REVIEW OF ACCOUNTING SEPARATION GUIDELINES

OBJECTIVE

1. To share with the industry and public IDA's decision following its review of the responses received to its consultation paper on the "Review of Accounting Separation for the Telecommunication Sector in Singapore".

BACKGROUND

2. IDA issued a consultation paper on 23 May 2001 to seek comments from the industry on the enhanced changes to the Accounting Separation Guidelines (ASG) for the telecommunication sector in Singapore to better meet the needs of a fully liberalised market.

3. On 25 May 2001, IDA conducted an Industry Forum to present an overview of the enhanced changes. Thirty-two attendees representing the Facilities-Based Operators (FBOs) attended the Forum. In response to the industry's request, IDA extended the deadline for submission of comments from 21 June 2001 to 29 June 2001.

4. Nine parties filed their comments at the close of the consultation: (1) Concert Global Networks (Singapore) Pte Ltd; (2) East Asia Crossing Singapore Pte Ltd (EAC); (3) MobileOne (Asia) Pte Ltd (M1); (4) Pacific Internet Limited (PI); (5) QALA Singapore Pte Ltd; (6) ST Teleport Pte Ltd; (7) StarHub Pte Ltd; (8) SingTel Group & (9) Singapore Cable Vision Ltd (SCV). IDA thanks all parties for their considered and constructive views and comments.

SUMMARY OF RESPONSES

5. Generally, industry players were in favour of most of the enhancements proposed. SingTel, however, viewed that the existing ASG already adequately addressed regulatory requirements. The imposition of a new Accounting Separation system would impose significant regulatory compliance costs which could far outweigh any benefits. QALA viewed

that non-dominant licensees should not be required to report at all due to the high implementation costs involved.

6. The following key points were made in the submissions:

<u>Two –level approach</u>
With the exception of SingTel, all Licensees who responded were in favour of the two-level approach to Accounting Separation, i.e. Detailed Segment Reporting (DSR) for Dominant Licensees and Simplified Segment Reporting (SSR) for non-Dominant Licensees. SingTel argued that a two-level approach is discriminatory against dominant Licensees and should therefore be aborted.

SCV contended that they should not be subject to DSR as they are not a truly dominant telecommunication company given the fact that they face intense and effective competition in all their markets.

<u>CCA vs HCA</u>
All responses were in favour of a Historical Cost Accounting (HCA) regime for Accounting Separation and were against the implementation of Current Cost Accounting (CCA), primarily due to the high cost of implementation.

<u>Degree of disaggregation and segment definitions</u>
The comments received were generally positive except for the differentiation of Internet access into Narrowband and Broadband. Some of the Licensees who responded saw no need for the segmentation given that the only difference between the two is speed of service delivery.

Comments were also made that the disaggregation of costs into fixed and variable elements is not useful and the cost of such disaggregation would outweigh the benefits derived. A similar comment was made with regard to the classification of costs as direct, directly attributable and indirectly attributable.

<u>Preferred method of cost allocation</u>
Comments were made that the allocation of unattributable costs based on contribution margin would give rise to cross-subsidies where there are negative margins.

7 In addition to the above, IDA received comments on the necessity to provide non-financial information and the cost effectiveness of producing the Statement of Mean Capital Employed. Suggestions were

also received on the extension of the timeframes for implementation and reporting as well as for the Statement of Mean Capital Employed to be submitted annually instead of half-yearly.

IDA'S CONSIDERATION OF THE KEY POINTS RAISED

8 **Two –level approach**

IDA views that the two-level approach to accounting separation should be maintained. This is consistent with international practices where operators with market power who could potentially use their position to engage in anti-competitive behaviour are subject to more stringent accounting separation arrangements. It would not be considered reasonable to impose DSR on non-dominant operators, as it is unlikely that non-dominant operators would be able to act anti-competitively.

CCA vs HCA

Due to the complexities and high cost of implementing CCA, any move towards that direction would involve a separate consultation process. IDA therefore agrees that HCA should continue to be used as the cost accounting base, and will consult the industry if it decides to move towards CCA.

Degree of disaggregation and segment definitions

IDA agrees that speed of service delivery as a differentiating factor in segmenting Internet access needs to be redefined. Nonetheless, segmentation is still necessary as there is a difference in the cost and revenue structures of Internet access services provided across different technology platforms. The segmentation into Narrowband and Broadband Internet access have thus been removed and replaced with four categories of Internet Access for both DSR and SSR namely, (i) dial-up over PSTN or ISDN, (ii) xDSL, (iii) HFC cable, (iv) other access modes such as private leased circuits.

Preferred method of cost allocation

IDA agrees that the allocation of unattributable costs based on contribution margin would give rise to cross-subsidies where there are negative or zero margins. To prevent this from occurring, IDA has changed the basis to an allocation based on direct, directly attributable and indirectly attributable costs. Licensees who wish to adopt another method of allocating these costs will be required to provide justifications for IDA's approval.

9 Other changes made include: -

(a) Modifying the Simplified Segment Income Statements to show separate revenues and costs received from or paid to external sources, the Licensee's internal businesses, controlled entities and/or related entities; and

(b) Removing the need to provide non-financial information that are currently submitted to IDA to prevent duplication of effort.

IDA'S DECISION

10 After careful consideration of the industry's feedback and follow-up discussions with IDA's consultants, IDA has decided to adopt the revised ASG as specified in **Annex A** which incorporates the above key changes.

11 The revised ASG will be **effective from 1 October 2001**. All FBOs must submit their revised Procedure and Cost Allocation Manual (PCAM) to IDA for approval within 90 days of the effective date of the ASG i.e by 29 December 2001. Subject to modifications which IDA may request, IDA will notify the Licensee of its approval within a further 90 days. The approval period may be extended by IDA if, for example, substantial modifications are required to the Licensee's initial proposed PCAM. Modifications that are requested by IDA must be incorporated in a revised PCAM and re-submitted to IDA within 30 days of the modification request. In its approval notice, IDA will notify the Licensee of the date on which the Licensee must begin reporting in compliance with the ASG.

12 Existing Licensees should continue to report under the current ASG until IDA has approved their revised PCAM. Those with financial year ending on March and December must adopt the revised PCAM from 1 April 2002 and 1 July 2002 respectively. Early adoption of the revised PCAM, subject to IDA's approval, is allowed.

13 Non-dominant FBOs who wish to be exempted from complying with the entire or certain provisions of the ASG must write in to IDA stating the reasons for the requested exemption.