



A Public Consultation Document

on

Draft Regulatory Framework and

Guidelines for Accounting Separation

23 June 2010

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Introduction

Accounting separation obligations can contribute significantly to the promotion and encouragement of fair, efficient and sustainable competition in telecommunications, as well as to other objectives of the Telecommunications Act.

Article 12 of the Telecommunications Bylaw states the conditions that CITC may impose on individual licenses to implement the objectives of the Act, including the conditions relating to the level of segregation of telecommunications services for accounting and regulatory purposes as may be determined by CITC.

Through this document, CITC presents for public consultation the draft Regulatory Framework for Accounting Separation "the Regulatory Framework" and the draft Guidelines for Accounting Separation "the Guidelines". These two documents set out CITC's view on the methodology for preparing accounts and systems and for presenting related information that shall be followed by any service provider that is designated by CITC to prepare Separated Accounts ("Designated Service Provider").

With the Regulatory Framework, CITC aims to replace the current Accounting Separation Policy issued with Decision No. 44/1425 and to define rules for an updated Accounting Separation regime.

With the Guidelines, CITC intends, inter-alia, to complement the Regulatory Framework and provide specific guidance to Designated Service Providers on how to prepare and present Separated Accounts.

Since the adoption of the Accounting Separation Policy in 1425, the telecommunications market in the Kingdom of Saudi Arabia has evolved significantly, with the introduction of competition in mobile and data communications and the more recently with the opening of competition in the fixed telecommunications markets. The Regulatory Framework and Guidelines are designed to reflect the evolving market conditions.

The new draft Regulatory Framework for Accounting Separation and related Guidelines are designed to flexibly apply to any market definitions and dominant service provider designations as have been or may be determined by CITC.

CITC is of the view that relevant, reliable and timely regulatory accounting and accounting separation information is required to inform many of its decisions and to monitor the

adherence of Designated Service Providers to the obligations set down in the Act, Bylaw and Regulatory Frameworks.

1. Purpose of the consultation

With this consultation, CITC intends to

- 1 permit and encourage the Stakeholders' contribution to the decision-making process;
- 2 give Stakeholders the opportunity to express their views and opinions on the draft Regulatory Framework and Guidelines;
- 3 allow Stakeholders to raise any remarks or questions related to the practical implementation of the Regulatory Framework and Guidelines; and
- 4 ensure consistency with national and international best practice in the adoption of an updated regime for Accounting Separation.

How to respond to this consultation

CITC invites all interested parties to participate in this Public Consultation. All comments must be received by CITC no later than 3:00 PM (KSA Time) on 1/9/1431 H corresponding to 11/8/2010 G.

This Public Consultation Document, including the draft Regulatory Framework (Attachment 1) and draft Guidelines (Attachment 2), are available for consultation on CITC's website at <http://www.citc.gov.sa>.

Responses and enquiries for the consultation should be directed to one or more of the following addresses:

a) E-mail to: reg_acc@citc.gov.sa

b) Delivery (hard and soft copy) by hand or by courier to:

Office of the Deputy Governor for regulatory policies and licensing affairs
Telecommunication and Technology Commission (CITC)
King Fahd Road, P.O. Box 75606
Riyadh 11588
Kingdom of Saudi Arabia

CITC welcomes all comments on the Public Consultation Documents. CITC particularly invites comments and responses to the specific numbered "Questions" set out in this Public

Consultation Document (the "Consultation Questions"). CITC encourages Respondents to support all comments with relevant data, analysis, benchmarking studies and information.

CITC may give greater weight to comments supported by appropriate evidence, however, it is under no obligation to adopt the comments of any Respondent.

Respondents are requested to submit their contributions using the following formatting guidelines:

- 1 Contributions should incorporate a Cover Page as per enclosed template [Annex A]
- 2 Contributions should clearly state the question or issue they refer to, using a table format as in the following illustrative example:

#	Question no.	Paragraph	Answer or issue	Evidence/Information
1	X	-	We support CITC position	Annex no. XY
2	-	XY	We recommend using a different approach	Benchmark in Annex XY Source: XYZ

Figure 0.1 Illustrative Example of contribution

- 3 Annexes or supporting documents should be clearly marked as such.

Respondents are requested, if appropriate, to prepare two separated sets of contributions: in the first one, confidential parts should be clearly marked ("Confidential Information Version"); in the second version, these parts should be properly redacted or summarised ("Public Version").

Questions not answered will be interpreted as "no comment" and, in principle, as tacit agreement with the proposed approach. Nevertheless, CITC encourages respondents to express their position and state their support, objection or alternative proposal.

CITC will answer to all reasonable requests for information or clarifications regarding this consultation document and will publish its answer (or a summary of it) on its website, so as to render it accessible to all Stakeholders. Requests must reach CITC by no later than 3.00 p.m. on 25/7/1431 H, corresponding to 7/7/2010 G.

Considerations

In order to assist interested parties in responding to the public consultation, CITC wishes to explain its approach and expand on the following seven main issues:

- 1 Use of the accounting separation information
- 2 Characteristics of the Regulatory Framework and Guidelines
- 3 Relationship with Regulatory Accounting
- 4 Preparation of Accounting Separation for regulated and not regulated Markets
- 5 Individual Relevant Services
- 6 Cost Accounting Convention
- 7 Preparation and Publication of Accounting Separation Information

1. Use of the accounting separation information

In CITC's view, "relevant, reliable and timely" regulatory accounting and accounting separation information is required to inform its decisions.

CITC intends to rely on Accounting Separation in order to, inter-alia:

- 1 Verify adherence of a Designated Service Provider to the obligations set down in the Bylaw of non-discrimination, objectivity, cost-based pricing and transparency.
- 2 Identify and prevent potential abuses of dominance or other anticompetitive practices by a Designated Service Provider.
- 3 Inform margin squeeze or predatory pricing tests.

2. Characteristics of the Regulatory Framework and the Guidelines

The Regulatory Framework and the Guidelines are designed to be technology neutral and applicable to all Designated Service Providers.

3. Relationship with Regulatory Accounting

The Guidelines contain detailed explanations on the relationship between Accounting Separation and Regulatory Accounting.

Regulatory Accounting can be defined as the obligation to prepare accounts, costs, revenues, information and systems for regulatory purposes. It is also an essential element in the fulfilment of the Accounting Separation obligation, where accounts, costs, revenues and related information are used in an Accounting Separation system.

CITC published with Decision No. (194/1429) Dated 23/02/1429H detailed guidelines on preparation of a LRIC Model for regulatory purpose "the LRIC Guidelines".

For the avoidance of doubt, the Accounting Separation Guidelines will not be a substitute to the existing LRIC Guidelines, but are intended to supplement and complement them, addressing specific issues related to Accounting Separation.

4. Preparation of Accounting Separation for regulated and not regulated Markets

CITC requires that all markets in which a Designated Service Provider operates must be subject to accounting separation, including markets in which the Designated Service Provider in question is not dominant, although CITC recognises that different conditions for preparation and presentation of information might apply in those markets. It should be noted that this obligation is imposed only on Designated Service Providers that are obligated to prepare separated accounts for a certain market or markets as designated by CITC. In CITC's view, this is an important element of the proposed account separation regime, since the obligation of non-discrimination and the prevention of cross-subsidization between regulated and non-regulated markets can only be ensured when costs and revenues are fully traceable, transfer charges are transparent and reconciliation between statutory financial accounts and regulated accounts is possible.

These provisions are consistent with international best practice and the specific regulatory and competition situation in the Kingdom.

5. Individual Relevant Services

CITC requires that a Designated Service Provider should prepare separated accounts for all markets in which it has an accounting separation obligation, at the level of individual relevant service and/or Products.

An accounting separation obligation is associated with the requirement to ensure and demonstrate that services included in that market are provided to third parties on a transparent non-discriminatory basis and/or according to cost based pricing (in case that such obligations apply). For this reason in CITC view, the preparation and presentation of separated accounts at the level of individual relevant service and/or products for all markets with an accounting separation obligation, does not represent an additional regulatory requirement.

CITC may additionally request at any time, on a case-by-case basis, that Designated Service Providers prepare and report ad-hoc information up to the service or product level. CITC may require this information in order, for example, to prevent margin-squeeze or predatory pricing conduct, and/or to carry out tariff approvals.

The above provisions are consistent with international best practice and the specific regulatory and competition situation in the Kingdom.

6. Cost Accounting Convention

The Regulatory Framework and the Guidelines provide that, unless stated otherwise by CITC on a case-by-case basis, Designated Service Providers should prepare Separated Accounts according to each and all of the Historical Cost Accounting (HCA), Current Cost Accounting (CCA) and Long Run Incremental Cost Accounting (LRIC) conventions.

CITC is of the view that the separation of accounts in all of the three cost accounting conventions is necessary to ensure understanding of costs/revenues for those services that are priced using a historical, current or long-run increment cost convention. LRIC is a widely used cost convention in costing and setting of regulated wholesale tariffs, such as interconnection services. HCA and CCA are useful, for example, in the examination of retail rates, examination of cross subsidisation in retail markets or the setting of wholesale tariffs based on retail minus regulation.

CITC is of the view that the cumulative preparation of three sets of accounts is a proportionate obligation, given that:

1. The preparation of accounts according to the HCA convention is always the starting point for the preparation of CCA accounts.
2. The preparation of accounts based on the CCA convention is an intermediate step in the preparation of LRIC-based accounts.
3. The LRIC Guidelines already require that the dominant service provider prepares accounts for cost-based pricing using LRIC.
4. CITC can postpone the implementation of this obligation, on a case-by-case basis.

7. Preparation and Publication of Accounting Separation Information

CITC requires Designated Service Providers to present two sets of Accounting Separation Documents, one specifically for publication and the other for internal use of CITC and the Auditor.

In CITC view, the publication of accounting separation information can greatly increase the confidence of Stakeholders that the Designated Service Providers has achieved full compliance with obligations set in the Regulatory Framework and Guidelines. On the other hand, CITC is aware that confidentiality issues may arise in connection with this publication requirement, due to the sometimes sensitive nature of the information required for the preparation of separated accounts. Thus CITC is of the view that the public interest and the protection of confidential information need to be properly balanced. In this respect, to determine where the right balance lies, CITC will evaluate if the benefits for the public interest deriving from the publication of particular pieces of accounting separation information outweigh any harm that may be caused to the Designated Service Provider from the publication of such data.

2. How views and information will be used

CITC plans to take into account, in the preparation of the final version of the Regulatory Framework and the Guidelines, all relevant respondents' contributions.

CITC will publish the "Public Version" of the responses to the consultation. Additionally, CITC intends to publish a summary of the responses to this consultation with its own comments on relevant contributions that are not confidential. Contributions that are marked as confidential will be taken into consideration but will, as a general rule, not be explicitly referred to or commented.

CITC will publish the name and address (or part of the address) of the persons and/ or organisations who contributed to the consultation.

3. Confidential information

Claims of confidentiality will be determined, if necessary, by CITC in accordance with the Rules of Procedure. In order to qualify as confidential, information must not be part of the public domain or knowledge and provided that it is clearly marked "Confidential Information Version".

4. Questions

Interested parties are kindly requested to complete a response for all questions.

4.1 General considerations

#	Question	Refers to paragraph(s)
1	Do you agree that an updated accounting separation regime can be useful in the current market and regulatory conditions?	Framework and Guidelines
2	What other soft or hard regulatory measures, such as compliance courses or operational/functional separation, can be effective in the current competitive conditions?	Framework and Guidelines

4.2 Regulatory Framework

General Considerations

#	Question	Refers to paragraph(s)
3	Do you believe that, in general, the Regulatory Framework provides the right level of detail, considered in combination with the more detailed Guidelines? If not, would you prefer the Regulatory Framework to be less detailed or more detailed?	-

Section 1: Introduction

#	Question	Refers to paragraph(s)
4	Do you agree that the existing Accounting Separation regime should be updated, for the reasons set out in the Introduction? If not, why? If yes, are there any other factors which, in your view, justify replacing the existing Accounting Separation Policy?	1.8

Section 2: Definitions

#	Question	Refers to paragraph(s)
5	Do you agree with the proposed definitions? If not, what changes or additions would you propose?	2

Section 3: Considerations

#	Question	Refers to paragraph(s)
6	Do you agree that it is essential that accounting information to be provided under the new accounting separation regime should concern both regulated and unregulated markets in which Designated Service Providers operate?	3.5

Section 4: Regulatory Framework

#	Question	Refers to paragraph(s)
7	Do you agree with the purpose of Accounting Separation set out in the Regulatory Framework? Are there any other factors you think should be added to this list?	4.1
8	Do you agree with the general principles proposed as regards the detail and level of accounting information to be provided?	4.5-4.8
9	Do you agree that, in addition to any regular reporting of Separated Accounts, the CITC should also request the submission of Separated Accounts on an "ad-hoc" (individual case) basis, at any time?	4.9
10	What other aspects, issues or provisions do you suggest should be incorporated in the Regulatory Framework?	-

Guidelines

Section 1: Definitions

#	Question	Refers to paragraph(s)
11	Do you agree with the definitions included in the Guidelines? If not, what changes or additions would you propose?	2

Section 2: Purpose and Scope of the Guidelines

#	Question	Refers to paragraph(s)
12	Do you agree with the purpose of the Guidelines? What other purposes should the guidelines have?	9

Section 3: Accounting Separation

#	Question	Refers to paragraph(s)
13	Do you agree with the objectives of Accounting Separation?	16-17
14	Do you agree with the importance and description of the principles stated in the Guidelines?	18-21
15	Can you suggest any other important principles that a Designated Service Provider should comply with?	18-21

Section 4: Level of Accounting Separation

#	Question	Refers to paragraph(s)
16	Please provide your opinion on the level of accounting separation required from a Designated Service Provider.	22-27
17	Do you think that imposing account separation at "individual relevant service level" is necessary? If not, what other level of detail could provide the same or other appropriate results?	24-25

Section 5: Cost Accounting Convention and Related Issues

#	Question	Refers to paragraph(s)
18	Do you agree that separated accounts must be prepared for each of Historical Cost Accounting (HCA), Current Cost Accounting (CCA) and Long Run Incremental Cost (LRIC) cost accounting conventions?	28
19	Do you think any other relevant information or provision should be included in the Guidelines regarding HCA in order to facilitate the implementation? If yes, please provide evidence of the related importance.	30-35
20	Do you agree on the valuation methods that must be used for CCA?	40
21	Do you agree with the provisions mentioned in the absolute valuation method?	41-43
22	Do you agree that appraisal method must be used for valuation of real estate assets?	48
23	Do you agree with the role and definition of the expert?	49-51
24	Do you agree with the list of criteria for assets that do not need valuation? Do you agree that non valuated assets shall not be higher than 20% of the total assets value, measured by the Gross Replacement Cost?	55-57
25	Do you agree that licence costs should not be revaluated?	58
26	Do you agree with the use of WACC as cost of capital also for	61-67

	HCA and CCA?	
27	Do you agree that consistency should be maintained between cost conventions?	68
28	Do you agree with the use of the "tilted annuity methodology for depreciation in LRIC conventions?	71
29	Do you agree with the use of the "straight line depreciation" methodology for HCA and CCA conventions?	72

Section 6: Preparation of the Accounting Separation System

#	Question	Refers to paragraph(s)
30	Do you agree with the proposed minimum stages of the accounting separation system? Is there any other stage that you would recommend?	79
31	Is each stage described clearly? What other information would you consider necessary?	80-99
32	Do you agree with the proposed attribution methods?	101-120
33	Is there any other relevant attribution category that must be considered in the guidelines?	101-120
34	Do you agree with the cases of transfer charges explained in the Guidelines?	124
35	Do you agree with the proposed method of calculation for transfer charges?	125-131

Section 7: Reporting Requirements

#	Question	Refers to paragraph(s)
36	Do you agree with the list of Separated Accounts Reports? What other reports should be required? What would be the benefits of obtaining these other reports?	138
37	Do you agree with the list of Related Information and Notes? What other Related Information and Notes should be required? What would be the benefits of obtaining these other Related Information and Notes?	139
38	Do you agree with the importance of publication?	143-144
39	Do you agree with the list of documents for publication? What other documents should be published and what would be the benefits of such a publication?	145
40	Do you think the timeframe for submission and publication is reasonable?	146-155
41	Do you agree with the precautionary and additional measures proposed by CITC? What other measures could be used?	160-167
42	Do you agree with the provisions and schedule for the first implementation?	168-176
43	Do you agree that a Designated Service Provider should be responsible to present an accounting separation methodology?	169

Section 8: Audit and Review

#	Question	Refers to paragraph(s)
44	Do you agree that the Auditor should give an opinion on the basis of "fairly presented" in accordance with the framework and guidelines? If not, what do you propose as an auditor opinion basis and why?	178
45	Do you agree with the technical capability requirements for the Auditor?	183-185
46	Do you agree with the auditor's listed tasks?	186-187
47	Do you find the content of the audit report detailed enough? What other information you think would be necessary? Why? What would be the benefit?	188-190
48	Do you agree with the importance of a review and conformity check of the Accounting Separation System and related documentation?	191-195
49	What other aspects, issues or provisions do you suggest should be incorporated in the Guidelines?	-

Annex A of the Guidelines: Reporting Templates

#	Question	Refers to paragraph(s)
50	Do you agree with the proposed templates?	N/A
51	Is there any other information or template you consider necessary for ensuring compliance with the objectives of the guidelines and accounting separation?	N/A

Annex B of the Guidelines: Management Declaration

#	Question	Refers to paragraph(s)
52	Do you think that the proposed declaration is enough to provide certainty in the quality of the information submitted?	N/A
53	Would you recommend any other declaration?	N/A

Annex A: Cover sheet for responses

Name of respondent:

Position:

Firm or organisation:

Address and Email:

Contact numbers:

Can we contact you if we have any question regarding your contribution?

YES

NO

Declaration

I declare that I have the right to submit a response in the name of the aforementioned Firm/Organisation/Person and confirm that the correspondence supplied with this cover sheet is my/our unique response to the consultation.

Date:

Full Name

Signed and Stamped

Attachment (1)
Accounting Separation Regulatory
Framework

Attachment (2)

Accounting Separation Guidelines