



cablebahamas

Consultation on

**SETTING REGULATED INTERCONNECTION CHARGES OF
BAHAMAS TELECOMMUNICATIONS COMPANY LIMITED
(BTC) GOING FORWARD**

ECS 21/2012

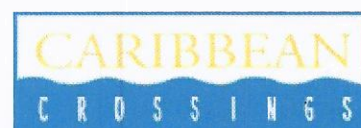
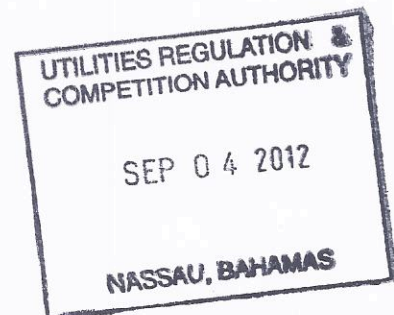
Submitted to the

Utilities Regulation and Competition Authority

September 3 , 2012

submitted by

Cable Bahamas Ltd.



Cable Bahamas Ltd., Caribbean Crossings Ltd. and its affiliates (hereinafter, "CBL") hereby respond to the public consultation document SETTING REGULATED INTERCONNECTION CHARGES OF BAHAMAS TELECOMMUNICATIONS COMPANY LIMITED (BTC) GOING FORWARD: ECS 21/2012 issued by URCA on 27th July 2012.

I. INTRODUCTION

The privatisation is reported to have cost \$28m¹ and CBL has not escaped the increased regulatory costs² of liberalization. We think that it is important that the electronic communications market benefits as soon as possible from cost and efficiency gains the various exercises undertaken by URCA seek to produce. It is important that URCA's proposed timelines account for rapid technological changes and therefore glide paths should bear in mind market conditions.

II. Responses to the Consultation

Question 1: Do you agree with URCA's stated rationale for the need to review BTC's RAIO charges on a regular basis in the current market environment?

The Access and Interconnection guidelines and URCA's Final SMP Decision require BTC to set RAIO charges based on efficiently incurred costs. In the consultation document, URCA states that its reference to 'cost' means BTC's latest available accounting separation cost data. CBL agrees that RAIO charges should be based on efficiently incurred cost and should relate to BTC's latest available costs. In an environment of falling service unit costs, using outdated cost information could lead to super-normal profits for BTC at the expense of consumers and other players in the electronic communications sector. This would be incompatible with URCA's statutory requirements to further the interests of consumers by promoting competition; and to further the interests of persons in The Bahamas in relation to the electronic communications sector. Therefore, CBL strongly favours reviews of BTC's RAIO charges on a regular basis.

According to URCA, the audit of BTC's 2010 A/S revealed "significant underlying concerns" which make it unclear to URCA whether the 2010 A/S results provide a sound basis for any revised RAIO charges. In particular there are observed fluctuation in RAIO service costs of the 2010 A/S compared to the 2009 A/S. According to URCA "the 2010 accounts revealed that the cost of the Point of Interconnection (Pol) network component was substantially lower in 2010 relative to 2009". In general, BTC's A/S results have fluctuated significantly from 2009 to 2010. CBL is not in a position to ascertain whether the 2010 Pol cost is correctly calculated and therefore preferable to the 2009 Pol cost. However, CBL wishes to stress that in a context in which unit service prices tend to fall in the overwhelming majority of jurisdictions, the use of outdated cost information is most likely to be at the expense of the general public and BTC's competitors. CBL believes that neither itself, other competitors nor the general public should bear the burden of shortcomings in BTC's information systems. Furthermore, CBL is concerned

¹ "BTC Privatization Cost nearly \$28m" - The Tribune, March 8, 2012,

² "Cable on track despite 40% Power Bill Rise" - Tribune - November 14th, 2011

that the main objectives behind the ex ante obligations are not being achieved as a result of significant deficiencies and concerns. The information is unreliable which will likely result in incorrect pricing.

CBL welcomes the application of efficiency adjustments but would like to note that they are insufficient. URCA admitted in its Final Decision on BTC's Cost Efficiency (ECS 20/2012) that it sees "merits in CBL's arguments on the potential impact of interconnection outpayments on BTC's efficiency results for the mobile market." CBL re-iterates that the impact of interconnection outpayments should be accounted for in the efficiency adjustment because of its very significant impact. If outpayments were to be taken into account, the efficiency adjustment to mobile charges would be significantly higher according to CBL's analysis. CBL agrees with URCA that a reasonable degree of certainty regarding RAIO prices in the market is desirable.

Question 2: Please comment on the options for setting BTC's RAIO charges going forward, including their merits in the current context of the electronic communications market in The Bahamas.

URCA specifies five criteria against which it is assessing the three options it gives. CBL believes that the first criterion namely "ensuring that RAIO charges move towards an efficient cost level" is not sufficient. In year 2012, RAIO charges should already be at an efficient cost level. This is what the Access and Interconnection Guidelines and the Final SMP Decision postulate. Anything else is insufficient at the expense of BTC's competitors and consumers.

Annual Updates

CBL believes that annual updates of RAIO charges on the basis of BTC's latest available separated accounts is not a valid option as long as there are "significant underlying concerns" about BTC's accounts. CBL agrees that substantial fluctuations in RAIO prices and the uncertainty they introduce in the market should be avoided.

Multi-year Glide Path

Glide paths are used in many jurisdictions to bridge the gap between existing termination charges and forecast future cost-based rates. Its main advantage is that it gives operators time to adjust retail prices where a rapid or sudden drop in termination rates may lead to distortions in the market. However, a glide path delays the introduction of cost-based termination rates. The target rate to which the glide path leads should be and actually is forward-looking in all jurisdictions CBL has been able to obtain information about³. A backward looking target like 2009 costs would be irrelevant and inappropriate in CBL's view, even if its 2009 costs was adjusted for 2009 inefficiencies. In CBL's opinion a glide path is a viable solution in principle if it is adequately implemented, i.e. the target rate is forward-looking and the duration is appropriate.

³ These jurisdictions include the U.K., The Netherlands, Kenya, Macedonia, Sweden, Norway, Spain Luxembourg and Portugal, amongst others.

Benchmarking RAIIO Charges

The level of service unit costs depends as much on methodology as on the point in time cost studies are carried out. In most instances, cost study updates lead to significantly decreasing fixed and mobile termination rates. If a benchmarking exercise were to be carried out, the timing of cost studies should be taken into account. Only countries that have recently updated their cost studies should be included. Furthermore, only jurisdictions using costing methodologies considered best practice should be part of the benchmark group. Finally, benchmarked countries should have similar characteristics as far as the main variables driving costs are concerned. All these constraints are likely to lead to a very small group of countries that are apt to be benchmarked. In this case the benchmarked rates would not be robust enough to form the basis for fixed or mobile termination rates. CBL believes that the benchmarking option does not meet any of the five criteria URCA sets out to assess the three options it describes.

Question 3: Please comment on URCA's proposed approach on setting BTC's RAIIO charges going forward.

In CBL's understanding, URCA intends to gradually move termination rates from today's levels to a target value of BTC's 2009 costs with a 2009/10 efficiency adjustment. URCA proposes to reach the target value in 2014/15 for fixed termination and in 2016/17 for mobile termination prices. While the proposed approach can be a step in the right direction, it is unclear to CBL how setting prices in 2017 at efficient 2009 cost levels achieves URCA's stated objectives, namely "to further the interests of consumers by promoting competition; and to further the interests of persons in The Bahamas in relation to the electronic communications sector". As is usually the case in other jurisdictions where glide paths are applied, it would be desirable to introduce a forward-looking element to URCA's approach on setting BTC's RAIIO charges going forward. Such a forward-looking element should take into account the expected efficiency gains between 2009 and 2014/15 or 2015/16 for fixed and mobile termination rates, respectively.

URCA may take account of an implicit efficiency gain assumption in the table below. If table values are in nominal terms, then the efficiency gain URCA assumes in the years it states is equal to the rate of inflation. Even if rates were in nominal terms, efficiency gains for years 2009/10-2012/13 are missing.

Table 4. Indicative RAIO charges for the period up to 2014/2015 (BSD cents / min)*

	Current RAIO	2012/13	2013/14	2014/15
<i>Fixed call termination</i>				
On-island service	1.98	1.03	0.92	0.92
Off-island service	2.65	1.63	1.47	1.47
<i>Mobile call termination</i>				
International traffic	7.24	5.52	4.80	4.16

* Subject to confirmation from BTC

Question 4: Please comment on the expected level of RAIO charges up to 2014/2015 based on URCA's proposed approach?

CBL believes that both fixed and mobile termination rates at any point in time covered by the glide path are excessive for the following reasons:

- Costs are based on BTC's separated accounts for 2009/10. Typically, cost-oriented termination rates decrease every year. Using outdated cost information is therefore likely to over-estimate cost-oriented prices for termination
- The efficiency adjustment to BTC's 2009/10 costs is too small because the efficiency study did not take account of the fact that BTC operates its domestic mobile business under a receiving-party-pays regime and therefore has no significant interconnection outpayments unlike the peer group it was benchmarked against. Furthermore, the efficient operator was defined as the median efficient operator instead of the top quartile efficient operator.
- There is no forward-looking efficiency adjustment to the rates. The glide path leads to 2009 efficient costs, assuming no efficiency gains between 2009 and 2014/15.
- If benchmarked against the jurisdictions which have conducted cost studies in the past two to three years, the proposed rates for both 2012/13 and 2014/15⁴ are amongst the highest of the benchmark countries selected by URCA.
- The duration of the glide path to achieve 2009 efficient cost is five years. Of the 15 countries we have examined, only the UK has implemented a 5-year glide path. All other countries implemented shorter glide paths, the average being three years. It's worth noting that the glide paths are not comparable with URCA's proposal as the

⁴ Compared with the benchmark countries announced 2014/15 rates where available, instead of current rates in the benchmark countries as in URCA's charts.

glide paths lead to forward looking estimates of costs for the year the glide path ends. In CBL's view, the mobile termination rate glide path duration is excessive and should be set to three years like the fixed termination rate glide path.

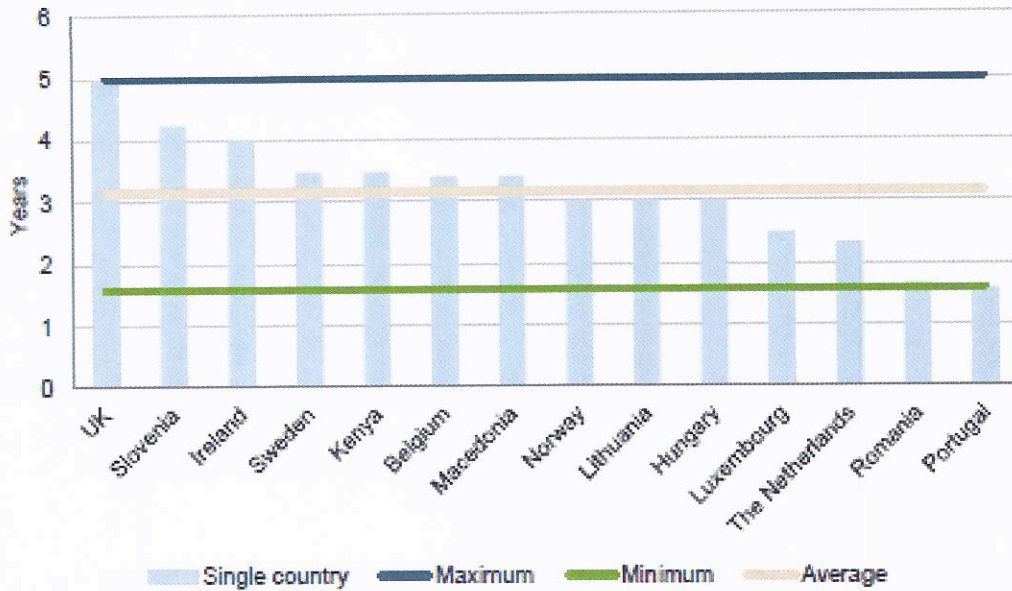


Table 1: Glide path length – source: Analysys Mason based on NRA information

The following figure shows the perceptual reduction set in the glide path per year. The maximum reduction each year has been increasing from 13% in 2007 to 55% in 2012. The average decrease has been around 16% per year.

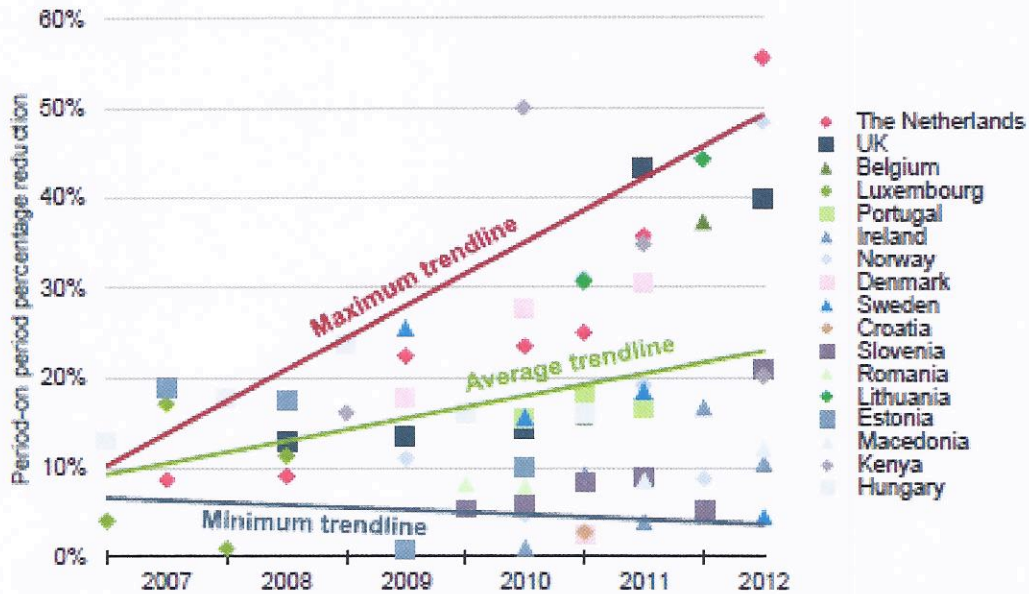
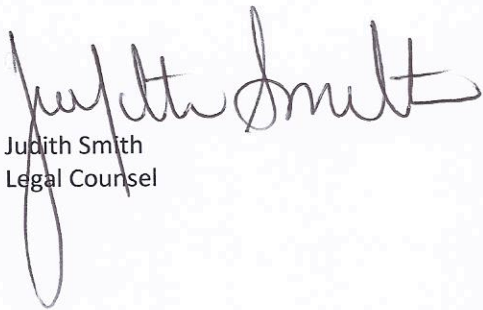


Table 2: Glide path reduction in MTRs per year – source: Analysys Mason based on NRA information

Additional Consideration

URCA in this consultation has focused on efficiently incurred cost as borne out by BTC's accounting separation results. There is also a structural aspect to consider. In the RAIO Final Decision, URCA approved two Pols and indicated that other Pols could be added if it economically and technically feasible. It is unclear who has to satisfy the burden. In order to deliver a call from a fixed to a mobile phone, the call must transit over BTC's fixed network, PoI. BTC's charges a transit fee. A direct PoI between the fixed and the mobile network would obviate the transit fee. Therefore implicit in the structure of BTC's network would seem to be a cost although unnecessary would be subject to an efficiency adjustment, when the ultimate efficiency would be a direct PoI between the mobile and fixed networks. It is CBL's contention that BTC should be disincentivized to create 'unnecessary' costs.

Respectfully Submitted:

A handwritten signature in black ink, appearing to read "Judith Smith". The signature is written in a cursive style with a large loop at the end.

Judith Smith
Legal Counsel