

No.022/TRAI/2011-12/ ACTO
Dated 10th February, 2012

Mrs. Anuradha Mitra,
Principal Advisor (FA&IFA)
Telecom Regulatory Authority of India,
Mahanagar Doorsanchar Bhawan,
Jawaharlal Nehru Marg (Old Minto Road),
New Delhi-110002.

Subject: Draft "The Reporting System on Accounting Separation Regulations, 2012" - Views / Suggestions regarding.

Ref.: ACTO's Letter No. 006/TRAI/2011-12/ ACTO dated 8th July 2011.
ACTO's Letter No. TRAI/2009-10/108 dated 11th August 2009

Respected Madam,

On behalf of Association of Competitive Telecom Operators (ACTO) and its members, we are pleased to submit our comments on the subject matter. We also thank the Authority for providing us an opportunity to submit our views on Draft "The Reporting System on Accounting Separation Regulations, 2012"

Our comments are enclosed for kind consideration of the Hon'ble Authority.

Thanking you,
Respectfully submitted

Yours sincerely,
for Association of Competitive Telecom Operators

Naveen Tandon

Naveen Tandon
Vice-President
+91-9811163896

(ACTO's reference letters enclosed as Annex-D)

**ACTO Response to TRAI on
“The Reporting System on Accounting Separation Regulations, 2012”
(hereinafter referred to as “proposed ASR 2012)**

ACTO welcomes the efforts of the TRAI in reviewing the Accounting Separation Regulations, 2004.

2. The System on Accounting Separation is a set of rules and procedures to ensure the attribution and allocation of revenues, costs, assets, liabilities and capital employed to individual activities and services, in particular considering direct and indirect operating costs.
3. The purpose of imposing an obligation regarding the Accounting Separation is to ensure that fair, pro-competitive and transparent criteria are followed by telecom service providers in allocating their costs to the services/ products and to prevent predatory conduct. The major resulting benefit has a transparent illustration of the relation between costs and prices (at both wholesale and retail levels), as the Accounting separation system should be able to break costs down in order to ensure that costs allocated to services/products do not result in cross subsidies, excessive prices and, in general, that costs are efficiently incurred.
4. It is important to note that under the Accounting Separation System, the transfer charges of services and/or internal purchases need to be clearly identified on business activity level to fulfill compliance with non-discrimination obligations. Transfer charges shall be the same as the prices charged for services offered by other telecom companies at the same conditions (i.e. provided at arm's length to downstream affiliate companies). The detail of information provided to the

Regulator should serve to ensure that there has been no price discrimination between the provisions of services internally and those provided externally to customers and allow identification of the average cost of services and the method by which costs have been calculated.

5. It has been observed that under the present accounting separation regulations, there is no system to ensure, check and determine that the transfer charges are non-discriminatory and the significant market powers / incumbents are not involved in anti-competitive, unfair and discriminatory behavior. It has also been noted that under the proposed ASR 2012, this issue somehow has not been taken up very clearly which we request it should be taken. Through proforma 'H'- "Statement of Related Party Transaction" an attempt has been made but there is no system to calculate the average cost of the product or network services provided internally or externally. As Accounting Separation is a common tool used by various telecom regulators to address anti-competitive concerns, therefore, the proposed ASR 2012 should generally enable monitoring of a systematic division of costs between retail and wholesale (external and internal).
6. The proposed ASR, 2012 presents some important changes over the existing established accounting separation regime/framework which was established over a period of time through a consultative process. For e.g. the present accounting separation reports are required to be prepared based on the Central Government Notification No. GSR 782(E) dated 27.11.2002, Notification / Order No. 7-4/2001-tariff dated

21st October, 2003 (**enclosed as Annex-A**) and guidelines issued by TRAI on System on Accounting Separation in December, 2002¹.

7. We would like to draw the attention of the Hon'ble Authority to the fact that International Telecom Union(ITU)'s Guidelines on the implementation of Regulatory Accounting in Telecommunications Sector of March, 2009 (**enclosed as Annex - B**) has recognized that accounting separation and cost accounting models are *ex-ante* obligations imposed on Significant Market Power (SMP) operators worldwide. Other available documents on the subject have also recognized that Accounting Separation is typically applied only to incumbent / SMP telecom service providers to monitor and identify anticompetitive conduct. Operators that have not been designated dominant or SMP in the relevant markets are exempt from such obligations or are subject to light-handed reporting requirements.

*(For ready reference please find **enclosed as Annex - C**, Accounting Separation Guideline-2004 released by IDA – Singapore Regulator)*

8. When considering which operators should be subject to an ex-ante regulation, the principles of proportionality and regulatory forbearance are considered. The implementation and upkeep of the accounting separation system requires significant regulatory resources if detailed and extensive reporting is required. This is justified if the operator in question is in a position to exploit its market power and potentially behave in an anti-competitive manner in the provision of wholesale and retail telecom services to access seekers. Conversely, imposing the same reporting requirements on operators that are not in the position to influence competition like our members and that do not

¹ http://www.trai.gov.in/Recommendations_content.asp

have dominant control bottleneck and/or other essential facilities should be reconsidered as the application of regulation must be driven by the objectives that they are meant to achieve. A one-size-fits-all regulation in this instance could be construed as “over-regulation” of alternative operators. Proportionate regulation also ensures that the authority’s resources are focused on more critical areas i.e. where there is a risk of anticompetitive conduct.

9. We are of the view that the proposed accounting separation guidelines, which are extremely detailed, will be appropriate for the monitoring of dominant/SMP operators but will be disproportionate for alternative operators. We urge TRAI to adopt practices similar to that applied internationally to the applicability / ambit of the proposed ASR on the service providers.
10. The Authority has very rightly noted in para 1 of the letter NO.16-07/2010-FA dated 16th January, 2012 that ASR enables the authority to address anticompetitive behavior, discrimination and predatory pricing concerns and to facilitate fair competition. It is further substantiated by the fact as mentioned in para 4 of the said letter that *“Business models of service providers have also changed over time. Vertically integrated telecom, service providers provide retail telecom services and products as well as wholesale services within the same jurisdiction with substantial concentration of market power..... New and more complex forms of upstream and downstream market relationships have emerged”*.
11. We note that there are no operators currently designated as SMP or dominant even if there are criteria recommended for such a determination (e.g., based on market share / revenue) in related context. An alternative approach to applying the proportionality

principle therefore is to distinguish between vertically integrated telecoms operators and non-integrated, stand alone operators (our member companies) that compete predominantly in the downstream telecom services market along with vertically integrated operators.

12. The latter would not be in a position to influence the competition particularly given that we rely on the integrated operators to provide us with relevant telecom resources. Given this, we believe that the information provided to the TRAI will largely be inconsequential in the TRAI's monitoring of anticompetitive conduct, but will require considerable regulatory resources of alternative operators.
13. We request that the authority forebears vertically non-integrated / standalone operators like our member companies from imposing ASR, by revising the threshold limit to INR 2,000 crores and above to be applied license wise.
14. It is humbly submitted that if TRAI is keen to implement the ASR in general at the very minimum we request that the reporting requirements should be divided into two separate set of formats for two levels operators, i.e. one for those who are vertically integrated operators providing up and downstream telecom services and the other for non-integrated / standalone telecom service providers. The formats and requirements should be devised accordingly.
15. The proposed regulation is required that with a view to assess the performance of new accounting separation statement, the service providers would be expected to provide the data for the last accounting year (2010-11) in soft copy in revised Proforma as

prescribed in Schedule-III to the draft Regulations. Such new provision under the proposed ASR, besides being a time consuming exercise, will increase the cost of implementation cost of accounting separation system. We therefore request that the same be dispensed with.

16. As per Regulation 3 on Manual & Reports, Service Providers are required to submit a copy of the Manual within one month from the date of commencement of new Regulation whereas Accounting Separation Manual has already been submitted by the service providers. Since there is no change in the items / information sought of the manual of the proposed ASR and the existing ASR, we request that there should not be any duplication of the information which has already been submitted to the Authority and accordingly the service providers who have already submitted the manual to TRAI should not be asked to submit it again unless there is a change.
17. As per Regulation 4(2) on Reports, the authority requires that in addition to the reports prepared based on Historical Cost Accounting, reports prepared based on Replacement Cost Accounting are also required for every second year. It is our experience that such requirements for Replacement Cost Accounting reports are almost always exclusively required only for dominant/SMP operators as arriving at such reports can be extremely costly involving significant resources which increases regulatory cost. We are of the view that only the vertically integrated / SMP operators should be obliged to provide these Replacement Cost Accounting reports. The replacement cost based reporting every alternate year should be dispensed with for vertically non integrated operators..

18. It is also requested that vertically non integrated operators may be exempted from the auditing as the auditor is not verifying any cost allocation / attribution parameters notified / approved by the TRAI. The Auditor is verifying only those parameters that have been filed by the telecom service provider under the accounting separation manual. Over and above, since the preparation and allocation of cost, revenue and capital employed is the responsibility of the management / company, therefore, merely verification of the data / arithmetic calculation in the prescribed format by the auditor for the sake of formality will not provide any fruitful results to TRAI and Telecom Service Providers.
19. With respect to auditing & Audit Report, our suggestion is that since as per the TRAI Act, management or officers of the company would be held responsible for any incorrect data submitted to the Authority, we would like to suggest that instead of asking for the auditor's opinion/certificate, if it is certified by the member of the Institute of Chartered Accountant of India (ICAI) or Institute of Cost and Works Accountants of India (ICWAI), whether member is in service / service in the same company or in practice, the same should be considered as a compliance of audit formalities under the proposed regulations. This would help to reduce the cost of the concerned service provider.
20. It is important to note that under the proposed regulations, TRAI has not prescribed as to which books of accounts should be the basis for preparation of accounting separation reports. Whether statutory financial statement prepared under Section 211 of the Companies Act 1956 or books of accounts prescribed under DOT's notification No. GSR 782(E) dated 27.11.2002 on "The Telecom Authority of India,

Service Providers (Maintenance of Books of Accounts and other Documents) Rules, 2002 to specify books of accounts which are to be maintained and notification / order No. 7-4/2001-Tariff dated 21st October, 2003 in the Gazette of India to specify the manner in which books of accounts / other documents are to be maintained. We understand that even in the new ASR, the underlying account preparation norms will remain same.

21. In Schedule IV of the Regulation TRAI has mandated for a certificate under which auditor has been asked to comment / opinion observation with respect to keeping of books of accounts in compliance of standard / costing principles issues by ICWAI. The relevant portion of the report as indicated in para 3(b) is reproduced below:

"In my / our opinion proper book of accounts have been kept by the company in compliance of cost accounting standards issued by Institute of Cost & Works Accountants of India and generally accepted cost accounting principles so far as appears from my / our examination of those books to enable the preparation of complete and proper accounting separation reports in accordance with the regulations"

With respect to above provision it is respectfully mentioned that in the main draft regulations, there is no specific provision to the effect that books of accounts will be maintained as per the standard issued by the ICWAI. Even as per our information, till date ICWAI has not issued any standards or principal *per se* applicable for Indian Telecom Industry. Therefore, this very specific clause will be in contradiction of TRAI's own guidelines on system on accounting separation which has been considered as a guiding factor for preparation of TRAI's ASR Reports till now.

In view of above facts instead of referring the standards/principles issued by the ICWAI, TRAI may update / revise its own present guidelines on “system on accounting separations” which shall be referred as underline principle / standards for preparation of proposed accounting separation reports as the prevailing practice in ASR are prepared based on guidelines issued by TRAI.

Summing up:

- The proposed ASR may be aligned with the international best practices / guidelines issued by the ITU and international regulatory practices. It should be applicable only to incumbents and SMP telecom service providers and not to vertically non-integrated / standalone operators as our members.
- The proposed ASR should have a system to examine the issue of anti-competitive behavior of telecom service providers. Therefore, the proposed proforma of ASR should be aligned in such a manner that it may provide the relevant information on the face of Proforma ‘B’ (Profit & Loss Statement for each product as prescribed in Schedule-I of the proposed regulation) and Proforma ‘H’ (Statement of related party transactions) to show the average cost per unit of services as well as revenue realized against it.
- The proposed ASR does not provide any relief to the standalone non-integrated telecom service provider. On the contrary, it has somehow created confusion regarding the maintenance of regulatory accounts hence forth.

- TRAI may consider two separate set of formats for two levels of operators, i.e. one for those who are vertically integrated operators providing up and downstream telecom services and the other for non-integrated telecom service providers.
- With respect to auditing & Audit Report, we would like to suggest that instead of asking for the auditor's opinion/certificate, if it is certified by the member of the ICAI or ICWAI, the same should be considered as a compliance of audit formalities under the proposed regulations. This would help to reduce the cost of the concerned service provider.
- A careful glance at the paper reveals that there are no major changes in the regulations and the formats have not been simplified or renewed as per the requirement of time and the same are as cumbersome as the existing ones. These need to be further reduced and revised based on classification of vertically integrated / SMP and vertically non-integrated / standalone operators.
- Further we have noted that in various regulations / Tariff orders / Guidelines, TRAI has proposed to switch over to forward looking costing allocation principles i.e. from FAC to Long Run Incremental Cost (LRIC) etc. Perhaps, the LRIC and its variants have not been indicated in the proposed ASR.
- We request to consider reframing of the draft ASR in a way to address the concerns of the competition which are taking place / will take place in the near future.

- Before finalizing proposed ASR, TRAI may update / revise its own existing guidelines on “system on accounting separations” which shall be referred as underline principle / standards for preparation of proposed accounting separation reports.
- Lastly, we understand that the implementation of the new ASR regulation should be made effective from a prospective date.
