THE HASHEMITE KINGDOM OF JORDAN

TELECOMMUNICATIONS REGULATORY COMMISSION

Accounting Separation Instructions

Explanatory Memorandum

November 2012

Content

1 Introduction

The Explanatory Memorandum summarises and evaluates the comments of the various members of the telecommunications industry in Jordan to the “Public Consultation on Accounting Separation Instructions” published by the TRC on 13 July 2011.

Formal responses to the Public Consultation Paper were received from Petra Jordanian Mobile Telecommunications Company (Orange Mobile), Jordan Telecommunications Company (Orange Fixed), Umniah Mobile Company / Batelco Jordan (Umniah/BTJ) unified response and Jordan Mobile Telephone Services Company (Zain).

This process was followed with another round of comments on comments where TRC received comments from Jordan Telecommunications Company (Orange Fixed), Umniah Mobile Company / Batelco Jordan (Umniah/BTJ) unified response and Jordan Mobile Telephone Services Company (Zain).

This Explanatory Memorandum provides an overview of the comments received by all operators and their comments on the interested parties responses accompanied by the TRC’s reasoned responses to those comments. In the discussion which follows, the TRC has maintained the original sequence of questions, and provided its assessment of those responses that are directed to a specific question.

2 General comments

In addition to the questions addressed in the consultation document, the stakeholders provided some general comments which are dealt with in this section.

Zain states that a cost-benefit analysis regarding the obligation for them to provide accounting separation would show that the costs outweigh the benefits of this obligation with regard to Zain. One of the reasons mentioned is that there is no additional benefit to the implemented cost model. Zain is also questioning the reason why they have this obligation when Umniah does not, and points out that both operators should be treated equally in this case. In Zain's comment on comments, they state that they agree with TRC that Orange Mobile should provide accounting separation due to its relationship with Orange Fixed.

Zain is generally asking for the proportionality of the remedy and addresses the questions of CCA, MEA and ABC and states that these issues imply that the regulatory burden is significant. On the other hand, as so few mobile markets are regulated, Zain asks if there are competition problems which can be addressed by accounting separation.

Orange Fixed and Orange Mobile list the principles they regard to be fulfilled when imposing remedies. They also state that the regulatory burden of accounting separation is high and that there are other remedies available to address the competition problems. Orange Mobile states that it is not the case in the mobile markets, as dominance has only been found for Orange in the termination markets and that it therefore has no possibility to cross-subsidize. Further, the TSLRIC cost model has been implemented and therefore neither excessive prices nor lack of transparency are problems to be addressed by accounting separation. Further, Orange Mobile refers to the retail markets shares and thereby sees no reasons for a different treatment of Umniah.

In their comments on comments, Zain expressed that they agree with Orange that accounting separation for mobile termination markets is disproportionate.

Orange Fixed also states that they see no justification to have accounting separation for any sub-division of SMP markets or non-SMP markets.

Orange Fixed and Orange Mobile state that there are better and more cost efficient ways to obtain ad-hoc information than to request for ad-hoc accounting separation.

Further, Orange Fixed and Orange Mobile state that accounting separation cannot be used for tariff regulation as different cost standards are used, that accounting separation information should be treated confidential and that the proposed formats and separated accounts should have been included in the consultation. The latter was also addressed by Zain in their comments on comments.

In their comments on comments, Orange Fixed and Orange Mobile agree with Zain that the remedy is disproportionate but disagree with Zain that there should be a lack of practicability. They disagree as well that there are arguments that accounting separation should be implemented in fixed markets. Further, Orange Fixed agrees with Zain that the LRIC model provides sufficient information to TRC.

Umniah/BTJ has stated in their comments on comments that the issue raised by the other stakeholders with regard to the justification for accounting separation and the obligation imposed are related to the market review decisions and therefore not relevant for this consultation. Further, Umniah/BTJ states that the obligation of accounting separation imposed on Zain and Orange is appropriate against the competition problems that exist (mentioned are cross subsidies, excessive prices and that costs should be efficiently incurred) and according to best practice. In the comments on comments provided by Umniah/BTJ, it is stated that the LRIC model is not enough to provide transparency.

With regard to the exclusion of Umniah from the accounting separation obligation, the operators Umniah/BTJ agree with TRC and state that Umniah is a “challenger” with other incentives and that they are neither integrated with a fixed dominant operator in the way Orange Mobile is nor dominant in the MACO market.

TRC Response

The general comments submitted by the stakeholders refer to the market review decision and not to this consultation. The decision to levy accounting separation has been taken previously and the current consultation only deals with the way by which this obligation is implemented. TRC would like to remind the market participants that accounting separation has been imposed as a remedy based on the potential competition problems identified throughout the process of market reviews.

Accounting Separation as a remedy to deal with competition problems is internationally widely implemented. TRC would also like to highlight that the decision to implement accounting separation is a decision based on the specific competition situation in Jordan and aims to overcome the possibility to discriminate and price squeeze and the possibility of a leverage of market dominance from one market to another (horizontally and vertically).

With regards to Zain`s comments about the additional benefit from accounting separation considering the implemented costing model, TRC would like to clarify that the costing model in difference to Accounting Separation is based on LRIC and that it is a forward looking. By applying accounting separation according to the principles set out in the accounting separation decision, TRC can better monitor the activity of relevant operators in all markets and enhance the ability of TRC to handle potential competition problems based on current and historic costs.

Further issues regarding the proportionality of the imposed remedies are discussed in the TRC responses throughout this document where it is applicable. TRC would also like to refer to the documents published with regard to the market review decisions.

With regard to Zain’s questions on CCA, MEA and ABC, these are dealt with below. Also the question raised by Orange Fixed stating that they see no justification to have accounting separation for any sub-division of SMP markets or non-SMP markets is dealt with below.

3 Introduction to Accounting Separation

Consultation question I: Do you agree with this aim and scope of Accounting Separation?

Zain agrees with TRC with regard to the aim and scope, though it argued that the remedy should not be imposed on Zain.

Umniah/BTJ has suggested an aim and scope which is focusing on promoting competition and transparency.

Orange fixed and Orange Mobile agree that accounting separation may be used to support the decision making of TRC but its value needs to be put into perspective, i.e. costs and benefits need to be weighed. Such support is ancillary to the main purpose of accounting separation and its scope/detail should not be extended for this purpose.

Orange Fixed and Orange Mobile state that the aims and benefits are overstated according to their point of view. They state that:

- Accounting separation can assist TRC in examining, but cannot 'demonstrate' compliance, absence of cross-subsidies and it cannot 'guarantee' transparency.

- The accounting separation will provide TRC with information needed for other regulatory obligations, but should not be used as a shopping trip for information. The regulator is entitled to obtain information, but accounting separation should not be the means of getting ad-hoc information.

- Accounting Separation as a standard tool will not be sufficient to fulfil other regulatory tasks, such as the cost-based pricing because this pricing is set by TRC using Efficient Hybrid TSLRIC costing methodologies.

- The objective of accounting separation stated in the consultation 'to give transparency to the market participants' is not correct except to the extent that this is a specific justified remedy to a specific market failure in a specific SMP market, which is not the case for the Jordan mobile call termination market.

- The scope of accounting separation should be limited to SMP markets of a dominant operator.

TRC Response

The issue raised by Zain that accounting separation should not be imposed on them is not the scope of this national consultation. In spite of this, TRC would like to clarify that there are several reasons why there is a benefit imposing Accounting Separation on Zain as well:

- Accounting Separation provides additional costing information as it is based on FAC (CCA) while the cost model is based on TSLRIC+. For assessment of cross subsidization, the costs based on FAC are relevant because they are closer to the actual costs and profits of the licensee than the costs of TSLRIC+ are.

- In addition, Accounting Separation shows the outcomes of the tariff regulation on the actual profitability for licensees derived from the regulated termination services (while TSLRIC+ assessments only show the theoretical profitability as a hypothetical efficient TSLRIC+ model is used).

- Further, due to the fact that Zain has been designated to have SMP in two markets, including the MACO market, there is a risk of cross subsidization both between the two regulated markets as well as between regulated markets and non-regulated markets.

- Accounting separation has proven to be an effective tool in many countries to overcome structural problems of asymmetric information between regulator and regulated companies and to overcome competition problems identified in the process of market analysis.

For these reasons, the implementation of Accounting Separation as an obligation for Zain will provide TRC with a tool to obtain information necessary to identify and remedy competition problems.

With regard to the comments by Umniah/BTJ that the aim and scope should be focusing on promoting competition and transparency, TRC regards the outcomes of the suggestion of Umniah/BTJ on the aim and scope to be comparable to the proposal in the draft consultation document.

With regard to the first point stated by Orange (Accounting Separation can assist TRC in examining, but cannot ‘demonstrate’ compliance, absence of cross-subsidies and it cannot ‘guarantee’ transparency), TRC has based its proposed Accounting Separation instructions on the international best practice, i.e. the ERG states that accounting separation can be applied to demonstrate compliance:[1]

> *An accounting separation system is a comprehensive set of accounting principles, procedures and techniques that can be applied to the preparation of financial information that demonstrates compliance with non-discrimination obligations and the absence of anti-competitive cross-subsidies. The outputs of such a system must be capable of independent verification (auditable) and fairly present the financial position and relationship (transfer charge arrangements) between product and service markets. Using accounting separation, a National Regulatory Authority (NRA) imposes on the notified operator a set of rules on how accounting information should be collected and reported.*

To make it more clearly, accounting separation is a tool to be used in regulations. According to the Market Review Decisions, severe competition problems have been identified in a set of Telecommunication markets, including the risks of cross-subsidization and other types of anti-competitive behaviour related to tariffs. In such cases, accounting separation provides necessary information. TRC does not agree that Accounting Separation cannot demonstrate the existence of anti-competitive behaviour. It does for instance indeed show if there are negative margins in some markets, financed by high margins in other markets, i.e. cross-subsidization. Further, according to the text proposed by TRC, it is stated that accounting separation will provide information and that this information is a tool for TRC, but not that it in itself will remedy the competition problems. As the value of information always depends on its quality and the specific situation, there might be situations where the information might not be enough and therefore TRC amends the Article 3 (b) with the word “can” to “The aim of Accounting Separation is to provide information that <u>can:</u>”.

With regard to the second point of Orange Fixed and Mobile (the accounting separation will provide TRC with information needed for other regulatory obligations, but should not be used

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1 ERG Report, Regulatory Accounting in Practice 2009, October 2009, ERG (09)41, p. 4.

as shopping trip for information and there should be no requirement for ad-hoc requests), this consideration has already been acknowledged by TRC in the proposed Instructions. It is stated that when ad-hoc information is required, TRC must provide well-founded reasons for this. This prevents that information requests are made when the benefits are not motivated by the related costs. Further, accounting separation has been decided within the Market Review Decisions in order to provide TRC with a tool to identify cross-subsidization and other anti-competitive behaviours related to tariffs. Within this decision, competition problems related to prices and tariffs, especially in the case of Orange Fixed where these have been identified for multiple markets, have been found. In these decisions, accounting separation has been deemed necessary. I.e. Accounting separation on an annual basis is required as an obligation due to the fact that it provides accounting information to TRC needed to deal with the problems of information asymmetry between the regulated operator and the regulator.

With regard to the third bullet point of Orange Fixed and Mobile (i.e. that Accounting Separation is a standard tool that will not be sufficient to fulfil other regulatory tasks because this pricing is set by TRC using Efficient Hybrid TSLRIC+ costing methodologies), TRC disagrees with Orange. The Accounting Separation information can be used by TRC to assess if the results of the Hybrid Model are consistent with the accounting data or not. It is not stated in the TRC proposal that the results of the Accounting Separation will be used solely, but that these results will support the decision making. There are several reasons to impose accounting separation also for the mobile markets:

- As already stated above Accounting Separation provides additional costing information as it is based on FAC (CCA) and not TSLRIC+ and further, it additionally shows the outcomes of the tariff regulation on the actual profitability for licensees.

- Further, data derived from FAC imposed via an Accounting Separation remedy are required to calibrate the input data of the LRIC model. That is also a specific recommendation #3 of the European Commission Recommendation on fixed and mobile termination rates (2009/396/EC)[2].

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[2] According to this recommendation, NRAs may compare the results of the Bottom-up modeling approach with those of a Top Down model which uses audited data with a view to verifying and improving the robustness of the results and may make adjustments accordingly.

- In difference to the tariff regulation based on cost modelling, Accounting Separation provides information on the profit margins for several markets and is therefore a tool to identify cross-subsidization. This is not the case for the cost models.

- For Orange Mobile and Orange Fixed, there is an additional reason to impose accounting separation, namely the relationship between Orange Fixed and Orange Mobile. Due to the fact that Orange Mobile shares a number of facilities with Orange Fixed, they might have lower costs than a "hypothetical operator" due to economies of scope and hence will be able to generate profits from termination services for cross-subsidization.

TRC disagrees with Orange's fourth bullet point (the objective of Accounting Separation stated in the consultation 'to give transparency to the market participants' is not correct except to the extent, that this is a specific justified remedy to a specific market failure in a specific SMP market, which is not the case for the Jordan mobile call termination market). This is because Accounting Separation provides information and more information cannot imply less transparency. As stated above, accounting separation is a useful tool, also for Orange Mobile and the mobile call termination markets, e.g. because Orange can derive additional advantages over its competitors due to its relationship with Orange Fixed.

With regard to the last bullet point (the scope of accounting separation should be limited to SMP markets of a dominant operator), it should be understood that it is not possible to restrict Accounting Separation to regulated business activities, i.e. SMP markets. Only if Accounting Separation covers the enterprise as a whole it can be shown that there are no illegitimate cross-subsidies between regulated and non-regulated markets which is one of TRC's aims, otherwise the separated accounts shall have no value if for certain services. Article 8 point c) of the Instructions has been amended to clarify that the Dominant Licensees have to submit one set of Accounting Separation documents for each regulated market and one set of documents for all other business activities that are included in the statutory accounts. This allows a reconciliation of Accounting Separation information and information derived from the statutory accounts. However, the Instructions do not oblige Dominant Licensees to conduct Accounting Separation between different non-regulated markets, only between different regulated markets, and between regulated markets and all non-regulated activities as a whole. For example, a Licensee that has been found dominant and obliged to implement Accounting Separation on three relevant markets, would have to submit four sets of Accounting Separation Documents, one for each regulated market and one for the rest.

In conclusion, TRC generally maintains its position in this regard.

4 Accounting Separation Principles

In this chapter the principles are described, which have to be fulfilled when compiling the Accounting Separation records.

4.1 General Financial Reporting Principles

Consultation question II: Do you agree on these general financial reporting principles?

Zain agrees with the principles proposed by TRC.

Umniah/BTJ proposes the following principles:

- causality, objectivity and auditability,
- transparency, neutrality, sufficiency and no-compensation,
- consistency,
- disaggregate-ability and
- reconciliation.

Orange Fixed and Orange Mobile agree on the accounting separation principles of relevance, reliability, comparability and materiality. Further the two operators ask for the principle of proportionality, as to regard that the markets and operators in Jordan are relatively small and therefore costs per consumer are relatively high.

Orange Fixed and Orange Mobile clarified what they consider the term comparability to mean, i.e. that the information provided should be consistent over time and does not prohibit changes which are reasonable.

Orange Fixed commented on the consistency principle stating that the criteria used to value assets must be maintained annually to make the results comparable.

Orange Fixed and Orange Mobile also ask for an addition to the definition of materiality and states that the costs for accounting separation are high. This is also expressed by Zain in their comments on comments.

In their comments on comments Zain stated that they do not disagree with the principles mentioned by Umniah/BTJ, but that these do not add anything to the proposal of TRC.

TRC Response

With regard to the comments submitted by Umniah/BTJ, TRC would like to clarify that it has based its proposal on the Accounting Separation on international benchmarking[3] with countries in the Middle East and Europe. These are containing the principles of compliance, relevance, reliability, comparability and materiality. Further the information must be complete and traceable.

With regard to the principles mentioned by Umniah/BTJ, these and other necessary principles are covered in various places throughout the Accounting Separation Instructions:

- The issue of objectivity is covered in Article 4 (including point b 2) and Article 6.
- Transparency is covered e.g. in Article 7 with regard to transfer prices, Article 3 with respect to the aims and Article 4 (b) point 2 regarding reliability of the information presented. Transparency is also a part of the FPIA principle.
- Auditability is further covered in Article 9.
- The issue of causality is covered in Article 6.
- Consistency is covered in Article 4 (b) point 3.
- The issue that there should be no off-setting (the treatment of costs and revenues in cost accounting should keep both concepts separate with no offsetting between them) is covered in Article 6 and 7.

TRC clarifies that the principles to be regarded when providing the Accounting Separation are relevance, reliability, comparability, materiality, causality, objectivity, transparency, and

[3] See e.g. ERG Report, Regulatory Accounting in Practice 2009, October 2009, ERG (09)41; Oman, Resolution No 112/2009 Regulation on Accounting Separation, Regulatory Accounting & Reporting Requirements; Comreg, Decision No D08/10, Document 10/67 from 31 August 2010.

auditability and it shall be complete and traceable to the auditor and to TRC. Further the principle of no offsetting shall apply:

- The information is relevant if it has the ability to influence economic decisions and is provided in time to influence those decisions.
- The information is considered reliable when it represents faithfully what it purports to represent, it is free from deliberate or systematic bias, it is free from material error, it is complete, its basis of preparation is carried out in an objective (fair) way and it has a degree of caution (i.e. prudence) applied in exercising judgement and making the necessary estimates.
- The information is comparable when it is consistent over time in the way in which a Dominant Licensee prepares and reports financial information, under consideration that reasonable and justified improvements are made over time.
- The information is material when it is of relevant significance and importance of a particular matter in the context of the preparation, presentation and audit of financial information. A matter is material if its omission or misstatement might reasonably influence the regulatory decision and economic decisions.
- Causality: The assignment of costs and revenues to each activity, asset element or service should be made through the cost and revenue drivers.
- Objectivity: Generators of costs and revenues must be objective and quantifiable through sufficiently reliable statistical, census or sample calculations related directly or indirectly to the services and information procedures.
- Transparency: The cost attributed to each activity, asset element or service should be susceptible to being disaggregated into the various components of which it is formed.
- Auditability: The Accounting Separation shall establish adequate interrelations with the external financial accounting records of the operator and with the information and statistical systems on which the cost drivers for allocating costs and revenues to services are based in order to facilitate the auditability of cost accounting.

- No offsetting: The treatment of costs and revenues in cost accounting should keep both concepts separate with no offsetting between them. In particular, revenues obtained from the provision of services should be valued at the operator's catalogue prices, separating out in the accounts any bonuses, discounts or price reductions of a commercial nature.

These general principles have been identified by benchmarking with other countries[4] and are regarded as rational.

Orange Fixed and Orange Mobile agree on the accounting separation principles of relevance, reliability, comparability and materiality.[5] Further the two operators ask for the principle of proportionality, as to regard that the markets and operators in Jordan are relatively small and therefore costs per consumer is relatively high. TRC regards the proposal of Orange Fixed and Orange Mobile regarding the principle of proportionality as a general principle, and not as specific of regulatory accounting, and so it is not necessary for TRC to introduce it as part of the Accounting Separation instructions. Further proportionality in itself cannot be a principle for the Licensee as this would imply that the Dominant Licensee is allowed to prepare insufficient Accounting Separation Information referring to the proportionality principle. Further, international best practice does not show that proportionality is a viable principle in the Accounting Separation instructions.

Regarding the term comparability raised by Orange Fixed and Orange Mobile, TRC regards it to be reasonable as it only provides a clarification of what is already implicitly included in the Accounting Separation Instructions. Hence, TRC alters the definition of comparable to "The term comparability implies a consistency over time in the way in which a Dominant Licensee prepares and reports financial information, under consideration that reasonable and justified improvements are made over time." Furthermore, changes in criteria will be allowed if they prove causality in cost/revenues allocation. Obliged operators should submit the re-

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[4] These general principles have been identified by benchmarking with other countries; Confer e.g. EU Recommendation on accounting separation and cost accounting systems und the regulatory framework for electronic communications, 2005/698/EC, Section 2; OFCOM, The regulatory financial reporting obligations on BT and Kingston communications in markets where SMP has been demonstrated – Accounting separation and cost accounting: Final notification and explanatory statement, 10 May 2004; Oman, Resolution No 112/2009 Regulation on Accounting Separation, Regulatory Accounting & Reporting Requirement; ERG Report, Regulatory Accounting in Practice 2009, October 2009, ERG (09)41, p. 30ff

[5] This principle is also included in other countries. Please refer to Footnote 4.

sults with the previous criteria and the new criteria (with significant impact), so as to allow TRC to assess the materiality and take this information into account when making its decision, and make an adjustment in the cost/revenue affected if needed.

Regarding the comment of Orange Fixed on the consistency principle, TRC would like to clarify that this is covered by the Accounting Separation Instructions in Article 4(b).

Orange Fixed and Orange Mobile asked for an addition to the definition of materiality. TRC has added this and states that the term materiality means that "the information is material when it is of relevant significance and importance of a particular matter in the context of the preparation, presentation and audit of financial information. A matter is material if its omission or misstatement might reasonably influence the regulatory decision and economic decisions or interpretations of interested parties." Such a reasonable influence will vary and the ERG states that "it is therefore not capable of general mathematical definition but is reliant upon qualitative judgements and estimates",[6] and therefore a specific value is not explicitly mentioned in most other countries.[7] The reason for the criterion of materiality is that it safeguards that the results are reliable and valid for regulatory and commercial decisions. A matter is material if its omission or misstatement would reasonably influence the economic decisions or interpretations of users. The materiality thresholds are taken into account when a regulatory authority uses the information for compliance purposes. For instance, a transfer charge showing non-discrimination may need to be calculated in a very precise and accurate way but a general cost-orientation obligation could be examined with broader materiality thresholds.

In conclusion, TRC generally maintains its position in this regard and has added further principles as proposed by the stakeholders.

[6] ERG Common Position (ERG(05)29), p. 31.

[7] E.g. the Irish Regulator COMREG has come to the conclusion that at threshold is impractical (see: COMREG, Decision D08/10, August 2010, p. 72, URL: http://www.comreg.ie/_fileupload/publications/ComReg1067.pdf); The threshold of 2 % is used by the Spanish regulator; The regulatory authority OFWAT in UK is using a threshold of 1% (OFWAT, Regulatory Accounting Guide 3.06, February 2007, p. 23).

4.2 Cost Standard (LRIC vs. FAC)

Consultation question III: Do you agree that these are the cost standards that should be required?

With regard to the use of FAC and/or LRIC, the following issues were addressed by the stakeholders:

- Zain states that they are not obliged to provide LRIC cost modelling under the current regime because the LRIC cost model is provided by TRC. Hence, the introduction of LRIC means that the regulatory burden is increased.

- Zain further states that Accounting Separation should either be based on FAC or LRIC, but not both, as this implies additional burden on the Dominant Licensees.

- Zain also states that the same cost standard should be used over all business activities in order to show that there are no anti-competitive cross-subsidies between regulated and non-regulated business activities.

- Zain also asks about the definition of the "enterprise as a whole", which is a definition included in the Instructions.

- Zain raised the question how to monitor non-dominant operators which are not obliged to accounting separation to ensure that there is no price discrimination. The issue was raised based on the phrase in the public consultation which states: "Dominant Licensees, which have been obliged to charge cost oriented prices based on LRIC shall prepare two versions of profit and loss statements and mean capital employed statements". Thereby the question especially refers to Umniah and other interconnection service providers to submit separate account because they are subject to cost orientation remedy.

- Umniah/BTJ believes that TRC should consider the following issues when deciding which cost standard to be used: the proportion of joint and common cost must be allocated according to the causality principle. It should, according to Umniah/BTJ, be kept in mind that the main limitation of FAC cost standard is the subjectivity associated to the allocation of un-attributable costs, and therefore the same cost standard should be used over all business activities to show that there are no anti-competitive cross-subsidies between regulated and non-regulated business activities.

- Zain has commented in their comments on comments that this limitation applies to LRIC as well as to FAC.

- Orange Fixed and Orange Mobile agree with the use of fully allocated costs as FAC is the appropriate cost concept to be applied in accounting separation being reconcilable to statutory accounts and more easily understood than other cost concepts. Further they disagree with the use of LRIC for certain markets due to the costs, difficulties regarding reconciliation, potential for confusion in case of parallel accounts of FAC and LRIC. They are also questioning what TRC will achieve by imposing both cost standards.

TRC Response

According international best practice and the comments made by the stakeholders, FAC is the preferred cost standard. When it comes to the option of having accounting separation based on LRIC as well, TRC is of the opinion that there are pros of having this in special cases, especially as it will provide TRC with useful information when approving tariffs based on LRIC as a cost standard. Hence, TRC is convinced that there might be situations when Accounting Separation based on LRIC is needed in order to approve tariffs. Examples of such situations are when the differences in costs between the FAC cost accounting and the cost modelling based on LRIC are significant without any reasonable explanation. Hence, there are benefits from having LRIC in certain cases but as the implementation of LRIC separated accounts requires considerable effort from the regulated operator, a cost-benefit consideration shows that while FAC implies less effort and can be implemented for all services, LRIC is only proportionate in certain cases. In these cases, TRC will additionally in writing require the regulated operator to provide the Accounting Separation based on LRIC as well as FAC.

I.e. to strike a balance between the interests of the stakeholders and TRC, TRC has revised the Accounting Separation Instructions in a way that FAC is required on an annual basis, but TRC is given the right, in exceptional cases only, to request Accounting Separation based on LRIC on an ad-hoc basis if this is regarded as necessary and proportionate. Article 5 of the

Instructions has been amended accordingly and the possibility to require Dominant Licensees to provide Accounting Separation based on LRIC has been moved to article 10 points b) and c).

Using FAC as the cost standard for the annual provision of Accounting Separation is consistent with international best practice. The European Commission's Recommendation can be understood as favouring FAC, which "may" be complemented by the LRIC valuation of assets where appropriate.[8] Further, FAC is the most common standard in the countries that have been benchmarked.[9]

With regard to Umniah/BTJ's comment that if FAC is used, one must keep in mind the limitations of un-attributable costs, TRC comes to the same conclusion as Zain has commented in their comments on comments, i.e. that this limitation applies to LRIC as well as to FAC. The reason is that the problem of un-attributable costs has nothing to do with the cost standard but is a problem which exists to Accounting Separation as such, because Accounting Separation per definition derives from the statutory accounts. In order to address this issue, ABC has been invented and this is also foreseen in the Accounting Separation Instructions. Further, with regard to the concerns of Umniah/BTJ that the costs will not be correctly attributed, TRC would like to point out that the Accounting Separation Instructions contains safeguards which makes the attribution of costs more accurate; including the requirement for an audit, the requirement regarding documentation, the demonstration of transfer charges as well as the principles used for the provision of the Accounting Separation.

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[8] European Commission Recommendation of 19 September 2005 on Accounting Separation and Cost Accounting Systems under the Regulatory Framework for Electronic Communications (2005/698/EC), Article 3 does not explicitly refer to the choice of the cost standard, but to the choice of the cost base. According to the Commission, the cost base should be current cost accounting (CCA) and based on modern equivalent assets (MEA). In regulatory practice, this cost base is typically used with either FAC or LRIC as cost standard. The Commission Recommendation can therefore be understood as recommending at least FAC, complemented by LRIC where this is appropriate.

[9] FAC is imposed in Ireland (Comreg, Decision No D08/10, Document 10/67 from 31 August 2010), Australia, Australian Competition and Consumer Commission, Current Cost Accounting Record Keeping and Reporting Rules, September 2004, UK, OFCOM, The regulatory financial reporting obligations on BT and Kingston communications in markets where SMP has been demonstrated – Accounting separation and cost accounting: Final notification and explanatory statement, 10 May 2004, p. 31; Oman, Resolution No 112/2009 Regulation on Accounting Separation, Regulatory Accounting & Reporting Requirements, Article 12; Saudi Arabia according to the Public consultation on Framework and Guidelines for Accounting Separation from 23 June 2010 (proposed).

When it comes to the Umniah/BTJ statement that accounting separation should comprise all business activities of a regulated operator and that it is necessary to have the same cost standard over all business activities, this is also proposed by TRC and already foreseen in the Accounting Separation Instructions. Hence, no changes to the Instructions are necessary.

As stated above, Zain asks about the definition of the “enterprise as a whole”. In order to clarify this, TRC changes the text of the Instructions to “all business units of the Dominant Licensee, which are presented in the same statutory accounts, including markets in which the Licensee has been designated as Dominant and markets where the Licensee has not been designated as Dominant. The reason for this clarification is that the Dominant Licensees are parts of international enterprises, while the accounting separation is only relevant for the Jordan markets also TRC defines the geographic market as inside Jordan.

With regard to Zain’s question about how to monitor non-dominant operators which are not obliged to accounting separation to ensure that it is not price-discriminating, this issue concerns the market review decision and not the Accounting Separation Instructions. Within the market reviews, TRC has found that accounting separation as an obligation is not proportionate to Umniah. One reason is that Uminah has less possibility to affect the market through any practices with the lack of transparency.

In conclusion, after considering stakeholders comments TRC will use FAC cost standards on a regular basis for all activities of dominant licensees and reserve the right to use LRIC on ad-hoc basis.

4.3 Cost Base (HCA vs. CCA)

Consultation question IV: Do you agree that CCA and MEA is the appropriate valuation method of assets for accounts based on FAC?

With regard to the question IV, i.e. to use CCA or HCA, the following was stated:

- Orange Fixed and Orange Mobile agree that CCA/MEA valuation should be required for separate accounts.

- Zain states that they think it is more appropriate to base accounting separation on HCA as this reduces the regulatory burden and leads to lower prices, which is advantageous for the consumers. This view is also shared by Umniah/BTJ with regard to the Accounting Separation for Orange Fixed. Zain is concerned that resting accounts according to CCA and MEA will incurred an extra cost and that the use of CCA could have the adverse effect of raising fixed cost and therefore the prices.

- Umniah/BTJ states that a mix of valuation methods can be used, including HCA, Indexation, Absolute Valuation and MEA. According to them HCA can be used if the asset has low value or is recently built as well as for ducts and copper cables, while MEA can be used for elements which are going to be replaced.

- With regard to the additional valuation methods additional to MEA, Zain has expressed its concerns with several methods because accepting different valuation methodologies would only cause regulatory uncertainty with "hours of argument spread over several months (or longer) as the appropriate methodology is debated and disputed".

TRC Response

With respect to the use of CCA, TRC regards it to be necessary in order to be able to derive sufficient information from the accounting separation and additionally it can be referred to as best practice.

- The requirement to only provide Accounting Separation based on HCA would have a set of negative consequences. One is that in case HCA is used, the results of the Accounting Separation will change from year to year depending on where the Dominant Licensee is in the investment cycle, e.g. when networks are not upgraded for a number of years but then upgraded to a significant extent in a specific year, the cost would fluctuate from year to year, making the results unreliable.

- Current cost accounting is recommended by the European Regulators Group (ERG, now BEREC) and the European Commission. Within the EU, both HCA and CCA are used, though ERG states that there is a trend towards CCA, particularly in the mobile markets.[10]

- Current cost accounting was originally developed to remedy the limitations of historical cost accounting in a world of changing prices due to inflation and rapid technological change. According to ERG, the main regulatory impact is that it requires the operator to record the value of assets to reflect their "value of the business" which, by implication, should result in a net asset cost base and measures of profits similar to that expected under fully competitive market conditions.[11]

Hence, although CCA implies extra effort, as stated by Zain, it is proportionate due to the benefits and because it is widely used elsewhere.

The second question, which was raised by Umniah/BTJ is the use of other methods than MEA. In fact using indexation or absolute valuation as well as book values does lead to similar or even identical results as MEA in certain cases. If well defined, the alternative valuation methods might imply more transparency as they are easier to implement. Further, different valuation methods are more suitable for specific kinds of assets than others, so the usual solution is use a range of methods to revaluate the assets:

- Absolute valuation is suitable for assets which prices are changing but that experience little changes in technology as long as the prices are officially available or can be proven by invoices. This is especially the case where the assets or part of the assets have been renewed recently.

- Indexation is also suitable for assets which prices are changing but experience little changes in technology when in the same cases a good index is available. This is especially true for buildings, network sites, civil works, safety/energy/air conditioning appliances and in general antenna infrastructure.

[10] ERG Report, Regulatory Accounting in Practice 2009, October 2009, ERG (09)41
[11] ERG Common Position: Guidelines for implementing the Commission Recommendation C (2005) 3480 on Accounting separation & cost accounting Systems under the regulatory framework for electronic communications, ERG (05)29

- For assets which experience extensive changes to technology, i.e. assets that became obsolete, MEA is the most suitable method.

- Book Value (Historic) for immaterial, short life-span and for not-regulated assets.

With regard to the concern as stated by Zain, i.e. that the use of different valuation methods in case of CCA will lead to long regulatory discussions, it is important that the valuation is clearly defined in the model in order to avoid regulatory uncertainty. Therefore it is necessary to define the valuation method for the different assets. TRC has made it clear above when to use which valuation.

Zain raised the issue of HCA as the basis for the preparation of accounting separation. TRC agrees and regards it necessary for the regulated operator(s) to provide the HCA accounts as well. Preparing both HCA and CCA does not imply extensive additional effort as the valuation of assets based on HCA is already conducted when the statutory accounts are compiled. Besides, Orange Fixed has already submitted HCA documents when FAC was the cost standard in the past. Further, as there is an additional value derived from Accounting Separation based on HCA because this makes the submission more auditable, the HCA is required as well.

Conclusion: TRC considers stakeholder comments with regard to valuation method where the dominant licensees may use different types of valuation methods depending on the type of assets and providing profit and loss statements and mean capital employed statements based on both Current Costs Accounting (CCA) and History Cost Accounting (HCA).

4.4 The Capital Maintenance Concept

Consultation question V: Do you agree that FCM is the right capital maintenance concept for Accounting Separation in Jordan?

Orange Fixed, Orange Mobile, Zain and Umniah/BTJ accept the FCM method.

TRC Response

TRC has decided to maintain its position to use this concept as in the Accounting Separation Instructions.

Consultation question VI: Do you agree on the adjustments to be made under FCM?

Umniah/BTJ clarifies that they see the differences between OCM and FCM refers to the treatment terms of profit and loss. For FCM further adjustments are taken into account with regard to holding gains or losses that arise due to the effect of asset specific price changes on current cost value of assets and the effect of general inflation on shareholders fund.

Orange Fixed and Orange Mobile agree with the proposal of TRC and ask for a clarification of the needed adjustments. Also Zain asks for clarification on the adjustments to be made and asks if there is a difference to the CCA method.

TRC Response

Based on these comments, TRC maintains its proposal. With regard to Zain’s question for clarification, FCM and OCM are two ways to implement CCA and it further defines how to value the assets, differing from the book value as used for HCA assessments. The main difference is that if FCM is applied, holding gains and holding losses adjustments are made, which is not the case if OFM is applied. With regard to a clarification of FCM, the steps to account for are included in the Accounting Separation Instructions, Article (5) c) 3.

5 Cost Causality / Attribution of Costs

This section deals with the way costs, capital employed and revenues are attributed to the different accounting units in the regulatory accounting.

5.1 Cost and Revenue Causality

Consultation question VII: Do you agree that Activity Based Costing should be prescribed as the methodology to be used to attribute costs?

Umniah/BTJ supports the proposal to use ABC. Zain states that ABC is international best practice but expresses concerns that ABC requires more information on allocation of indirect costs than the method used in for example a LRIC model. Therefore more information on the use of personal and resources will be needed to allocate costs based on activity so the information gathering process on the use of resources within the company will be substantially increased. In the light of this, Zain asks if it is proportionate to have this requirement for mobile operators in Jordan.

Orange Fixed and Orange Mobile agree that Activity Based Costing (ABC) provides a logical mechanism for cost allocation. They further propose a clarification that "All costs, assets and liabilities should be allocated to separate markets (revenues can be directly associated to markets). Allocations should be on a causal and reasonable basis drawing on ABC principles. Fixed common and joint costs should also be allocated."

TRC Response

TRC would like to clarify that no other method has been proposed for the allocation of joint and common costs which distributes the costs according to the actual usage of these resources related to the statutory accounts. Further, TRC regards ABC to be proportionate, not only because ABC is international best practice, but also because it is regarded to be a widely accepted and implemented method in the industry. When ABC is implemented, this does not only provide the necessary information for regulatory purposes, but also has the potential to support decision making by the regulated operator.

With regard to the proportionality for mobile operators to implement ABC, TRC regards this to be the case as telecommunications operations are characterised by a significant proportion of common and joint costs. Further, Orange Mobile shares resources with Orange Fixed and therefore ABC is required as a tool to separate these costs. Regarding Zain, this Licensee has been designated as dominant in both the termination as well as in the MACO market and in order to apply separation of joint and common costs, it is necessary to implement ABC, i.e. the benefits of ABC exceeds the additional costs of Zain and Orange Mobile.

With regard to Orange Fixed and Orange Mobile proposal to clarify that "All costs, assets and liabilities should be allocated to separate markets (revenues can be directly associated to markets). Allocations should be on a causal and reasonable basis drawing on ABC principles. Fixed common and joint costs should also be allocated" TRC would like to state that these issues are already covered by Article 6 of the draft Instructions. The proposal made by Orange Mobile and Orange Fixed does not change the outcome of the instructions but as they provide a clarification, the Accounting Separation Instructions are adjusted accordingly.

<u>Conclusion: based on the comments of the operators, TRC maintains its positions to adopt ABC to be used for Accounting Separation and inserts the clarification proposed by Orange.</u>

5.2 Transfer Charges

Consultation question VIII: Do you agree with these requirements for the determination of transfer charges?

Zain states that they regard this specification appropriate for fixed markets but that they are excessive for the mobile termination market.

Umniah/BTJ thinks that the transfer prices should be disclosed in order to be able to compare the charge of internal service to the price of external service (i.e. to be able to assess if there is any discrimination). This issue is covered with regard to question XVI below and not responded to in this section.

Orange Fixed and Orange Mobile state that they agree to the requirements 1, 2, 4, 5, 8 and 9 in Article 7 of the proposed Instructions but disagree with point 3, 6 and 7. With regard to point 3, Orange proposes the amendment "but subject to changes and improvements that may become necessary from time to time."

With regard to point 6 and 7, Orange proposes to clarify these points by redefining point 6 to "The charge for internal usage shall be equivalent to the charge that would be levied if the product or service were sold externally rather than internally' under a condition that the routing factor (network elements usage and frequency of network element usage) is the same for both upstream and downstream services." and point 7 to "In cases where wholesale services are not currently on offer (i.e. no wholesale tariffs exist) the transfer charges for the network part of retail services shall be calculated on the same basis and methodology, and using the same network element costs, as the wholesale services."

With regard to the overall definition, Orange Fixed states that this is not clear enough and states that "transfer charges, in the context of accounting separation, to relate to national sale of regulated products between upstream and downstream separated markets where applicable and defined as part of the accounting separation framework."

TRC Response

With regard to Zain's statement that they regard this specification to be excessive for the mobile termination market, TRC would like to clarify that transfer prices are an integral part in Accounting Separation. Transfer charges relate to transactions that flow between disaggregated entities, markets and services of a vertically integrated Licensee. A well-defined, transparent and verifiable transfer charging system is necessary to demonstrate non-discrimination and to calculate internal costs and revenues for both cost-orientation and non-discrimination purposes. The transfer charges reflect the vertically integrated nature of the Licensee and will enumerate the wholesale/retail relationships between the economic markets and services within the undertaking's scope of activity. When it comes to the effort required to determine the transfer charges, the requirement for services with tariffs approved by TRC based on cost orientation is low, as the regulatory approved charges can be used as transfer prices. Therefore the assessment needed for transfer prices for mobile termination, for instance, is less resource intensive.

With regard to Orange Fixed and Orange Mobile proposal to amendment the number three of Article 7, TRC regards the clarification made by orange to be valid in order to deal with changes over time. This amendment is only containing a clarification and does not change the content of the Accounting Separation Instructions, and hence, the clarification is added to the TRC proposal.

With regard to the amendment proposed by Orange when it comes to point 6 and 7, TRC's response is that this proposal is a clarification which narrows down the principle for the transfer charges to mainly consider the routing factors. Firstly, routing factors refer to "routing" and hence, are only valid for transmission services such as voice, but not dedicated capacity of local loop unbundling. Secondly, the definition proposed by TRC focuses on the very crucial point, namely that there should be no discrimination between internal and external provisioning. Therefore, TRC sees no reason to change the proposed Instructions in this regard as it would imply a too narrow definition.

With regard to the overall definition addressed by Orange, their definition is consistent and covered by the proposed Instructions with the difference, that the proposal of Orange Fixed is including the focus on vertically integrated value chains.

<u>In conclusion, TRC therefore maintains its position with a clarification of Article 7, point 3.</u>

6 Documentation and Separated Accounts

In this section the documentation and reporting formats are described and discussed.

6.1 Required Documentation

Consultation question IX: Do you agree that this information is relevant and sufficient for the Accounting Separation?

Zain does not object to the specifications but asks for a justification of the obligation to provide the information required, with respect to mobile networks. Zain has concerns that the mobile network structure is different from the fixed network structure because the mobile network operators are independent of each other and do not rely on dominant firms in the access networks. Zain also asked TRC to clarify how this information can be provided in the context of mobile termination in the way that adds any value to the LRIC model developed by TRC, i.e. Zain questions the practical difference between separated accounts for mobile termination and LRIC cost model for termination.

Zain needs further explanation to the point of consolidation of P&L and MCE.

Orange Fixed and Orange Mobile agree that the proposed content set out in the consultation document appears reasonable. Orange Fixed and Orange Mobile ask for standardized forms and formats for the Accounting Separation. This issue was also mentioned by Zain in their comments on comments. Regarding the response of TRC, this is elaborated in section 9 with regard to question XVIII. Please refer to this section for further discussion.

Umniah/BTJ disagree with TRC and asks for the following documents to be provided:

- Audited separated regulatory accounts
- Accounting documents
- Detailed Attribution Methodology

In their comments on comments Zain disagrees with these additional documents and states that more requirements on the documentation would only increase the regulatory burden and hence the costs.

The Orange companies also ask for clarifications on four points:

- With regard to the Audit trail, the stakeholders would like to clarify that this is included in the schedules that contain the calculation of the various allocation drivers and the documentation of the assumptions and data sources used and the cost model.

- With regard to “other supplementary schedules, as required”, Orange Fixed and Orange Mobile ask TRC to specify and discuss all additional supplementary schedules with the Dominant Licensees before imposing the requirements to confirm that the data is available and the effort to prepare these schedules is proportionate.

- Orange Mobile and Orange Fixed state with regard to the “right to require Dominant Licensee(s) and the auditor to answer questions... or to prepare additional supporting documents...”, that a formal right to question the auditor will require a tripartite agreement for the audit.

- Orange mentions that with respect to “reconciliation with statutory accounts or other source of costing information” the consolidation of profit and loss statement and mean capital employed for all markets will be compared to the statutory accounts and not to other costing information. Orange states that if the regulator has another view, the costing information should be defined as part of this Consultation.

TRC Response

Zain asks for a justification of the obligation to provide the information required with respect to mobile networks and their concern that the mobile network structure is different from the fixed network structure as well as the issue on how the information can be provided in the context of mobile termination in the way that adds any value to the LRIC model developed by TRC. TRC would like to emphasize that the reason the information has to be provided for mobile networks as well as for fixed networks is that the Accounting Separation information demonstrates the actual costs (based on CCA) in addition to the LRIC model which determines the cost of a hypothetical network operator. The former addresses the actual costs which are relevant for the competition problems of cross-subsidization. Further, Zain is dominant in more than one market, including the MACO market, which makes the situation in Jordan different from the situation abroad. As this implies more competition problems, including the issue of operators reliant on the wholesale access offers in the MACO market, cross-subsidization might be a serious issue in the Jordan mobile markets.

With regard to Zain’s question referring to the practical difference between separated accounts for mobile termination and LRIC cost model for termination, TRC would like to clarify that the information provided is based on different cost standards (LRIC vs. FAC) and they address different competition problems (i.e. excessive tariffs within the termination markets regarding the cost models and cross-subsidization between different services in case of the accounting separation).

The answer to Zain’s question for further explanation to the point of consolidation of P&L and MCE is that the consolidation of accounts refers to the aggregation of the different separated accounts in order to provide the sum of all the separated accounts to be compared to the statutory accounts. This is the same type of consolidation as a holding company does for its subsidiaries within the statutory accounts.

Comparing the documents referred to by Umniah/BTJ, TRC comes to the conclusion that the content required by Umniah/BTJ is covered by the proposal of TRC, i.e. audited separate accounts and accounting documents are covered in Article 8 (a) 1 and in Article 9 and the detailed attribution methodology is covered in Article 8 (a) 3. Yet TRC will add the following required documentations which are not limited to but include: statutory accounts of the relevant accounting year, routing factors table and a Fixed Asset Registry (assets in use, not in use, valuation, annual and accumulated depreciation, definition on the network elements, etc.). In addition, it is clarified that a Detailed Attribution Methodologies document is required.

With regard to the Audit trail, TRC does not agree with Orange on this point, because the Audit trail is there to demonstrate how the results of the Accounting Separation have been derived from the statutory accounts. The Audit trail is very helpful for the auditor as well as TRC approving the Accounting Separation Information submitted by the Dominant Licensee in order to safeguard that there are no errors in the Accounting Separation information submitted. It is necessary that the Audit trail shows the traceability as Orange states. Hence, a change of the TRC proposal is not necessary.

With regard to the issue on “Other supplementary schedules, as required“, which was raised by Orange Fixed and Orange Mobile, TRC would like to inform that these supplementary supporting documents might be required ad-hoc and cannot be specified in the Accounting

Separation Instructions because such documents will be required as a reaction on the Accounting Separation information provided by the Dominant Licensee. Hence, a change to the TRC proposal is not appropriate with this regard.

Another issue raised by Orange Mobile and Orange Fixed referred to the formal right to question the auditor will require a tripartite agreement for the audit. TRC does not agree as this might only be an issue for the contractual agreements between the Dominant Licensee and the Auditor without any involvement of TRC. TRC will post the questions it has to the auditor by directing these to the Dominant Licensee. Requiring the Auditor to answer questions about his Audit is proportionate in cases where question marks exist about the work of the Auditor, in order to clarify if the work performed is reliable and professional. In addition, TRC reserves the right to appoint its own Auditor (please refer to Article 9 b) of the decision.

With regard to Orange's question on the reconciliation with other source of information, TRC would like to clarify that the reconciliation with the statutory accounts are the most important reconciliation and if no other source of information is used, it is enough to provide this reconciliation.

<u>Conclusion: TRC maintains its view in this respect and has added more specifications on the documents as set out in the instructions.</u>

6.2 Level of Details for Accounting Documents

Consultation question X: Do you agree with this level of details, i.e. that the Accounting Separation should regard the markets and not business units or services and products?

Orange Fixed, Orange Mobile and Zain agree to the proposal of TRC to prove the separation for the different markets. Orange Fixed and Orange Mobile state that Accounting Separation can only be provided in markets where SMP has been designated.

Umniah/BTJ states that the Accounting Separation should include all products and services provided by designated licensee and not only those regulated. In their comments on comments, Zain states that they find the comment submitted by Umniah/BTJ somewhat confused, and that markets are regulated in Jordan and hence, these are the appropriate level of detail.

Orange Fixed and Orange Mobile state that information should not be published which is not related to markets with SMP. This issue is dealt with in question XVI.

Orange Mobile states that they think the Accounting Separation for mobile markets is not required, but this is an issue for the market review procedures and not this consultation, as already explained above.

TRC Response

As included in the TRC response regarding question I above, the text of Article 8 point (c) of the Instructions has been amended to clarify that Accounting Separation should be prepared for each of the markets in which the Dominant Licensee has been obliged to and additionally he should also prepare Accounting Separation including the total of all remaining business activities. One of the main objectives to introduce Accounting Separation is to demonstrate that there are no illegitimate cross-subsidies between regulated and non-regulated business activities. The Accounting Separation must therefore include all the activities of the Dominant Licensee as a whole. Otherwise the Accounting Separation would not demonstrate if cross-subsidization is taking place, but only the profitability of the regulated operator in certain regulated markets. The amended text also ensures reconciliation between Accounting Separation data and data retrieved from the statutory accounts.

7 Administrative Issues

In this section, the processes around Accounting Separation are dealt with.

7.1 Scope of the Audit

Consultation question XI: Do you agree that the auditor should generally be proposed by the Dominant Licensee and approved by TRC, and that TRC should have the possibility to appoint another independent auditor in exceptional cases?

Zain agrees with the proposal and Umniah/BTJ agrees as well, but states also that TRC should be able to appoint its own auditor.

Orange Mobile and Orange Fixed disagree that there should be an audit of the Accounting Separation as they state that TRC is in the position to carry out this task in itself at a much lower cost. If there is an audit, Orange does not agree that TRC should have the possibility to appoint the Auditor.

TRC Response

TRC would like to point out that the regulatory accounting needs to be audited by an independent auditor just as the financial accounting must be audited as well. International experiences show that an Audit is required, e.g. the European Commission recommends that the accounting separation statements should be subject to an independent audit opinion or a national regulatory authority compliance audit (subject to the availability of suitable qualified staff).[12] In several countries, e.g. Oman and the UK the regulated operator appoints the auditor.[13] This has the advantage, that the regulated operator can appoint the same auditor as for the financial accounting, which in turn reduces the costs for the regulated operator. Further, the auditor for the financial accounting has access to all relevant information and is familiar with the accounting of the regulated operator.

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[12] Commission Recommendation of 19 September 2005 on Accounting Separation and Cost Accounting Systems under the Regulatory Framework for Electronic Communications (2005/698/EC), Article 4.

[13] Oman, Resolution No 112/2009 Regulation on Accounting Separation, Regulatory Accounting & Reporting Requirements, Article 11; UK, OFCOM, The regulatory financial reporting obligations on BT and Kingston communications in markets where SMP has been demonstrated – Accounting separation and cost accounting: Final notification and explanatory statement, 10 May 2004, p. 53.

There is a risk that the independent auditor is not as independent as appropriate. In this case, it is important that TRC has the possibility in cooperation with the Dominant Licensee or on its own to appoint the independent auditor. This is in line with the ERG recommendation and the rules imposed in the UK.[14]

According to the decision, TRC has the right to appoint another auditor than the one chosen by the Dominant Licensee, if it has justified doubts about the auditor's independence or qualification, i.e., that is the auditor does not fulfil the standards required for auditing the statutory accounts. In this case, a second audit is required to be conducted by the auditor appointed by TRC. Further, for the first time accounting separation is submitted, TRC has the right to appoint a second auditor. This procedure does partly regard the concerns of the two Orange companies that it is better if the Dominant Licensee appoints the Auditor, as this is foreseen to be the standard case.

Umniah/BTJ would like TRC to have the right to have a second auditor. TRC intends to hire an independent auditor for the first round of approvals of accounting separation. Also for subsequent submissions, in case the auditor of the Dominant Licensee does not provide a sufficient Audit or if further assessment is needed, TRC will also appoint its own auditor.

<u>*Conclusion: TRC maintains its position and clarifies that it will hire an auditor for the first round of approvals and has the right to do so for later submissions as well.*</u>

Consultation question XII: Do you agree that the audit should be performed based on FPIA ("fairly presents in according with")?

Zain and Umniah/BTJ agree, while Orange Fixed and Orange Mobile disagree and propose that the Audit should be made according to e.g. PPIA ("properly prepared in accordance with") as the FPIA implies higher costs.

[14] ERG Common Position: Guidelines for implementing the Commission Recommendation C (2005) 3480 on Accounting Separation & Cost Accounting Systems under the regulatory framework for electronic communications, ERG (05)29, p. 38, UK, OFCOM, The regulatory financial reporting obligations on BT and Kingston communications in markets where SMP has been demonstrated – Accounting separation and cost accounting: Final notification and explanatory statement, 10 May 2004, p. 53.

TRC Response

According to international experiences and the view of Umniah/BTJ and Zain, FPIA is an appropriate requirement. In e.g. Oman, Ireland and UK it is stated that the audit should be fairly presented, which TRC regards as best practice.[15] OFCOM in UK summarises this issue as follows:[16]

> *"The FPIA audit opinion provides a high level of assurance and, in the context of regulatory financial reporting, is broadly equivalent to the "true and fair" opinion seen in statutory financial statements. It is a level of opinion therefore that is more appropriate to use at corporate or trading entity level and is therefore being proposed as the appropriate opinion for regulatory financial information for the defined SMP markets."*

Hence, FPIA should be stated in the Accounting Separation Instructions.

Consultation question XIII: Do you agree with the elements stated above to be covered by the audit?

Zain agrees while Orange Fixed and Orange Mobile disagree with any requirement for Separated Accounts disclosures including LRIC assessments and cover cost volume relationships.

Umniah/BTJ states that they regard the audit and the audit report to have a high value for the quality, objectivity and credibility and it increases the confidence of the stakeholders in the results presented. They further state that the audit report should clearly set out the respective responsibilities of the auditor and the dominant License and the basis on which the audit has been carried out.

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[15] Oman, Resolution No 112/2009 Regulation on Accounting Separation, Regulatory Accounting & Reporting Requirements, Article 11; Comreg, Decision No D08/10, Document 10/67 from 31 August 2010, p. 43; OFCOM, The regulatory financial reporting obligations on BT and Kingston communications in markets where SMP has been demonstrated – Accounting separation and cost accounting: Final notification and explanatory statement, 10 May 2004, p. 56.

[16] OFCOM, The regulatory financial reporting obligations on BT and Kingston communications in markets where SMP has been demonstrated – Accounting separation and cost accounting: Final notification and explanatory statement, 10 May 2004 , p. 56.

TRC Response

When it comes to the elements covered by the audit, the ERG states in its recommendation the elements to be covered as follows:[17]

> *"The main elements to be covered by the audit are the following: a) the scope of costs included in the model and the scope of costs allocated to individual regulated products (where appropriate); b) the reconciliation between the cost model and statutory accounts; c) correctness of figures, including operational data: volumes, technological parameters; d) methodologies used regarding amortization, cost capitalization, allocation and for the evaluation of the assets (e.g. current costs); e) transfer charges in separated accounts; f) reconciliation between the cost model and the separated accounts; g) Cost Volume Relationship and accounting system information. "*

Further, cost volume relationships are also mentioned in the ITU's "ict regulation toolkit". In both cases, auditing cost volume relationships are mainly referring to situations where LRIC is used as a cost base or the audit is targeting top-down cost models. As the Accounting Separation are prescribing FAC as the standard to be used except for ad hoc cases, the auditing of cost volume relationships should only then be prescribed, when these are required and proportionate. Hence, in case the CVRs are used, these must be presented to and approved by the Auditor.

TRC agrees with the comment made by Umniah/BTJ that the audit is important. With regard to the responsibilities, these are clearly set out in the Accounting Separation Instructions, including the elements to be covered by the audit.

With regard to the disclosure of information, this is dealt with in question XVI.

<u>In conclusion, TRC maintains its view about the elements covered by the audit.</u>

[17] ERG Common Position: Guidelines for implementing the Commission Recommendation C (2005) 3480 on Accounting Separation & Cost Accounting Systems under the regulatory framework for electronic communications, ERG (05)29, p. 38.

7.2 Time Frame and Approval Procedure

Consultation question XIV: Do you agree that the Accounting Separation documentation must be provided annually within three months after the end of the period to which it relates?

Umniah/BTJ agrees to the proposal of TRC that the Accounting Separation documentation must be provided annually within three months”. In the comments on comments, the TRC expressed its disagreement with Zain that more time (18 Months) is needed for the first provision of accounting separation.

Zain agrees that the accounting separation should be delivered annually, but asks for more time as it will need resources for building capable systems that comply with the needed requirement as the Irish example 6 month after the end of the accounting period. In their comments on comments, Zain expresses its disagreement with the submission of Umniah/BTJ.

Similarly, Orange Fixed and Orange Mobile agree that the information should be prepared annually, but ask for 6 months from the time when the statutory accounts are finalised. Orange Fixed and Orange Mobile also request additional 6 months for the first time for FAC accounts and 12 months in case LRIC is required.

TRC Response

All operators but Umniah/BTJ request more time. Internationally, the time frame for providing the Accounting Separation is typically longer than the proposed 3 months. In Ireland it is stated that the information should be provided within six months after the reporting period has ended. The same time frame applies in Oman.[18] TRC therefore decides on the time frame in the Instructions to be six months after the end of the fiscal accounting year. This also accounts for the fact that the operators in Jordan are relatively small compared to operators in other countries where Accounting Separation is applied.

Due to the date of the decision of these Accounting Separation instructions, it is not more viable to require the regulated operators to provide the accounting separation for the ac-

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[18] Comreg, Decision No D08/10, Document 10/67 from 31 August 2010; Oman, Resolution No 112/2009 Regulation on Accounting Separation, Regulatory Accounting & Reporting Requirements AND Oman, Resolution No 112/2009 Regulation on Accounting Separation, Regulatory Accounting & Reporting Requirements.

counting year 2011, as this would give them less than six month time. For the first delivery, TRC changes the time frame so that the first delivery will start with the accounting year 2012, giving the Dominant Licensees enough time for preparation.

In conclusion, TRC decides on the time frame in the Instructions to be six months after the end of the fiscal accounting year. For the first delivery, TRC changes the time frame so that the first delivery shall be provided not later than June 2013, starting with the accounting year 2012, giving the Dominant Licensees enough time for preparation.

Consultation question XV: Do you agree with the proposed instructions for ad-hoc requests from TRC?

Zain asks for a time frame of 4 instead of 2 months for delivery while Umniah/BTJ agrees with the proposal of TRC. Orange Fixed and Orange Mobile disagree that TRC should have the ability to request Accounting Separation ad-hoc.

TRC Response

With regard to the time frame for delivery, the ad-hoc requests are requests for additional reporting, which will be based on what has already been provided on an annual basis. Therefore, two month time is sufficient.

TRC has proposed to request information ad-hoc only when “this is necessary to examine the compliance with regulatory obligations”. This is necessary in case TRC has any doubts or the accounting separation information is not clear or inconsistent. An example for this could be if there are doubts that the accounting separation documents are consistent with the LRIC cost models used to set tariffs. Another situation where it might be necessary for TRC to require more information might be if the regulated operator introduces new offers with prices for which TRC has the suspicion that cross-subsidization is practiced by the regulated operator and therefore considers to implement further remedies. It should be mentioned that “if TRC obliges a Dominant Licensee to provide such documents, it shall specify the scope and level of detail as necessary and proportionate in the light of the question to be examined”. Hence, ad-hoc information will only be requested when necessary and appropriate. TRC is aware of the concerns of Orange Fixed and Orange Mobile and will only request what is possible and necessary.

In conclusion, TRC maintains its position.

7.3 Publication and Confidentiality Issues

Consultation question XVI: Do you agree that the information must generally be treated confidential and that TRC should be able to publish Accounting Separation only in certain cases?

Zain asks for the Accounting Separation to be published and do not agree with the proposal of TRC or the opinion of Orange (as it states in the comments on comments). Thereby it states that accounting separation is non-disclosed in several countries, but refers to UK where it is disclosed. It also states that disclosure is required as Accounting Separation is implemented to guarantee transparency for market participants.

Umniah/BTJ also disagrees with TRC's proposal and states that the information must be made public in full. It thereby also refers to the Recommendations of ERG from 2005.

Orange Fixed and Orange Mobile agree with the proposed procedure, but clarify that they would like to include a procedure for the publication of information, which includes rules stating that the information should only be published in exceptional circumstances and the publication should be consulted with the regulated operator in advance.

TRC Response

The comments submitted by the stakeholders include the request to disclose more information as well as to disclose less information. The proposal made by TRC strikes the balance between providing the market with sufficient information on one hand, and the need for operators to keep information confidential. It considers the information generally to be confidential as it states that "TRC treats the cost accounting information, in particular numerical data about costs, revenues and capital employed, and other undisclosed business issues as confidential". It also gives the Dominant Licensee the chance to influence what is being published as it states that “with regard to descriptive documents about the applied methodologies and principles, Dominant Licensees shall inform TRC whether such documents contain information that shall be treated as confidential. In such cases, the Dominant Licensee shall also provide a version without confidential information that is suitable for publication and shall provide TRC with reasons on why to treat such data as confidential.”

On the other hand, the proposal of TRC also foresees the publication of as much information as reasonable and justifiable and only for markets where the Dominant Licensee have been imposed cost orientation obligations: “TRC also publishes descriptive documents without confidential information as far as necessary to inform market players about the applied principles and methodologies. […] In exception of the principle of confidentiality […] TRC may publish transfer charges, profit margins and general costing data directly related to services and products for which the Dominant Licensee is obliged to charge cost-based prices”. In these markets, the prices based on LRIC are already known from the tariff regulation. Further, as TRC will have to approve the tariffs in these markets based on costs and the tariffs charged in these markets are of high relevance to the wholesale customers and other stakeholders, there is a substantial reason to publish this information. Further, the remedy to oblige the dominant operator to charge cost based prices is only imposed when this is reasonable based on existing competition problems related to tariffs. This also implies that the information to TRC and the other stakeholders in these markets are especially important in order to demonstrate compliance with the regulation.

When TRC applies this exception, it has to take into account the economic and legal interests of the Dominant Licensee versus the interests of other market players and the public interest to ensure fair competition”. As the article 47 of the Policy also states that “these requirements should be no more burdensome than is required to ensure fair competition” there are no reasons to change the proposal of TRC as it regards a balanced approach with regard to the disclosure of information.

<u>In conclusion, TRC maintains its position.</u>

7.4 Data Integrity and Maintenance

Consultation question XVII: Do you agree that the Dominant Licensees should keep the records for six years time in order to enable an audit or to derive information on the development up to six years back in time?

Orange Fixed, Orange Mobile and Zain agree. Umniah/BTJ generally agrees but states that no records should be destroyed after six years.

TRC Response

Based on the comments from the stakeholders, no changes are made to the proposal made by TRC.

8 Miscellaneous

Consultation question XVIII: Do you see any reasons to add any further issues to those dealt with in this document?

Orange Fixed, Orange Mobile and Zain state that Accounting Separation is an additional regulatory burden requiring extensive effort for the regulated operators to compile the information.

Orange Fixed and Zain have stated that they would like to see that TRC issues draft instructions before issuing final instructions.

Zain asks for an implementation period of 18 months as they regard accounting separation to be very resource intensive. Furthermore, Zain states that it needs a decision on the Accounting Separation by July 2012 in order to be able to prepare the accounts for the financial year 2013. As this issue is dealt with in question XVI and XV, TRC refers to the response provided in these sections.

Zain asks for the creation of an accounting set of books or asks if an offline process is required. The operator also asks for how the reconciliation should be made when the statutory accounts are based on HCA and the Accounting Separation is based on CCA.

Orange Mobile, Orange Fixed, Zain and Umniah/BTJ ask for a template for the results of the accounting separation. Orange Mobile and Orange Fixed asked for a second consultation on the format. In their comments on comments, Zain proposes that there should be an industry workshop discussing the process, its implications, expectations, benefits and the burdens.

Zain asks for how to account for operating expenses savings in the price of the asset when MEA is applied.

Umniah/BTJ proposes that the regulated operators should provide a methodology document in advance, which should be approved by TRC. Zain asks for the establishment of an industry group in order to clarify all the detailed issues.

Umniah/BTJ proposes that the accounting separation information should be published. Please refer to question XVI for the TRC response. Another comment made relates to accounting separation as a remedy for wholesale call termination. TRC thereby would like to refer to other parts of this document for the TRC comments on this issue.

Umniah/BTJ proposes that TRC should recalculate the cost of capital and not use the value extracted from benchmarks as applied by the TRC from earlier stages.

Another issue raised by Zain is if TRC has any international benchmark regarding the application of account separation on the mobile business.

TRC Response

With regard to the comments that accounting separation implies further regulatory costs to the regulated operators, TRC would like to clarify that it has proposed the Accounting Separation in a way which has the aim to reduce the burden as far as possible throughout the entire instructions, e.g. specifying the use of FAC instead of LRIC as far as possible and limiting the amount of information to be delivered as long as this is in line with international best practice.

With regard to the comment submitted that the operators would like to see that TRC issues draft instructions before issuing final instructions, TRC would like to clarify that the draft instructions were published within this consultation, i.e. this request has already been fulfilled.

With regard to the question of Zain concerning the creation of an accounting set of books and if an offline process is required, TRC would like to clarify that the procedure to be chosen is up to Zain as long as the principles and requirements are fulfilled, i.e. the outputs must be capable of independent verification (auditable) and understandable to the auditor and TRC. The implementation of CCA requires the operator to have a reliable database containing detailed information on the quantities of fixed assets in addition to all data which is normally available in the technical inventory, but this also requires reliable and available information on up-to-date prices.

With regard to the question of Zain concerning the reconciliation between statutory accounts based on HCA and the Accounting Separation based on CCA, TRC would like to clarify that this is one of the main tasks when the accounts are reconciled. Thereby the Dominant License should show that the revaluation of the assets according to CCA is one of the reasons for the deviations between the statutory accounts and the Accounting Separation results.

Another issue addressed by the stakeholders is a template for the results of the accounting separation. With this consultation, TRC has proposed Accounting Separation Instructions to be valid for different markets and different regulated operators. Hence, these instructions should be dynamic enough to not become obsolete when TRC is issuing new market review decisions or when regulated operators are introducing new services or restructuring themselves. If TRC would include detailed templates, these would not be generally applicable and would therefore imply that the instructions would become obsolete with every change in the market regulation. As all stakeholders submitting comments within the consultation have asked for a format for the Accounting Separation, TRC includes a non-binding recommendation on such a format into an annex of the Instructions. Thereby, the stakeholders have templates which they can relate to, but which are general enough to not become obsolete in case of regulatory and market changes.

TRC would also like to explain that the exercise of Accounting Separation is to transform/separate the existing statutory accounts and to modify these to a limited extent (i.e. based on CCA). The aim is not to provide new cost models or completely new accounting systems. As each Dominant Licensee have its own financial accounting and in most cases is expected to have its own ABC systems, imposing a common regulatory tool for Accounting Separation would not suit the internal systems of the Dominant Licensees. Doing so, the costs and regulatory would be increased in order to transform the sources of information to the formats provided by TRC.

With regard to the question of Zain on how to account for operating expenses savings in the price of the asset when MEA is applied, TRC would like to clarify that according to the concept of MEA, the value of the modern equivalent asset should be calculated taking into account the fact that assets might have a different functionality and different operating costs. New technologies are usually superior to old ones in terms of functionality and efficiency. Applying MEA means that assets of equivalent capacity and functionality are regarded. Where the MEA differs from the existing asset in terms of operating costs, asset life or service provided, this needs to be catered for during the asset revaluation by means of specific adjustments. These adjustments include:

- Operating expenditure adjustments: The operating cost of new equipment may be lower than that of the existing equipment. In this case, the cost of the MEA should be reduced by the present value of the additional operating costs associated with the existing equipment over the remainder of its life.

- Functionality adjustments: Similarly, new equipment may have increased functionality. If so, the cost of the MEA should be reduced taking into account differences in capacity and functionality between existing assets and its equivalent.

Regarding the question of Zain on the implementation of accounting separation in mobile markets in other countries, TRC would also like to highlight that the decision to implement accounting separation is a decision based on the specific competition situation in Jordan. One of the national characteristics of the Jordan markets is that TRC has found competition problems in the MACO markets, given the possibility of a leverage of market dominance from one mobile market to another as well (horizontal and vertical) and the link between Orange Mobile and Orange Fixed, of which the latter has dominance in a row of fixed markets, which implies that competition problems can be levered between fixed and mobile markets.

With regard to the proposal of the stakeholders to have an industry workshop or to consult the methodology documents in advance, before the accounting separation is provided, TRC would like to inform the stakeholders that these are welcomed to bilaterally clarify any related issues with TRC as well as with the auditor. With the Accounting Separation Instructions, TRC has issued the guidelines and the principles for the provision of accounting separation. As long as the dominant licensees provides Accounting Separation information which fulfils what is determined by the Instruction, TRC will approve the deliverables. Based on the consultation of the Accounting Separation Instructions and the possibility to clarify any issues bilaterally, the Dominant Licensees have enough information to provide Accounting Separation. TRC would thereby like to highlight, that it is bound to the Instructions and will not require any further documents or information than what is determined by these instructions.

With regard to the cost of capital, TRC would like to clarify that it is important to have a consistent regulation and that the same cost of capital should be applied disregarding the regulatory activity, as these costs are based on the costs of the entire operator.