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21 June 2017

Office of Utilities Regulation
3rd floor P.C. J. Resource Centre
36 Trafalgar Road
Kingston 10

by email & hand

Attention: Ambassador Peter Black CD, JP- Secretary to the Office

Dear Sirs:

Re: Cost Model for Fixed Termination Rates – The Decision on Rates: Application for Reconsideration

Application for Reconsideration

1. Pursuant to Section 60(4) of the Telecommunications Act ('the Act'), Cable & Wireless Jamaica Limited (dba Flow) hereby applies for a reconsideration of the Cost Model for Fixed Termination Rates – The Decision on Rates dated 7 June 2017 ('the Determination on Rates') issued by the Office of Utilities Regulation ('OUR'). Specifically, Flow seeks a reconsideration of the OUR's decision on the timeline or glide path for implementation of the Determination on Rates which is set out in paragraph 15.6:

> *15.6 The first of the glide-path for fixed termination rates becomes effective on 2017 July 1 and remains in effect until 2017 December 31. The second step will become effective on 2018 January 1.*

2. The result is that the OUR has ordered a six month implementation glide path for the reduction in the Fixed Termination Rates, with forty four percent (44%) of the reductions effective immediately on 1 July 2017 and one hundred per cent (100%) of the reductions effective in six months' time on 1 January 2018.

3. Flow submits that, a six month glide path, with a twenty three day notice of the first reduction, is (i) a wrongful exercise of the discretion of the OUR and (ii) a frustration of a legitimate expectation by Flow of a longer glide path, which together provides grounds on which it can argue that the OUR's decision is an error of law pursuant to Section 60(5) (b) of the Act.

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Legislative Framework for the Determination on Rates

4. The OUR has relied on Section 29(4)(a), Section 29(5) and Section 33(1) of the Act as the legislative basis to determine the rates charged for interconnection. These sections are copied below:

29 Obligation to Grant Interconnection
(4) The Office may-
(a) on its own initiative, in assessing an interconnection agreement, make a determination of the terms and conditions, including charges;
(5) When making a determination of an operator's interconnection charges, the Office shall have regard to-

(a) the principles of cost orientation or reciprocity;

(b) local or international benchmarks;

(c) any other approach that is relevant to the determination of interconnection charges.

33. Principles to guide determination of prices.
33. (1) Where the Office is required to determine the charges for the provision of interconnection by a dominant carrier, it shall, in making that determination, be guided by the following principles -

(a) costs shall be borne by the carrier whose activities cause those costs to be incurred:

(b) non-recurring costs shall be recovered through non-recurring charges and recurring costs shall be recovered through recurring charges;

(c) costs that do not vary with usage shall be recovered through flat charges and costs that vary with usage shall be recovered through charges that are based on usage;

(d) costs shall include attributable operating expenditure and depreciation and an amount estimated to achieve a reasonable rate of return;

(e) with the exception of interconnection charges for wholesale termination services, interconnection charges shall be established between the total long run incremental cost of providing the service and the stand alone cost of providing the service, so, however, that the

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prices shall be so calculated as to avoid placing a disproportionate burden of recovery of common costs on interconnection services;

(f) where appropriate, interconnection costs shall include provision for a supplementary charge, being a contribution towards the access deficit of the interconnection provider;

(g) in the case of charges for wholesale termination services, charges shall be calculated on the basis of forward looking long run incremental cost, whereby the relevant increment is the wholesale termination service and which includes only avoidable costs.

5. In this Determination of Rates, the OUR made a determination on the wholesale fixed termination rates. As part of the implementation of these rates, the OUR must determine the timeline or glide path for the transition from the existing rate to the new rate. This determination is made at the discretion of the OUR.

6. The OUR, as a body making administrative decisions, is under a duty to exercise its discretionary powers reasonably and in good faith and on proper grounds. Where the discretion is exercised otherwise, it provides grounds for a party affected to argue that there has been an improper exercise of the discretion. In this instance, Flow submits that OUR's exercise of its discretion to set a six month glide path for the implementation of the fixed termination rates, is unreasonable and an improper exercise of its discretion.

7. Further, where a body making administrative decisions, has by promise or practice, conferred on a person a legitimate expectation of a procedural or substantive benefit, it may frustrate that expectation, if to do so would be so unfair as to amount to an abuse of power. In this instance, Flow submits that in the context that the OUR had indicated a glide path of a maximum period of two years in the course of the consultation leading to the Determination of Rates, and given the size of the reductions of the Fixed Termination Rates, it had a reasonable expectation that the OUR would have implemented the new rates over a glide path which was longer than six months, and specifically with a longer notice than twenty three days for the first reduction.

Background on the Determination of the Glide Path

8. In Chapter 7 of the OUR's Consultation Document 'Cost Models for Fixed Termination Rates – Principles and Methodology' dated 19 January 2015 ('the Methodology Consultation') the OUR set out its principles for determining a glide

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path with a proposed maximum period of two years and sought a response from the industry on the efficacy of a glide path. The OUR's arguments read *inter alia*:

> *7.4 The length of this glide path cannot be determined at this point as it will depend on the size of the difference between the TLRIC and Pure LRIC termination rates. It should also be noted that the mobile termination rate was immediately adjusted to the Pure LRIC level which has created an anomaly, which needs to be corrected, where the fixed termination is higher than the mobile termination rate and is set using a different cost standard. The OUR is however mindful that the glide path needs to be reasonably short to curtail the negative effects of having a fixed termination rate which is above cost. As such the OUR will decide on the exact length of the glide path after the model is developed and the fixed termination rate is calculated. However, the maximum time period that will be considered for rates to adjust to cost is two years.*

9. In its response to the Methodology Consultation, Cable & Wireless Jamaica Limited (then dba LIME) argued against an arbitrary determination of a maximum glide path, or in the alternative, if one is being set, for a three year glide path. The argument is excerpted below:

> *16.1. LIME disagrees with the approach proposed by the OUR with respect to the glidepath. It is first worth highlighting the three elements to the OUR's glidepath proposal on pages 44-45 of the Consultation Document:*
> *i. "if the existing termination rate is above the TLRIC rate estimated by the model, then that means the operator has reaped significant benefit from having a termination rate which is above cost. In this case, the OUR proposes to immediately adjust the termination rate to its TLRIC rate."*
> *ii. the OUR will then "allow a glidepath from the TLRIC rate to the pure LRIC rate".*
>
> *iii. the OUR will decide on the "exact length of the glidepath after the model is developed and the fixed termination rate is calculated. However, the maximum period that will be considered for rates to adjust to cost is two (2) years."*
>
> *16.2. With respect to the first element, we disagree with the supposition that if the TLRIC rate is above the existing termination rate, LIME will have "reaped significant benefit". LIME reminds the OUR that the TLRIC derived through this proceeding is not a cost based on LIME networks, but an optimized network. One cannot assert that the existing termination rate generates above normal profits for LIME simply because it is higher than the TLRIC rate developed from a model of an optimized network. In this light, an immediate move to TLRIC would be unjustifiably punitive. We note that the situation*

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> *with the fixed network is completely different from that that with the mobile networks where the rates implemented before the LRIC modeling were not cost-based and clearly far above the costs of termination.*
>
> *16.3. As a side note, we understand that the OUR's anticipates the termination rate that results from this process will not be "substantially different what exists now."* [sic] *It is interesting, then, that the OUR did not discuss the glidepath approach if opposite case resulted, i.e., if the existing termination rate is below the TLRIC. Would this imply that the LIME had incurred significant losses on its termination service? What would the glidepath look like in that case?*
>
> *16.4. With respect to the second element, we agree that the glidepath should follow from the existing rate to the TLRIC to the pure LRIC rate.*
>
> *16.5. However, with respect to the third element, we believe it is not fair to cap arbitrarily the glidepath period to two (2) years. The OUR's justification for the cap appears to be that is that* [sic] *the fixed termination rate is above the mobile termination rate. We do not believe this to be the case (the average fixed termination rate is in fact above the mobile termination rate); however, in any case, LIME fails to see the relevance.*
> *Finally, we note that the OUR in its July 24, 2012 Determination Notice indicated that the glidepath for the mobile termination rate would not exceed three (3) years. If the OUR feels that the glidepath adjustment period should be capped, three years is the more relevant timeframe.*
>
> *16.6. Thus, LIME believes that the glide path for fixed interconnection should follow the following timeline:*
> - *2016: Existing rates*
> - *2017: TLRIC rates*
> - *2018: Reduction to half of the difference to the pure LRIC rate determined by model for 2019*
> - *2019: pure LRIC rates determined by model for 2019*
> - *2020: pure LRIC rates determined by model for 2020*

10. The OUR issued its Determination Notice 'Cost Models for Fixed Termination Rates – Principles and Methodology' dated 1 July 2015 ('the Methodology Determination') with Determination 17 on glide paths:

> *The Office may resort to glide paths for adjusting termination rates, the exact length of which will only be defined after reviewing the rates from the modelling exercise.*

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11. The determination followed a discussion of responses from Cable & Wireless Jamaica Limited (then dba LIME) and Columbus Communications Limited (referred to as Flow below):

    Use of Glide Paths
    6.1. LIME disagreed with the proposed approach for implementing the glide path for adjusting termination rates from the TLRIC to the Pure LRIC values, regarding the following aspects:
    o The OUR should not assume that termination rates generate unusual profits for LIME simply because they are higher than the TLRIC rate obtained for an optimised network,
    o Absence of explanation regarding the proceedings for the cases where existing termination rate is below the TLRIC.
    o According to the glide path defined for the mobile termination rate, the glide path adjustment period for fixed termination rates should be capped to three (3) years.
    6.2. Flow presented concerns regarding OUR's definition of a "significant difference" between existing termination rates and the TLRIC rate. According to the operator, a better approach would be to first determine the rates resulting from the modelling exercise and use the information on the actual observed differentials to arrange for further consultation on glide paths.
    6.3. LIME is not opposed to Flow's proposal to wait for the model results before consulting on the final glide paths. However, LIME considers that two principles should be set out in advance:
    o " The adjustment should take place over a three (3) year period".
    o The TLRIC rate should be set as an intermediate step between the existing rate and the Pure LRIC.
    6.4. The Office however disagrees with LIME that termination rates higher than the TLRIC rate do not generate unusual profits. The model will estimate an efficient operator's cost of providing termination service. Consistent with the position in the mobile LRIC process, the Office will only consider a glide path from the TLRIC rate to the Pure LRIC rate. According to the Act, rates should be cost oriented. If the current termination rate is above the TLRIC rate estimated by the model then that means operators would have already reaped significant benefit from having a termination rate which is above cost. The Office is cognisant of the need for rates to be quickly aligned with costs to be compliant with the stipulations of the Act and to curtail the negative effects of having a fixed termination rate which is above cost.
    6.5. The Office therefore acknowledges both operators' concerns regarding the definition of glide paths and is in general in agreement with Flow's proposal to only decide on the final glide paths after the results for the modelled rates have been reviewed. However, as stated in

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the Consultation Document, the Office will only consider a glide path up to a maximum of two years.
Determination 17: The Office may resort to glide paths for adjusting termination rates, the exact length of which will only be defined after reviewing the rates from the modelling

12. Following the Methodology Determination, the OUR issued its consultation on the draft model 'Cost Models for Fixed Termination Rates – Draft Model Consultation Document' dated 22 June 2016 ('Draft Model Consultation'). The OUR subsequently issued the Determination on Rates which is the subject of this application, and made its determination on the glide path as set out below.

Fixed Termination Rates
15.3. In the Methodology published on 2015 July 1, the OUR stated that if an existing termination rate is above the TLRIC rate estimated by the model, this would mean that operators would have reaped significant benefits from having a termination which is above cost. The OUR indicated that should such a scenario occur, the termination rate will be immediately adjusted to its TLRIC level. The OUR also established that glide paths will be allowed from TLRIC rate to the Pure LRIC rate only where there is a significant difference in the rates in dollar terms. While the OUR established that the maximum time period for a glide path should be two (2) years, it indicated that it will only decide on the final glide paths, detailing exact lengths and the adjustment steps, after the model is developed and the fixed termination rate is calculated. The OUR did not however, indicate the approach to be taken in the scenario where the current termination rates are lower than the TLRIC level.
15.4. After comparing the model's results with the tariffs in the existing reference interconnection offer, the OUR observes that current termination rates are much lower than the TLRIC model results. This means that the current rates already accord with the principle of cost-orientation and as such C&WJ would not have been benefitting from supernormal profits. It was also observed that there were significant differences between current termination rates and the rates resulting from the new methodology (Pure LRIC). Table 21 shows the comparison of current termination rates against the average of the LRIC model results for 2017-2020.

Services	Units	Average RIO	Average 2017-2020	Difference
PSTN - Local	JMDcent/min	41.33	9.39	-77%
PSTN – National	JMDcent/min	115.16	9.58	-92%
PSTN – International	JMDcent/min	144.70	10.04	-93%

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> *Services*
> *15.5 In its deliberations regarding the implementation of a glide path, the OUR took note of the significant differences found between the current rates and the Pure LRIC rates and the impact that the immediate reduction of the rates to the Pure LRIC level would have on C&WJ revenues. The fact that the current rates were also not above TLRIC was also taken into account. Based on these considerations, the OUR decided, in keeping with its statutory mandate to balance short term welfare gains of immediate price reductions with the long term interests of protection of efficient investment incentives, to implement a two-step glide-path. The first step of the glide-path for fixed termination rates becomes effective on 2017 July 1 and remains in effect until 2017 December 31. The second step will become effective on 2018 January 1.*

The OUR's Determination of a Six Month Glide Path

13. Flow is surprised at the six month glide path which has been set out by the OUR in the Determination on Rates. In the Methodology Consultation, the OUR proposed a maximum two year glide path. Flow had presented arguments for a three year glide path, in response to the OUR's suggested glide path. The OUR advised that it would make a determination on the glide path when the rates were set.

14. In the Draft Model Consultation which followed the Fixed Rate Termination was the Methodology Consultation, in the consultation process, the OUR gave no indication that it was moving away from the two year glide path previously determined. In the context of the consultation proceedings, and given the size of the reductions in the Fixed Termination Rates, Flow had a legitimate expectation, that any glide path determined by the OUR would be at least a two year glide path.

15. The OUR issued the six month glide path based inter alia on the following argument set out in the Determination on Rates:

> *15.5 In its deliberations regarding the implementation of a glide path, the OUR took note of the significant differences found between the current rates and the Pure LRIC rates and the impact that the immediate reduction of the rates to the Pure LRIC level would have on C&WJ revenues. The fact that the current rates were also not above TLRIC was also taken into account. <u>Based on these considerations, the OUR decided, in keeping with its statutory mandate to balance short term welfare gains of immediate price reductions with the long term interests of protection of efficient investment incentives, to implement a two-step glide-path.</u> The first step of the glide-path for fixed termination rates becomes effective*

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> *on 2017 July 1 and remains in effect until 2017 December 31. The second step will become effective on 2018 January 1.* (Emphasis Flow's)

Flow submits that as the determination of the glide path is at the discretion of the OUR. It is obliged to "balance short term welfare gains of immediate price reductions with the long term interests of protection of efficient investment incentives" in determining the glide path. Flow argues that in this instance, the OUR has failed to properly conduct that balancing exercise. In that it has exercised its discretion to implement a six months glide path with almost immediate effect for the first reduction, to the detriment to the "efficient investment incentive". The OUR does not appear to have given consideration to the magnitude of such sharp reductions on the immediate cash flow of the company, and the immediate and direct impact this reduction will have on working capital, investment incentives and potentially the long-term welfare of the society itself. Flow submits that there is no provision in the Determination on Rates which indicates that the OUR moved from the academic exercise of setting the fixed termination rates, to taking into consideration the impact of its determination on a business.

The Effect of the Reduction in Fixed Termination Rates on Flow's Wholesale Business

16. It is important to appreciate the difference between the existing and new rates, which is set out in the table below.

Services	UNITS	Current Rates	Rates – Jul 2017	Initial Change	Rates – Jan 2018	Overall Reduction
PSTN - Local	Jam $	$0.4133	$0.2536	39%	$0.0939	77%
PSTN – National	Jam $	$1.1516	$0.6237	46%	$0.0958	92%
PSTN – International	Jam $	$1.4470	$0.7737	47%	$0.1004	93%

If Flow's wholesale business is forced to implement the drastic revenue reduction over a six month time period, it will have a deleterious effect on Flow's ability to maintain and invest in its Wholesale Carrier Services operations.

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The reduction in the rates for the Incoming International Call Termination Service on PSTN, will also impose irreparable harm on Flow's Wholesale Carrier Services operations. Reducing these rates by the magnitude specified in the OUR's determination, over a truncated six month period, will significantly increase arbitrage between the termination rate and the settlement rates. This effect will reduce the settlement rates paid by overseas carriers and further diminish the resources required by licensed operators in Jamaica to maintain and invest in their networks.

The projected impact on the revenue of Flow's Wholesale Carrier Services operation is set out below:

[CONFIDENTIAL]

Remedies

17. In the circumstances, Flow seeks:
    (i) a glide path of a minimum of two years or a maximum of three years for the implementation of the reductions in Fixed Termination Rates as set out in the Determination on Rates; and
    (ii) a stay in the effective date of the first reduction from 1 July 2017 to a date when the new glide path is determined by the OUR or pending an appeal to the Appeal Tribunal.

Flow anticipates the favourable response of the OUR to this application. In the event that a stay of the effective date of the first reduction of 1 July 2017 is not granted, Flow requests that we be advised by the OUR on or before 27 June 2017.

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We reserve all rights in this matter.

Yours faithfully

Sola T. Hines (Ms.)
Legal & Regulatory Counsel

cc: Ms. Rochelle Cameron, VP Legal & Regulatory, Jamaica, Cayman, Trinidad & Tobago, Flow
Mr. Cedric Wilson, Director Regulatory, Policy, Monitoring & Enforcement, OUR