

31 August 2005

Mr. J P Morgan  
Director General  
Office of Utilities Regulation  
36 Trafalgar Road  
Kingston 10

Dear Mr. Morgan:

**Re: Digicel's Responses to Consultation on Accounting Separation for Cable and Wireless Jamaica: Supplementary Consultative Document (Document No: TEL 2005/02)**

Please find enclosed Digicel's responses to Consultation on Accounting Separation for Cable and Wireless Jamaica. Digicel welcomes the opportunity to comment on this important initiative in the telecommunications industry. Requiring Cable and Wireless Jamaica to provide separate accounts for its fixed and mobile businesses will further level the playing field for other service providers and bring substantial benefits to consumers.

Digicel agrees with the general thrust of what is being proposed by the Authority although it is difficult to fully appreciate the specifics envisaged in the end product at this stage. Digicel believe that the OUR needs in particular to ensure that the end product clearly and unambiguously identifies the interrelationship between Cable and Wireless' fixed and mobile networks. Enforcing appropriate cost transparency and allocation on the dual fixed and mobile operator, in accordance with international regulatory accounting practices, is the only way in which the scope for anti-competitive practices by Cable and Wireless can be curtailed.

Digicel is however grateful to be able to provide an input on this vital issue and hope the see the process implemented shortly.

Yours sincerely  
MOSEL (JAMAICA) LIMITED

Per: \_\_\_\_\_  
DAVID HALL

Chief Executive Officer, Digicel Jamaica

## **Accounting Separation for Cable and Wireless Jamaica**

Digicel welcomes the opportunity to respond to the consultation document on the Accounting Separation for Cable and Wireless Jamaica. Digicel believes that account separation is important because it helps to guard against incumbent operators engaging in anti-competitive behaviour such as predatory pricing and/or cross subsidisation which can often be disguised through cost misallocation. Consumers can also be protected from abuse of dominance through excessive pricing. The OUR is mandated under the Telecommunications Act 2000 to implement competitive safeguard rules which prescribe inter alia the separation of accounts of the dominant public voice carrier. Digicel believe this can be achieved without overburdening Cable and Wireless. In addition, the welfare loss that is negated by the use of accounting separation will more than compensate for any increase in cost associated with providing separated accounts.

Digicel has seen clear evidence of misallocation of costs by Cable and Wireless in other jurisdictions. This has reaffirmed its view that accounting separation should be introduced as soon as possible in Jamaica. Digicel contends that there is strong anecdotal evidence in Jamaica that suggests that C&W has engaged in misallocating costs for the purposes of gaining a competitive advantage in the market. As stated in previous documentation submitted by Digicel to the OUR, C&W J's accounts as published in a national newspaper for the quarter ended December 31, 2004, suggested the fixed line operations are highly profitable while its mobile division is apparently losing money. This raises concerns whether anti-competitive cross subsidization is taking place e.g. Digicel believes that there may be cross subsidisation between CWJ mobile and fixed networks through interconnect rates that are not cost based (too high for fixed interconnect, too low for mobile interconnect).

In addition, Digicel believes that the wider mobile market in Jamaica is highly competitive while little progress has been achieved in bringing competition to fixed line services. In this regard mandated separated accounts based on solid regulatory accounting principles will provide the OUR with a first point of reference in assessing where some of these problems might exist e.g. C&WJ may be extracting monopoly rents from its fixed line customer base which in turn is having an adverse affect on demand for fixed line services.

**Question 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.**

Digicel is not quite sure if the Fixed Access and Fixed Network categories referred to are wholesale. If both categories are wholesale, then Digicel would agree that the fixed network should be segmented into the three categories listed. However, Mobile Business should also be divided into wholesale and retail since C&WJ is offering wholesale and retail services on both the fixed line and mobile networks. This will help the Office in ensuring that C&WJ is not allowed to use its relative strength in both markets for any anti-competitive behaviour.

**Question 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.**

Digicel is in firm support of the various service categories that are being proposed for the separation of C&WJ retail services, though we suggest that Supplemental Retail be further aggregated by itemising emergency services and free phone services. Digicel are pleased to note that the OUR has included in its list the Directory enquiry service. As the OUR is aware Digicel has requested a wholesale DQ service from C&WJ in recent months but have only been offered the service at terms that are considerably above are

unacceptable and at rates that are considerably above international benchmarks for same. Digicel anticipate that the OUR will be able to assess what an appropriate cost for a wholesale DQ service is subsequent to this process.

**Question 3: 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.**

The main businesses and service categories as outlined in annex III of the document should constitute the areas that C&WJ is required to prepare statements of profit and loss and mean capital employed. These are the primary areas in which C&WJ can exploit its position of being both fixed line and mobile operator. Therefore transparency is necessary in ensuring that competition can be maintained through a level playing field for other operators, including prospective investors in the fixed or mobile sectors that will ultimately bring benefits to consumers.

**Question 4: Should Return (profit/loss) be calculated on the same basis as the cost of capital? Justify your response.**

In general, Digicel would answer yes to the question as it is posed, however, Digicel are somewhat confused by the following statement in the preamble to the question:

“For example if weighted average cost of capital is on a pre-tax and pre-interest basis...”.

Digicel believes interest payments (or the cost of debt) is fundamental to calculating the weighted average cost of capital. Therefore, while WACC can be calculated on a pre-tax or post-tax basis it is not clear how it is calculated pre-interest. Digicel believes that it would be helpful if the OUR provided more detailed on this to clarify what is being proposed although we would note that the format proposed in Annex IV of the consultation appears the correct approach..

**Question 5.1: Should the Statements of mean capital employed be in the format set out in Annex V? If not, propose an alternative.**

Digicel disagrees with the format for the Statements of mean capital employed and wishes to refer the OUR to the proposed statement in Annex C of the consultative document on Regulatory Accounts for a Dominant Carrier or Service Provider 2000 (a copy is provided below). Any attempt to aggregate the items will prevent proper analysis of the funding structure of each of C&WJ's business, thereby weakening the effect of the accounting separation. Hence it is essential that C&WJ is asked to provide detail statements which will allow the Office to use regulatory accounting as an effective tool to police cross-subsidization activities.

**ANNEX C: Statement of Capital Employed**

Business or Service Category Notes Previous Year Current Year

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Fixed assets  
Investments  
Deferred expenditure

-----  
Total Fixed Assets

-----  
Current assets  
Cash & short-term deposits  
Accounts receivable  
Due from related companies  
Inventories  
Current portion of deferred expenditure

-----  
Total current assets

-----  
Total Assets

-----  
Current liabilities  
Bank overdraft  
Accounts payable  
Current portion of loans  
Current portion of obligations under finance lease  
Taxation  
Due to ultimate parent company  
Due to related companies  
Dividends payable  
Dividends proposed

-----  
Total current liabilities

-----  
Net current assets (liabilities)

-----  
Long-term liabilities  
Loans  
Obligations under finance leases  
Deferred taxation

-----  
Total Long-term Liabilities  
-----

Shareholders' equity  
Share capital  
Capital reserve  
Retained earnings  
-----

Total shareholders equity  
-----

Capital employed  
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Source: OUR consultative document on Regulatory Accounts for a Dominant Carrier or Service Provider 2000

**Question 5.2: Should the figures reported in the statement be the average values for the period to which the statement relates?**

It is also important that every effort is made by the OUR in having the incumbent produce a weighted average mean capital employed statement. The simple average will not give a true reflection of the capital employed over the reporting period.

**Question 6: 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?**

Yes. Digicel agrees with the OUR that C&WJ's Statements of Profit and Loss and Mean Capital Employed must be reconciled with the audited annual financial accounts of the Company.

**Question 7: 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.**

Digicel believes that the statements of cost for C&WJ fixed and mobile should carry the level of details proposed in paragraph 4.6 of the consultative document. This is so, as C&WJ still has monopoly power on fixed line services, while being a key mobile service provider. Therefore, despite the competitiveness of the mobile industry it is of great

importance that such level of details be provided. It is also important that sufficient explanatory information accompany the statements.

**Question 8: 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?**

Digicel believes that transfers between C&WJ Main Business areas is where the threat of cross-subsidisation is greatest and must therefore be the focal point of regulatory actions if accounting separation is to have real effect in safeguarding against unfair cross-subsidies and anti-competitive behaviour. As such, Digicel strongly supports the OUR proposals to require CW&J to publish a statement of cost for the retail services as listed in the respective annex. Provision of this data should not pose an undue burden on C&W as one would expect it to ensure such internal transfer or accurately recorded already in order that it can satisfy itself that it does not behave in an anti-competitive manner.

**Question 9: 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?**

Digicel agrees that Regulatory Principles should be applied as the priority in preparation of the financial statements. This will clearly have implications for attribution methods and transfer charging principles that C&WJ may apply to its own accounting internally. Therefore where internal attribution/transfer principles conflict with how such principles as outlined in this document then the latter should take priority. Digicel would urge the OUR to be wary that where regulatory principles appear to remain silent on certain matters that C&W don't simply apply attribution methods or transfer charging principles that essentially are exploited to amount to 'balancing the equation' in the accounts. If the OUR in review identifies this as a potential problem then Digicel believes that

standard accounting policies should apply in the main where regulatory principles are silent on certain issues.

**Question 10: 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?**

Digicel concurs with the OUR that C&WJ should submit to the Office the requested documents within three months of the final determination notice unless C&W can satisfy the OUR of substantive and credible reasons as to why this might not be possible.

**Question 11: Should the Accounting statements along with related information and notes be published?**

The point must be reiterated that for the purpose of transparency and to avoid the creation of ambiguity C&WJ accounting statements must be published. This will enable other operators to be confident about the fairness of interconnection and other charges, thus promoting fair competition as well as encouraging investments.

**Question 12: 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.**

Digicel agrees with the six month time period as a maximum allotted time to CWJ for the publication of the regulatory accounts. Where necessary however there should be the flexibility to require that accounts be published earlier.

## **Conclusion**

Digicel is grateful for the opportunity to provide comment on the Accounts Separation of C&W Jamaica fixed and mobile operations. It is also important that the incumbent who



participates in the upstream and downstream of both the fixed and mobile markets is not allowed to misallocate costs so as to gain a competitive advantage through anti-competitive strategies. Despite not entirely agreeing with the reported format, Digicel nevertheless welcomes the proposed required documents of profit and loss accounts, statements of capital employed, statement of service unit costs and a statement of reconciliation. We regard the reconciliation statement as being particularly important in order to ensure that regulatory and audited financial accounts are seen to be fully consistent and can then draw strength from one another.

However, Digicel believes that C&WJ should be asked to provide more details of the network elements required for fixed origination, termination and transit, and the extent to which these are used exclusively for the services in question, and the associated cost allocations. This will enable the Office to clearly understand the interrelationship between C&WJ fixed and mobile networks.

It is also important that the OUR remains vigilant and not allow C&WJ to use delay tactics to delay such an important process.