REVIEW OF ACCOUNTING SEPARATION FRAMEWORK FOR TELECOMMUNICATION SECTOR IN SINGAPORE

1. The SingTel Group[1] ("SingTel") welcomes the invitation of the Info-communications Development Authority ("IDA") to respond to the consultation on a review of the accounting separation framework for the telecommunication sector in Singapore. In this response, unless otherwise specified, a reference to "SingTel" is a reference to the group containing the following entities:

   Singapore Telecommunications Limited ("SingTel")
   Singapore Telecom Mobile Private Limited ("SingTel Mobile")
   Singapore Telecom Paging Private Limited ("SingTel Paging")
   SingNet Private Limited ("SingNet")

2. <u>Background</u>

2.1 Existing Accounting Separation framework

2.1.1 SingTel notes that the existing regulatory framework already requires operators/licensees to comply with accounting separation. The existing Accounting Separation Guidelines ("ASG") were developed by IDA before full liberalisation of the telecommunications industry in April 2000. The purpose of the existing ASG is to act as a safeguard to develop effective competition, detect and monitor anti-competitive practices such as cross-subsidies within diversified or integrated telcos, predatory pricing, non-arm's length transactions between entities etc.

2.1.2 SingTel has developed systems, procedures and processes to ensure compliance with the existing ASG regulatory requirement, reporting on the following services since 1 April 1997:

   Basic network services
   Basic retail services
   Satellite uplink & downlink
   Broadband access wholesale services
   Broadband access retail services
   Internet access services
   Public cellular mobile services
   Paging public radio paging services
   Public mobile data services

[1] The SingTel Group comprises Singapore Telecommunications Limited (SingTel), Singapore Telecom Mobile Private Limited (SingTel Mobile), Singapore Telecom Paging Private Limited (SingTel Paging) and SingNet Private Limited (SingNet)

2.1.3 The reporting statements generated for each service mentioned above include:

Income (P&L) statement
Statement of related entity (internal) transactions
Statement of fixed assets
Balance sheet
Reconciliation of all the service P&L statements to the audited company P&L statement
Reconciliation of the service fixed asset statements to the Fixed Asset Note in the company's audited accounts
The audited company Balance Sheet (BS); and
An annual audit report.

2.1.4 We strongly contend that the existing ASG adequately addresses regulatory requirements and there is no need to amend or alter the existing ASG. To do so, would impose significant regulatory compliance costs on existing operators. We contend that, in the absence of any manifest shortfall in the existing ASG, the existing ASG should be retained.

2.2 Proposed Accounting Separation framework:

2.2.1 Notwithstanding the views expressed in 2.1.4 above, we note that IDA now wishes to review the existing accounting separation framework ("ASF") and states that the new framework proposed is meant to monitor for anti-competitive activities, eg cross-subsidies, potential predatory pricing etc. In this regard, IDA has made several recommendations, including but not limited to

(a) Applying accounting separation requirements at 2 levels: Detailed Segment Reporting ("DSR") and Simplified Segment Reporting ("SSR")
(b) Additional segmentation of services
(c) Implementation of a Current Cost Accounting ("CCA") approach over a 2 - 3 years' timeframe
(d) New reporting architecture and cost allocation principles
(e) Further disaggregation of costs
(f) Provision of additional non-financial information

3. General Comments - Cost of Regulatory Compliance

3.1 SingTel has already invested significant amounts in developing systems, procedures and processes to ensure compliance with the existing ASG. The introduction of any new framework, it is important to ensure that the costs of regulatory compliance should not outweigh the benefits of the regulatory requirements. As we have indicated above, the imposition of the new proposed

ASG will result in significant regulatory compliance costs. If adopted, we estimate that compliance with the proposed accounting separation requirements will require substantial implementation costs of between $7 million to $10 million and yearly operating costs of $1 million to be incurred simply to enhance and maintain the existing systems, procedures and processes.

3.2 As a practical matter, operators would already have implemented accounting and financial systems which can be complex and designed to meet specific business and statutory requirements. Additional requirements outside the normal operational and management needs of a business operation would require substantial investment in time and costs in implementing new systems and resources to support these additional requirements

3.3 For example, the current accounting system is not designed to allocate balance sheet items to each segment and this makes it almost impractical to provide meaningful Statements of Capital Employed for each segment.

3.4 We submit that IDA considers carefully such costs and operational issues to avoid imposition of onerous requirements. SingTel has already invested significant amounts in developing systems, procedures and processes to ensure compliance with the existing ASG. Should a new and unduly rigid and demanding accounting separation framework be imposed, this will result in operators bearing an additional cost burden, leading to an increase in the overall cost structure of an operator, which would in turn translate into high cost of service provision. In such an environment, the ultimate bearers of such costs would be the consumers. This is a situation that should be avoided and we urge IDA to consider carefully the nature of the accounting separation regime, taking into account the consumers' interests. We contend that the existing ASG should be retained.

4. Detailed Segment Reporting ("DSR") vs Simplified Segment Reporting ("SSR") - IDA invites comments on its proposed two-level approach to accounting separation.

4.1 In Section 5.2 of its consultation document, IDA proposed that Dominant FBOs and their controlled entities submit reports based on DSR whilst all other FBOs submit reports on SSR requiring the following:

(a) **Detailed Segment Reporting** - requires statements for the following key segments

- (i) Access
- (ii) Domestic Network
- (iii) International Network
- (iv) Retail Services, which are further divided into key service types as follows:
    - Fixed Line Access
    - Domestic Calls

- International Calls
- Domestic Leased Circuit Services
- International Leased Circuit Services
- Narrowband Internet Access
- Broadband Internet Access
- Mobile Domestic Access and Calls; and
- Other Activities.

(b) **Simplified Segment Reporting** - requires statements for the following segments
(i) Fixed Domestic Services
(ii) International Fixed and Mobile Services
(iii) Mobile Domestic Services
(iv) Narrowband Internet Access
(v) Broadband Internet Access; and
(vi) Other Activities

4.2 Not equitable to impose DSR on a small & select group of licensees only

4.2.1 If IDA perceives a need for accounting separation to monitor for anti-competitive conduct, we do not agree that this could be achieved by merely imposing detailed DSR requirements on only a small and select group of licensees. We set out our views below.

4.2.2 IDA has proposed to require DSR on Dominant FBOs, their controlled entities and potentially related entities. Where SingTel is concerned, this would imply that entities like SingTel Mobile, SingTel Paging and SingNet would be required to report on a DSR level too. This treatment is discriminatory and unfair to these entities who have no market dominance and need to compete vigorously in their respective markets with competitors who are not similarly burdened. We elaborate on this point below.

(a) The paging market is experiencing such a rapid decline that it has become a "sunset" industry. The mobile & internet markets experience intensive competition.

(b) We note that where the vigorously competitive mobile market, none of the 3 existing players - SingTel Mobile, M1 and StarHub Mobile - have significant market power.

(c) SingNet is only an SBO and competes in a market where there are currently more than 20 Internet Service Providers ("ISPs") and many more resellers of internet services. There is no reason why it should be subject to DSR when IDA does not require any SBOs to be subject to the new accounting separation framework.

4.2.3 We believe that where none of the other FBOs providing internet, mobile or paging services are required to report on a DSR basis, a non-discriminatory form of treatment should be accorded to SingTel Mobile, SingTel Paging and SingNet too. In our view it would be unfair to subject these entities to DSR. These entities operate in competitive markets and should not be subjected to additional burdens above and beyond those of their competitors.

4.2.4 IDA should monitor the activities of the rest of the industry which comprises some 30 Facilities-Based Operators ("FBOs") and more than 500 Services-Based Operators ("SBOs") and not just a small group of Licensees. As it is, with the trend towards mergers and acquisitions in the info-communications industry, it is possible that substantial cross-holdings among the licensees involved could enable these licensees to provide cross subsidies to each other or engage in less than arm's length related entities transactions with each other. If IDA believes that accounting separation allows the regulator to police and detect anticompetitive conduct, then we submit that it is crucial for IDA to require the same level of reporting details from <u>all operators</u> and not create a two level approach whereby IDA focuses intensively on the activities of only a small number of operators.

4.3 Recommendation to IDA for a One-Level Reporting Approach - SSR

4.3.1 Given that IDA wishes to detect anti-competitive conduct and would need to achieve a balance between the requirements of the framework against the compliance costs associated with these requirements, we would recommend that IDA imposes the same reporting requirements approach, whether DSR or SSR, on <u>all operators</u> in terms of the relevant segments.

4.3.2 We would propose that the SSR reporting approach be imposed on all FBOs as this represents an objective and comparable reporting structure, where the FBOs are required to produce statements on the actual types of retail services they offer based on the same accounting separation requirements.

4.3.3 A one-level reporting approach for all operators, ie SSR only, would achieve the following:

(a) IDA receives information on the same segments and can make useful comparisons. If a two-level approach is used where DSR requires provision of Statements of Mean Capital Employed, it serves little purpose to IDA as far as comparisons and benchmarking with other operators are concerned if DSR is imposed on some FBOs only.

(b) Anti-competitive conduct by one operator can be better detected with increased comparability.

(c) SSR has a lower cost of regulatory compliance than DSR and is fair and equitable to all operators in the market.

4.3.4 Should IDA need any additional information or layer of details from any one operator, such information can be required by IDA as and when necessary. Cost will therefore be incurred only when a relevant need arises.

4.3.5 Fair and equitable approach

(a) The final approach used by IDA should be fair and equitable to all operators. Hence, whilst we advocate that all operators should be asked to comply with similar requirements on a non-discriminatory basis, should IDA implement different reporting requirements on different operators, eg between different FBOs, then IDA should not impose on entities which are related to Dominant FBOs the same reporting requirements as those imposed on Dominant FBOs. Hence, in the case of SingTel Mobile, SingTel Paging which are clearly not Dominant FBOs, the reporting requirements on these operators should be based on the merits of their individual cases and should not, in any way, simply default to the requirements imposed on SingTel. SingTel Mobile and SingTel Paging should not be subjected to additional burdens above and beyond those imposed on their competitors.

(b) In the case of SingNet which is only an SBO operating in a competitive market, we reiterate that a fair and consistent approach be taken. IDA does not impose accounting separation requirements on other SBOs, and as such, SingNet should not be subject to accounting separation.

5. <u>Historical Cost Accounting ("HCA") vs Current Cost Accounting ("CCA")</u>

5.1 IDA invites comments on

(a) Whether accounting separation should be based on “pure” HCA, a modified form of HCA, or CCA

(b) Should CCA be implemented now or later? If later, what would be an appropriate time of implementation

5.2 In its consultation document, IDA recommends that accounting separation should initially be based on HCA but should move to CCA over a 2-3 year timeframe. In stating this, the IDA admits in its consultation document that -

"To change both the reporting structure and cost basis would require substantial changes to a Licensee’s existing accounting separation procedures and systems"

and

"The extended timeframe for implementation of Current Cost Accounting (CCA) is intended to allow for the expected significant implementation process required".

5.3 We believe that HCA is a more objective cost basis than CCA as the latter will violate the conventional realization principle as valuation of assets under CCA depends on changes in market price. One of the implementation issues with CCA is the subjectivity in determining market value of assets, increases or decreases in costs. The CCA presents a "presumed" notion of costs based on subjective analysis of the changes in costs and values, instead of costs being objectively measured on an arms-length basis.

5.4 CCA is not adopted in the Statements of Accounting Standards (SAS) in Singapore. The Institute of Certified Public Accountant (ICPAS) has acknowledged[2] that there is no international consensus on the merits and benefits of using CCA as a cost accounting standard. It would be anomalous, and consequently, even confusing for operators to have to conform to different sets of cost accounting policies for the financial reports they have to generate - HCA for all statutory accounts and CCA for accounting separation reports. In fact:

(a) The use of CCA will burden the operators with a high cost of compliance with investments in new systems and immense manual efforts to prepare the information using CCA. There are no means to derive empirical cost information for CCA purposes and operators would have to rely on manual means to compute their costs according to CCA standards.

(b) The use of CCA will result in cumbersome and inefficient reconciliation of accounting separation statements with the company (and its audited) accounts.

5.5 In ACCC's draft of the Telecommunications Industry Regulatory Accounting Framework published in November 2000, it was highlighted that HCA was recommended and that it was not practical to move directly from such existing cost arrangements to a completely new reporting architecture with a new cost basis and a new cost standard simultaneously as such changes involve significant investments in time and effort by both the operator and the regulator.

5.6 Comment

5.6.1 We propose that the accounting separation framework continues to adopt HCA as the cost accounting base.

5.6.2 We note that IDA intends for accounting separation to move towards CCA over a 2-3 year time frame. This step should not be taken in isolation without considering the actual accounting standards used by other regulatory and accounting bodies in the country. We recommend that IDA reviews the move to CCA in line with the accounting standards used in the SAS and when it thinks it is appropriate to move towards the CCA, this should be done only

[2] "Information Reflecting the Effects of Changing Prices", Exposure Draft (ED) of the proposed new Statement of Accounting Standards SAS 37

after in-depth consultation with industry and the accounting profession is done.

6. Reporting Architecture & Cost Allocation Principle

6.1 IDA asks for comments on

(a) The degree of disaggregation and the segment definitions proposed for DSR & SSR

(b) The preferred method of cost allocation for DSR & SSR

(c) The degree of prescription in the ASG that should be specified for cost allocation methodologies for DSR & SSR

6.2 Comments

6.2.1 Degree of disaggregation and segment definitions

As stated in paragraph 4, we recommend a one level reporting approach (ie SSR) to apply to all operators. To be consistent with the treatment accorded to all other SBOs, SingNet, which is an SBO, should not be subject to accounting separation requirements.

6.2.2 Cost Allocation Methodology

We agree generally with IDA's recommendation of a Simplified Cost Driver Attribution Methodology as it is commonly applied. The Detailed Cost Driver Allocation Methodology & Capacity Utilisation Methodology would require a significant level of details that is not likely to be supported by operators' accounting systems.

6.2.3 Degree of prescription for cost allocation

In relation to the degree of prescription for cost allocation, we submit that:

(a) The level of disaggregation of costs in terms of Fixed and Variable costs may not be useful and the cost of preparation will outweigh the benefits derived. Other than outpayments, licence fees and cost of sales, costs incurred by a telecommunications operator are not that clearly identifiable as fixed or variable in nature and may vary neither linearly nor directly with cost drivers.

(b) The requirement to classify costs into direct, directly and indirectly attributable is arbitrary and serves little purpose for accounting separation.

(c) Should operators be required to identify such costs, the process and the method(s) involved are arbitrary and will result in inconsistencies in the classification of costs according to each operator's interpretation. The outcome would cause distortions in analysis by IDA.

(d) We believe that it may be more useful for operators to separately identify internal network costs in the segment reporting of retail services as it would be more effective in monitoring cross-subsidization practices.

7. Non-Financial Information Reporting

7.1 IDA asks for comments on:

(a) Should non-financial information be required as part of the standard reporting requirements?

(b) Should the same level of non-financial reporting be required under both DSR and SSR?

7.2 We are of the view that IDA should require all operators to be subject to one level of reporting ie reporting requirements should be the same for all operators.

7.3 We note that IDA has specifically proposed the following information be reported as part of the normal accounting separation requirements:

Fixed Domestic Services	Number of residential direct exchange lines(DEL), Number of business DEL,
Domestic calls	Total installed domestic call minutes, % or number of unsuccessful call attempts, Number of connected calls, Number of call minutes
International calls	Total installed international call minutes, % or number of unsuccessful call attempts, Number of connected calls, Number of call minutes,
Mobile services	Total installed switch call minutes capacity, Number of subscribers, Number of calls, Number of call minutes
Narrowband Internet Access	Number of dial up Narrowband Internet Access subscribers, Number of leased circuit Narrowband Internet Access subscribers, Average monthly hours of use per dial-up
Broadband Internet Access	Number of Broadband Internet Access subscribers, Installed capacity for Broadband Internet Access

7.4 We note that IDA has already put in place the existing measures to monitor market trends and developments:

(a) Information submitted by operators in accordance with its "Provision of Information" framework, containing:

- Domestic Services - Number of Residential & Business DELs;
- International call connections & minutes;
- Mobile subscribers, including prepaid;
- Paging subscribers;
- Total number of narrowband internet access subscribers (broken down into dial-up subscribers and leased circuit subscribers);
- Total number of broadband internet subscribers

and several other categories of information

(b) Additionally, operators are required to provide the necessary information for IDA to understand any development or issue as and when IDA requires such additional information.

(c) IDA has in place necessary guidelines to prevent cross-subsidies and any anti-competitive behaviour as set out in Sections 7 of the Telecom Competition Code ("TCC").

(d) IDA has the powers to require licensees to file its tariffs and prices and can require an operator to adjust the tariff or scheme if such tariff or scheme is deemed to contravene any provision in the TCC.

7.5 We are therefore of the view that non-financial information should not be part of the standard reporting requirements.

8. <u>Reporting Requirements</u>

8.1 IDA asks for comments on its proposed frequency and timing of the reporting.

(a) IDA proposes that the current 6 month reporting cycle be continued under the revised ASG and has recommended the following timings for the reports to be submitted:

Statement	Period & Frequency	Timing
Income Statements	6 monthly (for the 1st 6 months and 2nd 6 months of the licensee's FY	Submitted to IDA 4 mths after end of relevant reporting period
Reconciliation of Consolidated Income Statement	Annual (for licensee's full financial year)	Submitted to IDA 4 mths after end of relevant reporting period
Statements of Mean Capital Employed	6 monthly (for the 1st 6 months and 2nd 6 months of the licensee's financial year)	Submitted to IDA 4 mths after end of relevant reporting period
Reconciliation of Consolidated Mean Capital Employed Statement	Annual (for licensee's full financial year)	Submitted to IDA 4 mths after end of relevant reporting period
Non-Financial Report	6 monthly (for the 1st 6 months and 2nd 6 months of the licensee's financial year)	Submitted to IDA 4 mths after end of relevant reporting period
Audit Report	Annual (for licensee's full financial year)	Submitted to IDA 2 weeks after audit completion date

8.2 Comments

8.2.1 We are in general agreement that the accounting separation reports for operators (based on the one level of SSR reporting approach) be submitted 4 months after the end of the reporting period. However, we wish to highlight that operators, particularly FBOs and operators who are publicly listed companies, have existing statutory requirements, reporting timelines and obligations to the Stock Exchange and Registry of Companies. If DSR is required, a reasonable reporting period would be 6 months after closing of accounts, given the additional work and resources required.

8.2.2 The preparation of accounting separation reports is done at the company level and reconciliation of statements will be made against audited company’s accounts and not against consolidated audited accounts of the operator.

8.2.3 The Statements of Mean Capital Employed should be submitted on a yearly basis instead of half-yearly. Our systems are currently not set up to generate such reports and we anticipate the efforts required to process and furnish the information would be laborious.

9. Accounting Separation Statements

9.1 IDA asks for comments on the following:

(a) The format and content of proposed accounting separation statements for each type of reporting

(b) The level of detail that should be required in the Income Statements for each type of reporting; and

(c) The level of detail that should be required in the Statement of Mean Capital Employed for DSR

9.2 Comments

9.2.1 As noted in paragraph 4, we recommend that there should only be one level of reporting for all operators based on the SSR approach. Hence, there is no need for the requirement indicated in Section 6.4.4 of IDA's consultation document to prepare a separate Simplified Segment Income Statements under DSR. Any duplication of efforts must be avoided.

9.2.2 We note that IDA's Accounting Separation Guidelines (Schedules 2.1 - 2.4, Schedules 3.1 - 3.2) requires a comparison of the previous financial year against the prevailing financial year reported on. For the first report, SingTel will not be able to produce comparative reports for the previous financial year. We do not believe that it is practicable. However, in the event that it was, it would be extremely costly and time consuming.

9.2.3 We request that for the first year, this requirement be replaced by statements reflecting only the prevailing financial year's information. Any implementation of the ASG can take effect on a prospective basis and not retrospectively.

10. Administrative Requirements

10.1 IDA has requested for comments on

(a) The required content on the operators' Procedure & Cost Allocation Manual

(b) The PCAM approval process

10.2 Comments

10.2.1 An unqualified auditors' report should provide IDA with reasonable comfort that proper and acceptable processes and accounting policies are in place. Management letters have therefore no relevance to the accounting separation process unless the auditors' opinion itself is qualified for control weaknesses.

10.2.2 Our comments on the approval process are contained in paragraph 12 below.

11. <u>Accounting Separation Audit</u>

11.1 IDA asks for comments on its proposed audit approach and proposes that an audit be undertaken by an independent auditor appointed by the operator to audit the operator's compliance with the Licensee's PCAM (which would need to be approved by IDA), and whether the Licensee has exercised consistency in applying the ASG and the PCAM. In addition, IDA will retain a reserve power to appoint an auditor to re-audit the accounting separation reports if it is concerned that the initial audit is inadequate. All audit costs will be borne by the Licensee.

11.2 Comments

11.2.1 We note the requirement for an independent opinion on the extent of the operator's compliance with the ASG and to this extent, operators already ensure that all existing accounting separation reports are audited before submission to IDA.

11.2.2 However, unless the auditor appointed is other than an accounting firm of international repute or issues an adverse report, we do not agree with any re-audits, much less the rationale for operators to bear the cost of such re-audits imposed by IDA.

11.2.3 Should re-audits be considered by IDA unilaterally as necessary, it would not be fair to require operators to bear costs of such re-audits. IDA should fund any re-audits from the licence fees collected from operators.

12. <u>Implementation</u>

12.1 IDA asks for comments on:

(a) Implementation issues; and

(b) The proposed timeframe for implementation.

12.2 IDA proposes that for existing operators, the proposed <u>implementation dates</u> for the ASG are:

- By end September 2002 for those whose financial year commences on 1 April
- By end December 2002 for those whose financial year commences on 1 January or 1 July

12.3 In Section 7.1.1 of the consultation document, IDA also states that an operator must submit its proposed PCAM to IDA for approval within 90 days of the effective date of the ASG and IDA would take at least another further 90 days before notifying the operator of its approval or modifications that are needed. Where modifications are required, these would be resubmitted to IDA within 30 days of the modification request from IDA and in its approval notice, IDA will notify the operator of the date on which the operator must begin reporting in compliance with the new accounting separation guidelines.

12.4 Comments

12.4.1 It is necessary that operators be given sufficient time to prepare and analyse the effect on any revised accounting separation framework on the company. Our existing accounting and operating systems are established for statutory reporting and also to meet the commercial needs of the organisation. To comply with the proposed framework, major changes to our systems are required which would need a reasonable implementation period. A major revamp of the entire system may even be necessary to avoid tedious and laborious efforts.

12.4.2 Operators must be given a minimum of 12 months from the approval of the PCAM to implement and establish the necessary systems to comply with the new reporting requirements.

13. Conclusion

13.1 SingTel believes that the existing ASG adequately addresses regulatory requirements. In our view there is no need to amend or alter the existing ASG. SingTel has invested significant amounts in developing systems, procedures and processes to ensure compliance with the existing ASG. The imposition of new guidelines will impose significant regulatory compliance costs on existing operators. In the absence of any manifest shortfall in the existing ASG, the existing ASG should be retained.

13.2 IDA proposes to impose DSR on Dominant FBOs, their controlled entities and potentially related entities whilst all other FBOs only need to comply with SSR. Where SingTel is concerned, this would imply that entities like SingTel Mobile, SingTel Paging and SingNet would be required to report on a DSR level. We believe that this would be unfair, unreasonable and inequitable. SingTel Mobile, SingTel Paging and SingNet operate in competitive markets and should not be burdened with additional regulatory obligations above and beyond those imposed on their competitors. A fair and equitable approach should be adopted, with the same reporting requirements imposed on all operators.

13.3 It is also crucial to note that the framework must be useful. Implementing a two (2) level reporting approach proposed in the consultative document will serve little purpose in terms of comparisons and benchmarking across the operators. We recommend that a one (1) level reporting approach be used and we support the implementation of the SSR on FBOs.