C&WJ at a competitive disadvantage. C&WJ acknowledge that a mobile 'basket' will be the reconciling difference between the regulatory and statutory accounting statements and would therefore require inclusion in the AS modelling process. However, C&WJ believes that this information should be outside the scope of any public reporting requirement.

C&WJ is also not clear on the Business definitions outlined by the OUR. Within the Fixed Access Business the OUR has stated that the Business will contain ‘all the revenues (installation, rental, relocation, reconnection, etc) from access, as well as the costs, assets and liabilities associated with supplying connections and maintenance of ordinary business and residential exchange lines, including the low user tariff or any special tariff plan, domestic and international toll free lines, foreign exchange lines, and direct inward dialing lines and other access line technologies such as Integrated Services Digital Network (ISDN)’. C&WJ believes that the revenue for this business should be derived from transfer charges made to the Retail arm of C&WJ and any charges made to other operators for the wholesale provision of access services. Put more simply, customer line connection and rental will be a service provided by the Retail Business. The revenue from line connection and rental provided to end-users will therefore be recorded against Retail. Thus, the cost of providing customer lines will initially be recorded against the Local Access Network Business and there will need to be a transfer of costs to Retail in order to match revenues with their associated costs. In this way the Fixed Access Business (together with the Fixed Network Business) will return the appropriate Weighted Average Cost of Capital (WACC), adjusted for any ‘retail minus’ charging as appropriate.

C&WJ believes that it may also be appropriate to have an additional Exchange Line Rental & Connection retail business to appropriately capture the Retail Access Business. Exchange line rental and connection are products offered to customers as a retail product. The structure proposed by the OUR suggests that both wholesale and retail costs be lumped together into the Fixed Access Business. Within separated accounts the Access business typically represents wholesale and will return the allowed WACC. Blurring the divide of retail and wholesale will also have implications for the model build itself and any effort to reconcile it from an audit and internal compliance perspective.

Question 3.2: Should C&WJ be asked to disaggregate its Retail Services Business into the nine service categories listed at 3.8.0 above? Respondents should justify their response. The definitions of each disaggregated business area are set out in Annex II of this Document.

C&WJ does not object to the request to prepare A/S information at the level proposed in paragraph 3.8 and would be prepared to model and supply the OUR with information at this level of disaggregation. However, C&WJ has some concerns about the relevance of some of these services with regards to providing a greater level of transparency for the telecommunications industry. C&WJ is adamant that aspects of this information should be shared only with the OUR.

Local Calls

The inclusion of service costs for Intra-Parish and Inter-Parish Calls does not add value to the process of A/S. Intra-Parish and Inter-Parish calls are captured by the Price Cap Regime and wholesale local minutes are based on "Retail-minus" as per the *Telecommunications Act 2000.* The objectives of A/S as outlined by the OUR are not met by the inclusion of the service costs for these services. There does not exist the possibility of discriminatory pricing of wholesale local calls as the services are offered at the retail price less the prescribed margin. C&WJ therefore proposes that the OUR removes these services, as inclusion would simply increase the audit costs of the regulatory accounts without any commensurate benefit. The Fixed to Mobile call rate is a composite of the Fixed Retention rate (which is set by the OUR) and the rate set by the mobile operators for the termination of calls on their networks. The Fixed Retention rate is outlined in the Reference Interconnect Offer (RIO) which C&WJ has demonstrated to be cost-based to the OUR. C&WJ sees it appropriate to limit Fixed to Mobile Reporting to simply the fixed retention given that one aspect of the rate for Fixed to Mobile calls is beyond the scope of C&WJ Fixed Line operations.

Public Payphones

The OUR must bear in mind, as discussed, that C&WJ does not earn revenue from Public payphones. The revenue that is generated from the consumer's use of this facility arises from the sale of phone cards. Based on this fact, C&WJ recommends that Public Payphones be removed from the listing in 3.8.0 as a reporting requirement given its lack of relevance.

International Outgoing Calls

Numerous services as defined in Annex II are now competitive based on the evolution of the telecommunication market over the last few years. These include International Outgoing calls, Data Communication Services and Internet Service Provision where competitors to C&WJ have alternative wholesale inputs to those provided by C&WJ. The market for International Outgoing calls is aggressively competitive and the publication of C&WJ's unit cost information will significantly inhibit the Company's ability to compete effectively. Publication of this information without similar publication from other operators would be discriminatory on the part of the Regulator and would not promote healthy competition. The potential for "margin squeeze" in wholesale market for International Outgoing minutes is very limited as this service is also offered on a "Retail-minus" basis.

Data Communication

The imminent competition in the provision of Data communication services must be considered along with the publication of any unit costing information for these services. Internet Service Providers are no longer limited to purchasing wholesale inputs for their service provision from C&WJ. There are now wireless technology options available that many operators are utilizing. The submission of detailed financial and operational information and suggested subsequent publication of said information would place C&WJ at a competitive disadvantage. Competitors would have greater insight into the operations of the company without any reciprocal information being made available to C&WJ.

Supplemental Retail Services

As defined in Annex II, the Supplemental Retail service category may include competitive services such as the sale of international prepaid calling cards. Again, the commercial sensitivity of data on this service must be appreciated. Based on foregoing arguments, C&WJ will provide only the costs for each service level but is unwilling to provide commercially sensitive volume data. It would be exorbitantly expensive to produce profitability reports for different services as well as to audit these reports.

Regulatory Financial Statements

Question 4.1: As stated in Annex III, should these constitute the main businesses and where applicable service categories for which C&WJ should be required to prepare statements of profit & loss and mean capital employed? Justify your response.

As stated above in this response C&WJ is willing to produce AS information at the level proposed in Annex III of the document with the exception of detailed reporting on its Mobile business and reporting on individual services. C&WJ would be averse to producing Profit & Loss and Balance Sheet Statements for the individual service levels that are outlined as part of the Fixed Retail Services Business. Justification for this position has been provided in response to Question 3.1t. Service cost information will be provided for some of the service levels in 3.8.0 as per response to Question 3.2. C&WJ proposes that information be published at the business level and service specific reporting be provided to the OUR (See response to Question 6.1 for proposed level of detail for publication). As outlined below C&WJ believes that a more consolidated set of specific services is appropriate in the initial years of AS. For the mobile business the level of disaggregation should be at the level of the Company's annual statutory accounts and reconciliation submitted to the Office under confidential cover..

Question 4.2: Should Return (profit/loss) be calculated on the same basis as the cost of capital? Justify your response.

C&W agrees in principle that if a pre-tax cost of capital is used, the return on capital employed should also be assessed on a pre-tax basis.

Furthermore, as the intention of calculating and using a pre-tax cost of capital is presumably to determine a reasonable rate of return that should be permitted in order to reward equity holders from post-tax profits via dividends, it is important that the cost of capital is appropriately adjusted in a timely manner for any changes in the tax burden borne by the regulated entity[1]. To a large extent, the tax burden will consist of the corporation tax rate, although it may also be appropriate to consider the impact of other forms of effective profit taxation such as licensing and compliance costs.

The situation is slightly different when one considers the position of debt holders and the costs of servicing debt. Debt holders receive their returns in the form of interest paid from the pre-tax profits. Consequently, the returns should be assessed <u>after</u> interest paid (or payable) is deducted and the relevant cost of capital should be appropriately adjusted

[1] C&W Jamaica has prudently adopted International Financial Reporting Standards and appropriately provides for deferred taxation. Consequently, the appropriate tax rate by which to uplift the requisite return of equity holders should be the actual, relevant corporation tax rate, as opposed to any 'effective' corporation tax rate suffered in any particular year.

to reflect the weighted proportion of 'cheaper' debt finance in the regulated entities capital structure.

Finally, when determining an appropriate rate of return for regulated services and the cost of capital to be used, it is worth considering the currency in which debt and equity holders are remunerated. Cable & Wireless Jamaica's equity holders are remunerated in Sterling, while many of the business's creditors (i.e. short-term debt holders) hold debts denominated in US$. Consequently, when considering the appropriateness of the cost of capital, C&W Jamaica believes that allowance should be made for any discernible trend in J$ currency devaluation i.e. the cost of capital should be uplifted so as to ensure that sufficient J$ profits exist from which to remunerate debt and equity holders in their respective currencies of payment.

Question 4.3: Should the Statements of mean capital employed be in the format set out in Annex V? If not, propose an alternative.

The format displayed requires a level of detail that requires greater time for compilation of data without significant movement towards achievement of AS objectives. The statement of mean capital employed should simply represent totals for Fixed Assets, Current Assets, Liabilities and the Mean capital employed. C&WJ believes there is no value added by a breakdown of the said data.

Question 4.4: Should the figures reported in the statement be the average values for the period to which the statement relates?

CWJ agrees that in subsequent years that the figures reported in the mean capital employed statement should be the average values for the period. For the initial period of A/S C&WJ proposes to use closing values only since opening values for the period are unlikely to be available. This is because, unless the valuation methodology can be agreed prior to March 2006, the Current Cost Accounting (CCA) valuation process required for separated accounting purposes may not have been carried out for the opening period and it would be both difficult and disproportionate to carry out these onerous valuations retrospectively. This approach is typical in the implementation year of an A/S model under CCA. For subsequent periods C&WJ proposes the use of a simple average. C&WJ does not believe the use of weighted average values is operationally feasible or proportional, as this would require C&WJ to perform fixed asset register analysis each month. The differential between weighted average and a simple average is not expected to be material hence the benefits of the use of weighted average values would be limited.

Question 4.5: Do you share the Office's view that C&WJ's Statements of Profit and Loss, and Mean Capital Employed should be reconciled with the annual statutory financial accounts (i.e. Profit & Loss, Capital Employed) of the Company? If not, why not?

It is appropriate that the regulatory accounts be reconciled with the statutory accounts. C&WJ agree that both P&L and MCE reconciliation's will be a necessary requirement in any audit. C&WJ proposes that the reconciliation be provided to the OUR. However, the Company does not believe that the reconciliation should be published. This is because, as set out above, the Mobile arm and certain Retail services of C&WJ's operation should not be subject to separated accounting and consequent reporting of commercially sensitive data. Clearly in any reconciliation to the statutory financial records of the Company the Mobile business would be a necessary balancing element. If the above were followed, that is where reconciliation's are provided to the auditors and OUR only, it would still allow the auditors and the OUR to have full visibility of the A/S process. It would also provide other operators the assurance that the regulatory information has been reconciled to statutory records, while the information pertaining to C&WJ's Mobile business and competitive Retail services would remain out of the public domain.

Reconciliation will necessarily include CCA adjustments to fixed assets. In turn, this will also result in reconciling items to the P&L reconciliation in order to address unrealized CCA holding gains and losses. Reconciliation is a useful check but there is little value in their publication, particularly given the complexity of the reconciliation. The OUR has not indicated how C&WJ should display reconciling adjustments but C&WJ presumes that these are only required if independently material.

Question 4.6: As part of C&WJ Accounting Information, do you think that a statement of cost for its fixed and mobile network services should be produced as per the discussion above? Explain your response.

Fixed Network Statement of Cost:

C&WJ is prepared to provide the OUR with this statement, however, the Company objects to any proposal to make much of this information publicly available. The OUR argues in the consultation that the Act requires that charges for interconnection services be transparent. C&WJ's review of the Act reveals that it requires that the terms and conditions of interconnection charges be transparent. Section 33 (1) of the Act outlines the principles which should guide the OUR in reviewing the charges established by a dominant carrier.

The Act places the responsibility of ensuring that interconnection charges are properly determined on the OUR and C&WJ maintains that the terms and conditions of interconnection charges will be transparent without the requirement to release C&WJ's commercially sensitive information into the public domain. C&WJ believes that aspects of information suggested by the OUR be included in the Fixed Statement of Costs are confidential and should be shared only with the OUR. For example, C&WJ believes that it should not disclose International Outpayments. The agreements with international partners are confidential and are acutely commercially sensitive, the confidentiality of this information is confirmed by the terms and conditions of the contracts. Any disclosure of this information by C&WJ would be a breach of contract.

Mobile Network Statement of Cost:

C&WJ strongly believes that this statement should not be a requirement of Accounting Separation. Given the competitive nature of the mobile market, and given that C&WJ is not the dominant mobile player in Jamaica, the Company is surprised that the OUR would request the production of a Statement of Network Costs for its Mobile business without a similar requirement being made of other mobile operators. C&WJ maintains that while Mobile operations will form a 'basket' of revenue and cost, it will not be further disaggregated. C&WJ does not accept that any level of disclosure greater than that applicable to other mobile operators in the market is appropriate. In this regard C&WJ would be constrained to avail itself of the due process provided under section 7 of the Telecommunications Act which speaks to the treatment of confidential information.

Question 4.7: Should C&WJ be required to publish a statement of cost for a list of retail services and containing such particulars as set out in Annex IX?

CWJ strongly disagree with the proposal to produce and publish all elements of this statement. As far as C&WJ is aware there is no precedent for incumbents to publish a statement that details respective volumes of Retail products. C&WJ is willing to produce and publish unit costs for Fixed Retention, International Incoming Calls and Remaining Services, as discussed in response to Question 3.2. This will reflect much of the information outlined in Annex XI. However C&WJ is unwilling to publish commercially sensitive volume data.

Accounting Framework Documents

Question 5.1: Do you agree that the key components of the Accounting Documents should be Regulatory Principles, Attribution Methods, Transfer Charging, and Accounting Policies? If not, why not?

C&WJ agrees that four of the key components of the Accounting Documents should be the Regulatory Principles, Attribution Methods, Transfer Charging and Accounting Policies. The OUR however has not commented on the method used for valuing assets although C&WJ notes that a valuation methodology is mentioned in the 'Notice of Proposed Rule Making' (NPRM).

On July 31, 2003, the OUR issued its determination titled "*Principles and Methods of Asset Valuation for Regulatory Purposes*". In this Determination, the OUR approved the use of the industry standard approach of Current Cost Accounting (CCA) using Modern Equivalent Asset (MEA) and absolute valuations as necessary for asset valuations. The OUR has directed that that these values be rolled forward, for regulatory purposes, until further specific studies are done. Coming out of that Determination, MEA values were used to derive the current interconnection rates and in the setting of the price cap regime. C&WJ would therefore expect that the A/S information would be produced on a current cost basis.

C&WJ proposes that, in addition to the components specified in paragraph 5.1 documentation on the Detailed Asset Valuation Methodology (DVM) should be produced by The OUR. The DVM provides an outline of the methodologies adopted for deriving gross replacement costs for each of the asset classes that comprise the fixed asset register as well as the basis of valuation of various assets classes within the fixed assets register of C&WJ. The OUR needs to specify an indexation method and possibly, the accounting entries to reflect changes in the CCA valuation year on year.

The OUR has outlined the key components of the Accounting Documents and also indicated their order of priority in the event of conflict between all or some of these documents. The order of priority as suggested by the OUR indicates a possible departure from typical accounting policies as regulatory edict would supersede established accounting policies. This departure will need to be documented. . For example, C&WJ has adopted accounting for deferred taxation in accordance with international accounting standards but the OUR has been silent on this issue.

Question 5.2: Is three months from the publication date of the final determination notice a reasonable time period to assemble the Accounting Documents and submit them to the Office for consultation and review?

C&WJ believes that the OUR may have misinterpreted the timing of the production of Accounting Documents and their purpose in a typical Accounting Separation process. C&WJ would expect that as an output of this consultation the OUR will publish comprehensive Regulatory Accounting Guidelines (RAG). It is these guidelines that should include, by way of example, detailed information on the regulatory accounting principles, principles of cost causality, cost allocation principles, the level of separation of the accounts, transfer charges, definitions of main businesses and the high-level valuation approach to be taken. Until these comprehensive guidelines are established C&WJ will not be in a position to begin building a separated accounting model that complies with the OUR.'s requirements.

The Accounting Documents produced by C&WJ will be a 'living' document that will be developed as the accounting separation model is built. For example, it could not be possible for C&WJ to provide detail on the model structure in the Accounting Documents until the model is constructed and finalized. C&WJ notes that the OUR has gone some ways to provide a broad overview of this type of information within Chapter 3 of the NPRM. However, typically, Accounting Guidelines are more detailed as can be seen from the '*Regulatory Accounting Guidelines for Cable & Wireless Guernsey*', published by the Office of Utility Regulation in Guernsey and which can be found at http://www.regutil.gg/docs/OUROUR.0425.pdf.

It is C&WJ's expectation therefore that the Accounting Documents are submitted together with the Accounting Separation statements themselves. It is also C&WJ's understanding that typically the Accounting Documents will be audited in the same manner as the model and statements themselves to ensure that they have been correctly interpreted and have complied with the requirements of the OUR as set out in the RAG.

C&WJ believes that this process has precedence in all jurisdictions that carry out Accounting Separation. C&WJ would be prepared to submit a framework Accounting Document to the OUR prior to submission but this could only be on the understanding that this would be a 'framework' and would be amended as necessary as the accounting separation process and model develops. C&WJ would also suggest that once the Regulatory Accounting Guidelines are finalized that a collaborative approach be adopted between the OUR and C&WJ to facilitate the creation of the A/S model and the initial separated accounts. For example, this could be by way of monthly meetings between the two parties where C&WJ can explain progress on the model build and driver collection process and seek assurances from the OUR that the RAG has been interpreted correctly.

Publication of Financial Information

Question 6.1: Should the Accounting statements along with related information and notes be published?

C&WJ does not support the OUR.'s proposal to publish 'commercially sensitive' or 'competitive service' information.

C&WJ believes that to produce (and publish) statements at a very detailed level, as suggested in paragraph 3.8, in the initial years of separated accounting may not be in the best interest of any party. It must be appreciated that the development of a robust activity based costing model for A/S is an extremely complex and resource intensive process. In other jurisdictions it has taken a number of years, and several submissions, to hone a model and related cost drivers to a satisfactory level. In particular the financial reporting information required for A/S modelling is fundamentally different from what is currently available to C&WJ from its accounting system. Therefore a system 'redesign' will be necessary before such information can be sourced and applied for A/S modelling purposes. These variables mean that any attempt to report at a very detailed retail business level, as suggested, in the initial year(s) of accounting separation could result in a less accurate and reliable output.

For this reason C&WJ proposes that, while it is prepared to provide a split of Retail activities as outlined in 3.8 to the OUR., that for publication the sub-categories be consolidated. This will enable greater reliability to be placed on the statements while the model is 'bedded in'. This approach has been adopted during the development stages of costing models by regulators in other jurisdictions, such as Guernsey, and in no way reflects any failure by the incumbent or a softening on the part of the regulator but is simply a pragmatic approach that acknowledges the difficulty and complexity of developing a robust model to produce disaggregated separated accounts.

C&WJ's would welcome further discussions with the OUR. as to the most appropriate consolidation. Analysis of necessary cost drivers and best practice in other jurisdictions suggests that the following may be appropriate:

3.2.1 Consolidation of Fixed Retail Services Business

Proposed by OUR.	Consolidation proposed by C&WJ
	Exchange line rental & connection
Intra-Parish Calls Inter-Parish Calls Fixed to Mobile Calls	Inter-Parish and Intra-Parish to be removed Fixed to Mobile to be changed to Fixed Retention Rate

Public Payphones	Remove from reporting requirement No longer relevant
International Outgoing Calls[2] International Incoming Calls	International calls
Directory Enquiries (DQ) Data Communication Services Internet service provision Supplemental Retail Remaining Services	Remaining Services

Question 6.2: Do you agree that the Publication of C&WJ's regulatory accounts should not exceed six (6) months from the end of the financial year to which they relate.

It is accepted that industry 'best practice' is to publish regulatory accounts within six (6) months of the end of the financial year to which they relate. C&WJ would point out however that in almost all cases in other jurisdictions, for example Guernsey and Bahrain, operators have required an extended time frame to submit initial sets of accounts. The complexity and resource requirements of activity based costing and separated accounting should not be underestimated. By way of example, and setting aside from the onerous model build itself; a system to measure and allocate engineering staff activity information (a key cost driver) takes significant time and resource to establish. Clearly once this system is embedded, fine-tuned and staff become more familiar with the requirements of accounting separation, the collection of the data will become less burdensome year on year. Given there are potentially hundreds of cost drivers requiring data collection such as this, the hurdle of establishing these processes and methodologies in the first years of accounting separation becomes more obvious. C&WJ would ask that the OUR bear this in mind when imposing initial deadlines and suggest that a more appropriate timeframe for submission and publication in the initial year of production of regulatory accounts would be nine (9) months, moving towards six (6) months in subsequent periods.

[2] International Outgoing Calls should be removed, as there now exists effective competition for this service. Publication of costing information for this service would place C&WJ at a competitive disadvantage, as other operators would be able to adjust their strategies given this information without C&WJ being privy to any reciprocal information from these operators.

Cost, complexity and timing of Separated Accounting

For the avoidance of doubt, and although not directly addressed by the OUR in any of the questions in this consultation, C&WJ wish to make clear the difficulties the Company faces in terms of expected cost, complexity and timing issues surrounding A/S.

Cost

C&WJ acknowledges the OUR.'s views that the Company will need to have similar costing information for its normal business operations. However the production of A/S information to support C&WJ's business operations will not be of the form proposed by the OUR. A significant proportion of the cost involved in the proposed systems is the required external audit. Providing an audit opinion at the level of individual services will be extremely expensive and C&WJ is unwilling to directly bear this cost, particularly given the overall dynamics of the Jamaican telecommunication market. C&WJ has justified this position with alternative solutions to proportionally allocate the burden of this cost in its response to the NPRM. To reiterate the key points:

C&WJ strongly believes that the industry as whole should directly bear the cost of the regulatory audit. It must be noted that in terms of total share of the telecommunications (mobile and fixed) market that C&WJ has approximately 0.8 million subscribers against the 1.4 million held by Digicel[3]. Viewed in this context C&WJ is not the major player in Jamaica and it is interesting to note that Digicel, although misinterpreting the proposed requirements of Mobile Network operators (MNOs) as regards this and the NPRM states its belief that the resource requirements (and cost) of accounting separation and the audit process places a disproportionate burden on operators. In addition Jamaica has, as occurred globally in developing telecommunications markets, seen high levels of mobile versus fixed penetration. C&WJ estimates that fixed line teledensity in Jamaica is approximately 15% while mobile penetration has reached 70%. Importantly, of this mobile market C&WJ has less than 50%.

The issues above are very important when considering a fair and proportionate mechanism to allocate the cost of the regulatory audit between operators. The OUR has drawn reference from other developed fixed markets where accounting separation and regulatory audits have been required. In these jurisdictions the incumbent has initially met the regulatory audit cost but is able to pass this on to other operators by driving the cost through the costing model onto regulated components and products that are constituent parts of the Reference Offer. Because fixed penetration in these markets is very high the costs are shared amongst the fixed and mobile industry players in a proportional manner (as all operators use fixed network components on the dominant operators network). Jamaica is clearly very different and C&WJ will not be able to pass the cost through to other operators in this way because of fixed line displacement by mobile .

[3] Market analysis done by C&WJ.

It should also be noted that in the other jurisdictions to which the OUR refers, the incumbents have had clear dominance in the telecommunications market as a whole, both in terms of market share and total revenue. Arguably it is more proportional in such instances to expect the incumbent to bear the regulatory audit cost. C&WJ agrees with Digicel '*that it is disproportionate to burden one operator*', C&WJ, with such costs. To be clear, accounting separation is a requirement of the OUR and benefits other operators in the wider market. C&WJ already has in place costing systems for its internal operating purposes therefore any additional costs, particularly as regards an external audit, will bring no additional benefit to the Company.

On this basis C&WJ strongly believes, while it is prepared to meet the significant costs associated with the necessary systems and resource requirements of preparing separated accounts, that the audit costs should be met directly by all players in the industry. There are a number of possible ways that this could be achieved, one of which is prorating the cost by eligible revenue. Examples of this type of cost allocation between competing operators can be seen in many USO funding mechanisms. Recovery of the audit cost is also possible via an additional charge on the bills of interconnecting parties as well as wholesale customers. This item would be clearly identified as the "Regulatory Audit Cost" and would be applied to all interconnecting parties and wholesale customers on an equitable basis. The charge would be applied on a monthly basis. C&WJ would welcome the opportunity to discuss this issue further.

The Company is also likely to incur significant additional costs resulting from the outcome of this consultation. As an example of cost levels that other operators have incurred when implementing A/S, the incumbent in Guernsey attributed direct costs of over £1M (J$100M) in its first year to A/S because of the excessive and disproportionate requirements placed on the company by the regulator. This cost must be viewed in the context of an island of 60,000 inhabitants and a network comprising only five switches. C&WJ continues to strive to become a more efficient operator and is anxious to avoid this type of excessive regulatory cost. The Company therefore is very keen to have the OUR carefully consider all of the requirements made within this consultation. Reporting detail equals cost in an A/S environment.

Complexity and timing of A/S

C&WJ looks forward to working with the OUR to design and implement a pragmatic and proportional A/S solution. Notably C&WJ has already proactively begun implementing a new accounting separation system that has the capability to produce separated accounts. C&WJ 's existing costing system is not capable of producing regulated accounts as specified by the OUR.

As outlined below it is essential in any A/S process to have year-on-year continuity in terms of systems use and development. The projected timeline to complete the roll out of the new accounting separation system is April 2006.

There are very many technical issues, processes and resource requirements that must be addressed during the ABC model build and A/S process. To put this into context C&WJ believes it is beneficial to outline some of the necessary work-streams, such as:

- The disaggregation, re-classification and the re-valuation to current cost (CCA) of individual assets that make up approximately thirty (30) fixed asset categories. This process also requires a model to be built that calculates CCA depreciation, holding gains and losses and supplementary depreciation so that CCA inputs may be fed into the Activity Based Costing (ABC) model.
- The definition and subsequent collection of cost driver information for (typically) in excess of one hundred and fifty (150) drivers. By way of example this will include detailed analysis of network component use, staff activity and non-network assets to name just three areas. Defining appropriate driver methodologies and the driver collection process normally requires several fulltime staff dedicated solely to this task. It should be noted that often the A/S driver data sought is reliant on an output spanning the financial year in question. This data is difficult or impossible to source retrospectively, for example analysis of staff activity, as this will clearly change materially from year to year as the business focus changes. Deriving and documenting the driver methodologies is also a particularly onerous task.
- The new accounting separation system model design and build. This is highly specialized skill that can be expected to require the fulltime attention of an A/S expert during the first year of the A/S process. The complexities of the model build itself are too numerous to document here however C&WJ would be happy to discuss these issues further with the OUR. Again C&WJ reiterate a willingness to use a collaborative approach during this model design and build.
- Statement production: A system must be implemented to interrogate the ABC model so that the appropriate information can be extracted to construct accurate and reliable financial statements. This is a highly specialized skill that is a time and resource intensive process.
- The statutory financial information must be analyzed and disaggregated so that the regulatory information is coherent and consistent with the ABC model structure. This is a complex analysis that requires significant resource in the initial years(s) of accounting separation prior to establishing a workable and accepted process and methodology.

This is a ‘high level’ summary of **some** issues that will need to be addressed. It is important to note that much of this work can be started only after the OUR has published detailed Regulatory Accounting Guidelines. Specific to C&WJ it should also be appreciated that the format of information required for A/S reporting, by the OUR, is fundamentally different to that currently being implemented by the Company in the new accounting separation system. Therefore a redesign of the new system, once implemented, will be necessary before this information will be in a form that supports A/S. Also, any meaningful regulatory reporting will require financial, cost driver, operational and statistical data for a complete financial year.

For these reasons it would not be possible for C&WJ to comply with A/S requirements, as specified in the OUR's Supplemental Consultation, before the financial year ending March 2006/07. C&WJ would again emphasize that the methodology, model and systems must be in place at the beginning of the reporting year for which A/S is required. This timeframe for system and process implementation is typical of the experience in other jurisdictions. C&WJ would be happy to justify this position more fully by way of a draft project plan and reference to model-build timelines in other jurisdictions should the OUR require further explanation to the above.

Conclusion

C&WJ is cognizant of the OUR's goal of a level playing field for all competitors in the telecommunications market. It is also understood that as the incumbent fixed line service provider, C&WJ is in a unique position in the market and certain regulatory safeguards associated with some areas of C&WJ's operations will be proposed and/or implemented. While C&WJ can appreciate the need for transparency in all markets in which the Company operates, the OUR needs to appreciate the fact that as a commercial entity operating in competitive and non-competitive markets, C&WJ will make all attempts to comply with the regulator, but will not place its operations in any commercially compromising position. C&WJ stands ready to be party to any collaborative effort with the OUR that will expand and improve the service quality of telecommunications services being offered to the Jamaican consumer.

Cable & Wireless Jamaica
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