



# **GUIDELINES FOR CALCULATING THE NET COST OF THE UNIVERSAL SERVICE OBLIGATIONS FOR THE BAHAMAS TELECOMMUNICATIONS COMPANY LIMITED**

**STATEMENT OF RESULTS AND FINAL DECISION**

**ECS 09/2015**

**31 DECEMBER 2015**

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## 1. INTRODUCTION

The Utilities Regulation and Competition Authority (URCA) issues this Statement of Results pursuant to section 119(1) and Schedule 5 of the Communications Act, 2009 (Comms Act).<sup>1</sup> This Statement of Results forms part of the consultative process regarding how The Bahamas Telecommunications Company Limited (BTC) is to calculate the net cost of the universal service obligations (USO) as contemplated in section 44(3) of the Comms Act.

The consultation for this subject was launched in August 2014, with the publication of URCA's consultation document "Guidelines for Calculating The Net Cost Of The Universal Service Obligations For The Bahamas Telecommunications Company" [URCA document reference ECS 15/2014]<sup>2</sup> (BTC's NAC Guidelines).

Comments were duly forwarded by both BTC and Cable Bahamas Limited (CBL) on behalf of itself and its affiliates Caribbean Crossings Ltd. and Systems Resource Group Ltd. CBL's comments on ECS 15/2014 also included its responses to the public consultation on "Guidelines for Calculating The Net Cost Of The Universal Service Obligations For Cable Bahamas Limited" [URCA document reference ECS 16/2014]<sup>3</sup> (CBL's NAC Guidelines). This Statement of Results provides a summary of the comments that were received from BTC and CBL to ECS 15/2014 along with URCA's responses to those comments and its final decisions. URCA wishes to thank both BTC and CBL for their responses to the consultation document. A copy of the responses from BTC and CBL to ECS 15/2014 (including CBL's responses to ECS 16/2014) can be downloaded from URCA's website at [www.urbahamas.bs](http://www.urbahamas.bs).

While URCA has sought to respond directly to comments and representations received during the consultation process, URCA expressly states that any failure by URCA to respond in this document to any issue raised by the respondents does not necessarily signify agreement in whole or in part with said issue, that it has not considered the comment or that it considers the comment to be without merit. The publication of this Statement of Results brings to an end URCA's public engagement on the Guidelines for calculating the net avoidable cost (NAC) of the USOs for BTC and will result in the publication of the Final NAC Guidelines for BTC [ECS 10/2015].

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<sup>1</sup> <http://www.urbahamas.bs/download/088554800.pdf>

<sup>2</sup> <http://www.urbahamas.bs/download/071866900.pdf>

<sup>3</sup> <http://www.urbahamas.bs/download/071879800.pdf>

## **STRUCTURE OF THE REMAINDER OF THIS DOCUMENT**

The format of the remainder of this document is as follows:

- Section 2** Summary of comments that were put forth by BTC along with responses from URCA and the final decisions
- Section 3** Summary of comments that were put forth by CBL along with responses from URCA and the final decisions
- Section 4** Outline of the subsequent activities that will be undertaken by URCA as it relates to the Universal Service Obligations (USO) for BTC

## **2. BTC's RESPONSES TO THE CONSULTATION DOCUMENT**

In this Section, URCA summarises and responds to the substantive comments received from BTC on the consultation document, as follows:

- Section 2.1 - Summary of General Comments to the Consultation Document
- Section 2.2 - Summary of Comments to Specific Topics within the Consultation Document [ECS 15/2014]

### **2.1 Summary of General Comments to the Consultation Document**

#### **2.1.1 Data sources**

BTC emphasized the importance of reasonable figures being used to estimate the net cost of the USO. BTC indicated that many of the figures will be derived from BTC's accounting and operational systems which were designed to meet other purposes that may not satisfy requirements for the estimating of net costs. BTC noted that some of the data used to justify claims for universal funding may have to be estimates based on a number of assumptions.

#### **URCA's response**

While URCA accepts that BTC may adopt slightly different approaches in implementation to those suggested by URCA, the NAC Guidelines were drafted with consideration given to the cost accounting system which is currently used by BTC. URCA understands the limitations associated with using fully allocated costs based on historical cost accounting for the purposes of estimating net costs. Bearing this in mind, URCA has stated that estimates should be made where appropriate. Any estimates made by BTC will have to be suitably justified.

URCA's proposal to calculate the net cost of USO services at the level of individual islands is the preferred approach having duly considered the various options. URCA emphasises that this level of analysis is not only pertinent in so far as it is consistent with the presumption that an operator would make its initial decisions about entering the market at an island level, but that it also reflects the technical organisation of the communications network of an operator.

However, URCA acknowledges that it might not always be feasible for BTC to calculate net cost at the level of individual islands. URCA notes that BTC has not opted to make use of the proposals which were put forth by URCA regarding the estimation of avoidable costs. URCA reminds BTC that the universal service provider (USP) is responsible for the quantification of the net cost of the USO as a first step before URCA can consider whether the estimated net cost of the USO constitutes an unfair financial burden on the USP and whether compensation is required.

The consultation document [ECS 15/2014] proposed what URCA considers to be the best possible approach to the calculation of net costs. Any methodological approach that is utilised by the USP in

support of their claim for compensation from the universal service fund (USF) will be critically reviewed for its robustness. BTC will of course be expected to provide evidence to URCA to justify any costing methodology that differs from that which has been presented as the preferred approach.

### **URCA's final decision**

**The BTC NAC Guidelines which have been proposed by URCA are indicative. BTC may very well determine elements of the net cost of its USO using slightly different approaches that are sufficiently robust, transparent, verifiable and consistent with the principles set out in the Final NAC Guidelines for BTC [ECS 10/2015].**

#### **2.1.2 Basic internet services**

BTC referred to its universal service obligations as per Schedule 5 of the Comms Act. BTC then noted that the provision of broadband services has since been revolutionized. BTC questioned how its existing (interim) internet USO should now be viewed and how costs should be estimated today.

### **URCA's response**

URCA reminds BTC of URCA's final decision on BTC's internet USO in the "Framework for the Clarification and Implementation of Existing Universal Service Obligations (USO) under Section 119 and Schedule 5 of the Communications Act 2009" [ECS 01/ 2013].<sup>4</sup> Section 4.6 of that document outlines what BTC should do in the event that it ceases to provide dial-up internet service as a result of network transformation. In that instance, BTC is still required to meet its obligations and must propose an appropriate substitute service with which it would meet the obligation, and obtain URCA's prior approval to any change in the services it provides in fulfilment of its internet USO.

To date, URCA has not been made aware by BTC of an appropriate substitute service that BTC intends to provide instead of dial-up internet service as part of its USOs. URCA is cognisant that dial-up internet service as set out in the obligation would represent outdated technology which is not consistent with global efforts to achieve ubiquitous broadband access. URCA is currently reviewing the dial-up USO having regard to these developments, and in the meantime encourages BTC to consider broadband technologies as appropriate substitutes for dial-up. URCA would welcome such an approach by BTC, subject to including all appropriate costs in considering the NAC of providing BTC's dial-up USO.

### **URCA's final decision**

**BTC remains responsible for the provision of basic dial-up internet services to all populated areas and basic dial-up internet services free of charge to specified institutions, as per section 119(1) and Schedule 5 of the Comms Act. The cost of the provision of said services should be based on past records.**

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<sup>4</sup> <http://www.urcabahamas.bs/download/012155400.pdf>

**BTC should formally inform URCA of the internet service (including upload/download speeds) that it intends to provide to populated areas and specified institutions in the absence of dial-up internet service.**

### **2.1.3 Intangible benefits**

BTC believes that URCA has adopted an approach to intangible benefits that is taken by other regulatory bodies without having first assessed the relevance of said approach to The Bahamas.

That said, BTC supported URCA's intent to ensure that the calculation of intangible benefits is based on an objective and transparent approach. However, it did not agree that the calculation of intangible benefits should extend to other services such as mobile telephony. BTC disagreed with URCA's position that BTC's status as a universal service provider is an advantage in the mobile market. BTC believes that in many key segments it may be disadvantaged because of the perceived association of BTC with "outdated" services (e.g., payphones). BTC also believes that its role as a universal service provider is not a "unique selling proposition" and therefore has not conferred any competitive advantage of value as it relates to intangible benefits. BTC posited that there is no competitive value to intangible benefits.

Furthermore, BTC suggested that the presence of two universal service providers reduces any competitive advantage that may exist due to the designation of universal service provider.

BTC indicated that a distinction must be made between the intangible benefits provided by the universal service designation and the intangible benefits provided by other factors (e.g., longevity and past government ownership). BTC is of the opinion that any intangible benefits that are included must be due solely to the USO requirement. BTC further stated that any intangible benefits that result from other aspects (e.g., market dominance, size) should be excluded.

While BTC was pleased that URCA has excluded the life cycle and marketing estimates from intangible benefits, it did not agree that other intangible benefits are material.

### **URCA's response**

URCA acknowledges that the scope of intangible benefits is much broader in the European Union than in The Bahamas. However, where BTC believes intangible benefits are immaterial, it is for BTC to demonstrate why that may be the case. Intangible benefits have been included due to the comparative advantage that a USP may derive (e.g., lower costs as a result of higher volumes, higher revenues, better customer acquisition and retention). URCA considers that the inclusion of specific intangible benefits for the purposes of calculating net costs is relevant to USPs in any commercial market regardless of locale. Enhanced brand value and ubiquity were specifically determined as being relevant to the determination of the net cost of the USO due to their importance to the Bahamian market and their direct applicability to the universal service provider designation.

Intangible benefits relating to mobile services were contemplated by URCA due to possible demand complementarities. In URCA's view, BTC may possibly experience increased sales of mobile products

due to it being a complementary product to fixed line USO services. Although the introduction of a second mobile service provider may reduce the impact of this intangible benefit, BTC still stands to possibly gain more mobile customers that it would have otherwise gained in the absence of its provision of fixed line USO services. While the “key youth segment” may not pay for the fixed line product in their household, both they and fixed line account holders may be inclined to also purchase mobile services from BTC due to familiarity with BTC as a service provider. Similar logic applies to the issue of replacement calls, an issue that was raised by BTC. BTC is, in URCA’s view, more than aware that replacement calls are more than likely made on its mobile network. That inclination on the part of the customer is considered by URCA to be a very clear intangible benefit. URCA does not believe that BTC is in any way disadvantaged because of a perceived association with services like payphones.

URCA acknowledges that BTC might not have a “unique selling proposition” as there are two universal service providers. However, as it specifically relates to the provision of fixed line telephony universal service obligations BTC is in a unique position to gain from intangible benefits that are associated with that role. The competitive value of intangible benefits may, in URCA’s view, be zero only in instances where the exact same service is being offered by more than one universal service provider in the same location.

#### **URCA’s final decision**

**Consideration of the intangible benefits as identified by URCA in BTC’s NAC Guidelines should be made by BTC when preparing net avoidable cost estimates for funding from the USF.**

### **2.2 Summary of Comments to Specific Topics within the Consultation Document**

#### **2.2.1 Methodology documented in these guidelines**

BTC suggested that the third bullet point in Section 1.2.1 on page 3 of the consultation document [ECS 15/2014] would be better expressed as ‘Revenues foregone’ as opposed to “Revenues to be made”.

#### **URCA’s response**

URCA agrees that the wording of this particular bullet point should be changed to “Revenues foregone” instead of ‘Revenues to be made’.

As it relates to the universal service obligations, the provision of a service to the specified institutions will automatically create a net cost as there is no foregone revenue that will offset the overall cost of offering the service for free.

#### **URCA’s final decision**

**The wording of the bullet point in question will be changed to read as follows:**

***“revenues foregone in serving specified institutions on both economic and uneconomic islands; and ...”***



**In addition, other editorial revisions will be made throughout the Guidelines as appropriate.**

### **2.2.2 Critical elements of a net cost calculation**

BTC disagreed that net cost calculations should be adjusted to reflect the costs of a new operator. Instead, BTC believes that the determination as to whether investment costs due to the universal service obligation were efficient at the time that they were made is most important.

In BTC's opinion, URCA has confused the aims of universal service funding with the aims of wholesale service costing. BTC further states that it is important for URCA to note the effect of stating access costs using historical cost accounting (HCA) versus current cost accounting (CCA).

BTC further suggests that URCA should clarify that efficiency adjustments are not needed as a consequence of using HCA valuations.

#### **URCA's response**

URCA notes that its consultation document [ECS 15/2014] and final decision [ECS 01/2013] specifically addressed this concern.

It remains URCA's position that in order to obtain a true estimate of the net cost of the USO, the level of avoidable costs should reflect the latest and most efficient technology with an optimal network configuration. That is to say, a network operated by a new entrant would have to effectively compete with established market players who may or may not have previously held a monopoly position. The incumbent service providers were, to URCA's knowledge, therefore never strictly bound by normal market pressure to be as efficient as possible. Costs under such optimal configuration can be derived from bottom-up cost models which can produce estimates of long run incremental cost (LRIC) of activities/products. LRIC is in fact the preferred cost modelling approach.

It is of the utmost importance that the universal services be provided in a manner that is efficient (i.e., at least cost) in order to maximize economic welfare and therefore provide the most benefit to customers.

URCA recognizes that costs valued on an HCA basis do not depict the costs of a new entrant or efficient costs as best practice would require. Costs valued on a CCA basis are recognized as being superior. The consultation document stated that BTC's NAC Guidelines can be applied with either a HCA or CCA approach given that BTC's existing cost accounting records are on a fully allocated costs based on historical cost accounting basis. URCA accepts that costs will be valued using fully allocated costs (FAC) based on historical cost accounting for the purpose of the net cost of the USO calculation.

As such, efficiency adjustments to estimates using FAC based on HCA should be made for efficiency as appropriate.

Given the above, URCA considers that BTC is mistaken in its belief that URCA has confused the aims of universal service funding with the aims of wholesale service costing.

### **URCA's final decision**

**Efficiency adjustments will be to estimates for the net cost of the universal service obligations using fully allocated costs based on historical cost accounting.**

#### **2.2.3 Analysis at island level**

BTC does not believe that URCA's suggestion to assess the net cost of providing universal service in uneconomic areas at the island level is appropriate. BTC stated that "reasonable and defensible" zones should be chosen by the universal service provider.

BTC proposed to analyse the net cost on the basis of exchange area (Main Distribution Frame- MDF) or by cabinet.

### **URCA's response**

URCA is of the view that the net cost of the USO should be assessed at the island level. As previously stated, this level of analysis is not only pertinent insofar as it is consistent with the presumption that an operator would make its initial decisions about entering the market at an island level, but that it also reflects the technical organisation of the communications network of an operator.

BTC's arguments do not satisfy URCA that assessing costs by island may not be appropriate and in URCA's view may result in an underestimate of the net cost associated with BTC's universal service obligations.

### **URCA's final decision**

**The BTC NAC Guidelines which have been proposed by URCA are indicative. BTC may very well determine elements of the net cost of its USO using slightly different approaches that are sufficiently robust, transparent, verifiable and consistent with the principles set out in the Final NAC Guidelines for BTC [ECS 10/2015].**

#### **2.2.4 Avoidable costs absent the USO**

BTC suggested that the cost of all network elements that are required to provide fixed services to uneconomic islands should be included in the net cost calculations. BTC is also of the opinion that URCA should confirm that the aforementioned costs are to include those that are relevant for the provision of broadband services.

BTC does not think that costs which are common to managing all islands should be treated as unavoidable. BTC feels that this approach would only be defensible if LRIC is used to derive costs. BTC notes that URCA has proposed that FAC be used for estimating the net costs of universal service. Under this approach, each network element is allocated a share of common costs. If a network element is deemed avoidable in relation to the provision of universal service costs then all costs associated with that network element, including its share of common costs becomes avoidable. BTC

states that not taking into account all costs associated with the network element would “erroneously” incorporate long run incremental costing (LRIC) principles into what otherwise should be limited to FAC.

### **URCA’s response**

URCA is of the opinion that BTC’s separated accounts include an allocation of costs to network components and services that can be separated in terms of being avoidable or unavoidable for the purposes of the USO. Even if the FAC method is used in strict adherence to the concept, an adjustment should be made to the final estimate to account for that method’s limitations as compared to CCA, which would be considered superior in the evaluation of the true avoidable costs of the USO.

As to BTC’s comment regarding broadband, URCA considers that only revenues and costs of services provided over the fixed access network that are applicable to BTC’s universal service obligations should be taken into account when assessing the net cost of the provision of universal services. As stated above, BTC is free to satisfy its dial-up USO through the provision of broadband internet access, which URCA would accept and encourage as a substitute. In such circumstances, BTC would be permitted to include the cost of providing such broadband services.

### **URCA’s final decision**

**BTC may only include the cost of providing broadband if it provides USO internet service via broadband.**

**FAC is only being allowed for the purpose of estimating net cost because the universal service providers do not currently make use of any other cost accounting method. FAC is not the preferred regulatory approach for estimating common and joint costs. While it is important that BTC takes a consistent approach to its estimates, strict adherence to fully allocated costing methods specifically as it relates to joint and common costs is not advisable.**

#### **2.2.5 Variations in cost of providing access by zone**

BTC indicated that universal service providers in other countries use geozones to approximate the costs of providing service in areas that differ in access network costs due to topographical qualities. BTC stated that it intends to make its own proposals regarding the selection of “subdivisions”.

BTC also added that the use of bottom-up cost models may not be necessary or appropriate where BTC can use actual data.

### **URCA’s response**

See URCA’s previous responses to these proposals in Section 2.2.3 of this document.

### URCA's final decision

The BTC NAC Guidelines which have been proposed by URCA are indicative. BTC may very well determine elements of the net cost of its USO using slightly different approaches that are sufficiently robust, transparent, verifiable and consistent with the principles set out in the Final NAC Guidelines for BTC [ECS 10/2015].

#### **2.2.6 Cost of providing communications services over subscriber lines**

BTC does not consider the use of line traffic to be an appropriate measure for the derivation of access network costs. BTC stated that the length of access lines is the driver of costs in the access network and therefore proposes that loop length be used as the main measure of cost.

### URCA's response

URCA accepts that BTC may adopt approaches in implementation that differ from those that are suggested in the guidelines because of data availability or technical requirements provided that the approaches remain consistent with the principles set out in the Final NAC Guidelines for BTC.

### URCA's final decision

**BTC may adopt approaches in implementation that differ from those that are suggested in the BTC NAC Guidelines because of data availability or technical requirements provided that the approaches remain consistent with the principles set out in the Final NAC Guidelines for BTC [ECS 10/2015].**

#### **2.2.7 Revenues absent the USO**

BTC suggested that it may be able to provide actual data (as opposed to averages) for uneconomic areas depending on how the geographic zones are split. BTC noted that this information would clearly be more accurate than the use of averages.

BTC indicated that it does not have revenue data for 56 kbps dial-up service as this service is no longer provided. Internet and broadband revenues are now treated as a single category by BTC.

BTC found it surprising that URCA did not include replacement calls in its proposals for calculations as seen with other regulatory bodies (i.e., Belgium, Ireland, Italy and Spain). BTC noted that the value of replacement calls should be offset against foregone revenue because the calls would take place if the USO was not in force. BTC proposed to ignore replacement calls on the fixed network but include an estimate for the net revenue from replacement calls on the mobile network in its submission for universal service funding.

### URCA's response

URCA is not opposed to the use of actual data where applicable by BTC to inform its net cost estimate. It is expected that actual costs as taken from the BTC separated accounts will be used if available. The BTC NAC Guidelines were written with consideration given to the information that is currently available to BTC.

BTC is encouraged to provide USO internet services via broadband. Formal notification of the proposed USO internet service via broadband must be submitted to URCA for consideration. Note that the ECS Policy speaks only to the provision of broadband internet services. BTC must obtain URCA's prior approval to any change in the services it provides in fulfilment of its internet USO. URCA is not in possession of any information which indicates that BTC no longer intends to fulfil its universal service obligation to provide dial-up internet services.

URCA acknowledges BTC's point regarding the inclusion of replacement calls. In theory, replacement calls increase the net cost of the USO; however replacement revenues from USO customers using other fixed lines is unlikely. Replacement revenues from mobile could be considered for the period during which BTC remains the monopoly provider of mobile. URCA has elected not to include replacement calls for the purposes of calculating net costs as there is unlikely to be any actual data in support of this proposition.

#### **URCA's final decision**

**The BTC NAC Guidelines which have been proposed by URCA are indicative. BTC may very well determine elements of the net cost of its USO using slightly different approaches that are sufficiently robust, transparent, verifiable and consistent with the principles set out in the Final BTC NAC Guidelines.**

BTC is encouraged to provide USO internet services via broadband. Formal notification of the proposed USO internet service via broadband must be submitted to URCA for consideration.

#### **2.2.8 Foregone revenues from public pay apparatus**

BTC maintained the position that since payphones do not carry advertising there are no revenues to be included in the universal service obligations calculations for public pay apparatus.

#### **URCA's response**

URCA clarifies that possible advertising revenue was only to be considered in addition to the fee that users of payphones pay to make a call. If public payphones do not carry advertisements then only the revenue that BTC makes per call should be included in the values that will feed into the wider foregone revenue estimation.

#### **URCA's final decision**

**Revenue from calls that are placed on public pay apparatus should be included in the net cost estimates for universal service obligations.**

### **2.2.9 Summary of critical elements of approach**

BTC sought clarification on what is meant by the term “Wholesale revenues from access, outgoing calls and ancillary services as applicable” in Table 3 of the consultation document. BTC suggested that the line be deleted.

#### **URCA’s response**

URCA clarifies that wholesale revenue from access, outgoing calls and ancillary services, as applicable, refers to any revenue that BTC may earn from providing network access services. This would include local loop unbundling (LLU) or wholesale line rental (WLR) revenues.

#### **URCA’s final decision**

**The heading will remain in the table for consideration by the USP when applying for funding from the USF.**

### **2.2.10 Definition of uneconomic customers**

BTC indicated that it does not compile data at the level of individual customers or access lines. BTC suggests that a proxy must be used for the purposes of determining the cost of uneconomic customers in economic islands. BTC proposes to use loop length (as measured by capacitance) to determine the cost of uneconomic customers.

#### **URCA’s response and final decision**

**URCA accepts that BTC may adopt approaches in implementation that differ slightly from those that are suggested in the BTC NAC Guidelines because of data availability or technical requirements provided that the approaches remain consistent with the principles set out in the Final NAC Guidelines for BTC.**

### **2.2.11 Foregone revenue absent the USO**

BTC reiterated that it intends to include all revenues related to the provision of the access network inclusive of those related to broadband services. However, BTC considers that the use of averages for customer revenues will not suitably identify the differences in the distribution of customer revenues. BTC therefore intends to use more detailed information on the distribution of customer revenues.

#### **URCA’s response**

BTC should use cost information from elements of its network that are relative to its universal service obligations. This then would be to the exclusion of any cost or revenue information related to broadband services. With that said, BTC may only include the cost of providing broadband if it elects to provide USO internet services via broadband.

As noted in the consultation document, URCA accepts that BTC may adopt slightly different approaches in implementation to those suggested in the BTC NAC Guidelines because of data availability or technical requirements. If BTC is inclined to use “more detailed information” for the purposes of calculating foregone revenues absent the USO, it may do so provided that its approach remains consistent with the principles set out in the Final BTC NAC Guidelines.

### **URCA’s final decision**

**Broadband services are not to be included in net cost estimates for the provision of USO if BTC is not providing broadband internet services as a USO. BTC may only include the cost of providing broadband if it elects to provide internet USO service via broadband.**

**The BTC NAC Guidelines which have been proposed by URCA are indicative. BTC may very well determine elements of the net cost of its USO using a different approach so long as that approach is sufficiently robust and consistent with the principles set out in the Final BTC NAC Guidelines.**

#### **2.2.12 Net cost of special tariffs to specified institutions**

BTC expressed the view that under the Communications Act, CBL is required to provide free internet services to the specified institutions. BTC indicated that it believes its obligation is to only provide 56 kbps dial-up service in areas where CBL does not have coverage.

BTC contends that it will exclude institutions that are served by CBL’s universal service obligations from its assessment of foregone revenues absent the USO. BTC has indicated that it may need URCA’s assistance in obtaining information as to which institutions are being served by CBL’s universal service obligation.

### **URCA’s response**

URCA considers it necessary to clarify BTC’s universal service obligation as it relates to the provision of dial-up internet service to specified institutions as per the Communications Act. Section 119 (1) and Schedule 5 of the Comms Act imposes an internet obligation on both BTC and CBL. BTC is a designated universal service provider for basic dial-up internet services free of charge to specified institutions regardless of coverage provided by CBL. This issue was addressed by URCA in ECS 01/2013.

BTC should not exclude institutions that are served by CBL’s universal service obligation from its assessment of foregone revenues absent the USO. URCA considers that providing BTC with information regarding which specified institutions are served by CBL’s universal service obligation is not required under the Comms Act and is irrelevant to the discharge by BTC of its own statutory internet USO.

### **URCA's final decision**

**BTC remains responsible for the provision of basic dial-up internet services to all populated areas and basic dial-up internet services free of charge to specified institutions, as per section 119(1) and Schedule 5 of the Comms Act. BTC is encouraged to provide USO internet services via broadband. Formal notification of the proposed USO internet service via broadband must be submitted to URCA for consideration.**

#### **2.2.13 Net cost of special tariffs**

BTC did not agree with URCA's suggestion in Section 4.2 of the consultation document to reduce the estimate of revenues foregone for the provision of internet services to special institutions due to elasticity of demand. BTC is of the opinion that this adjustment would not be appropriate for dial-up service. BTC went on to state that in cases where the dial-up service is assigned to a telephone number on the same island, the marginal price to the user of extra internet services is zero, and the usage – and the revenue foregone – would be the same whether or not the service is provided free of charge or priced at the prevailing commercial rates.

### **URCA's response**

By way of clarification, URCA considers that in the absence of universal service, there would undoubtedly still be some specified institutions that would subscribe to paid internet services. Therefore, URCA is of the view that BTC cannot use estimates to suggest that they are giving up revenue from all of the specified institutions in question. There will undoubtedly always be some institutions that will subscribe to internet services regardless of market price. In that sense, the demand is more or less inelastic. This however is a loose interpretation of the principle for the purposes of this document. URCA understands BTC's concern with the use of the concept of price elasticity in a strict sense and will revise the wording in the applicable Section of BTC's Final NAC Guidelines accordingly.

As it specifically relates to the provision of dial-up internet services, although the service is provided over a fixed telephone line with 'unlimited' local calling plans, the dial-up internet service is not free. BTC makes/made revenue from the provision of that service by way of monthly rental charges for the modem which was required to access the internet. Though the marginal cost of providing dial-up internet service may have been zero for BTC, there was still revenue that was made.

### **URCA's final decision**

**BTC should take into consideration the fact that there will always be specified institutions that will subscribe to internet services at the prevailing market price.**



### **2.2.14 Net cost of public payphones on economic islands**

BTC outlined that it does not collect cost information for individual payphones by economic or uneconomic island. BTC indicates that it is likely to estimate the cost of public pay apparatus using a nationwide average.

#### **URCA's response and final decision**

**URCA stresses that BTC may adopt approaches in implementation that differ slightly from those that are suggested in the BTC NAC Guidelines because of data availability or technical requirements provided that the approaches remain consistent with the principles set out in the Final BTC NAC Guidelines.**

### **2.2.15 Need to adjust for cost efficiency**

BTC considered the possible adjustment to USO costs in order to reflect annual efficiency gains misplaced for two reasons. The first reason given by BTC is that the adjustment is forward looking whereas compensation for the USO is based on costs that were incurred in the past. Secondly, BTC feels that efficiency adjustments should be made to correct for inefficient decisions that were taken when the USO investments were made and not for supposed inefficiencies in the present.

BTC noted that an efficiency adjustment based on a line fault index would be more appropriate than one based on URCA's previous efficiency analyses.

#### **URCA's response**

The need to adjust actual costs in order to ensure that the net cost of the USO reflects efficient costs was decided by URCA in ECS 01/2013.

Best practice dictates that CCA be used to depict the costs that a new operator would face in order to efficiently provide a service in the present day. That is to say, a network operated by a new entrant would have to effectively compete with established market players who may or may not have previously held a monopoly position and were therefore never strictly bound by normal market pressure to be as efficient as possible. The costs are forward looking because URCA seeks to determine present day costs of providing services based on the applicable costs of network elements that were incurred in the past. That is the very nature of the extrapolation. The basic idea is to determine how much it will cost to provide the proposed services using elements of the existing network. Specific efficiency adjustments are necessary because BTC does not have cost/revenue data in CCA format. Instead, BTC uses FAC based on an HCA basis. The method currently used by BTC does not provide a true estimate of the present day efficient net cost of the USO.

It is of the utmost importance that the provision of universal services be provided in a manner that is efficient (i.e., at least cost) in order to maximize economic welfare and therefore provide the most benefit to customers.

### **URCA's final decision**

**Adjustments for efficiency should be made as outlined in the Final BTC NAC Guidelines.**

#### **2.2.16 Enhanced brand value**

BTC considered URCA's proposal to calculate the value of BTC's brand as 10% of its expenditure on advertising and marketing as flawed for the following reasons:

- BTC held that URCA's suggestion does not distinguish between the value of the BTC brand that is solely due to the USO versus other factors such as service quality, price position, size of operation and company history.
- BTC opined that the value of 10% does not take into account BTC's opinion that the USO does not provide any competitive advantage on islands where both BTC and CBL are present.
- BTC felt that the use of 10% of the advertising and marketing expenditure as a proxy for brand value is an attempt to relate a capital sum to an annual flow of expenditure.
- BTC suggested that some other national regulatory bodies regard the method of relating brand value to annual expenditure on advertising and marketing as inferior.

BTC maintained that even if advertising and marketing expenditure is used as a proxy for brand value on the grounds of simplicity, the rate of 10% is not justified. BTC finds this number to be arbitrary and believes that it should be reduced substantially to no more than 1%.

Furthermore, BTC considered that a proxy of this sort should only be taken from the budget used to market fixed services. BTC finds it difficult to see how the provision of services like landlines and payphones would assist BTC in appealing to key segments of the mobile market.

### **URCA's response**

Having regard to the arguments made in ECS 01/2013, in which URCA used international benchmarks (suitably adjusted) to arrive at the proposed value of 10%, and having considered BTC's comments, URCA is of the view that quantifying enhanced brand value as 5% of advertising and marketing expenditure would be suitable to The Bahamas.

### **URCA's final decision**

**Enhanced brand value should be calculated at 5% of advertising and marketing expenditure.**

#### **2.2.17 Ubiquity**

BTC accepted that some customers who relocate from uneconomic to economic islands may choose BTC over CBL as a result of BTC's role as a USP for telephony and internet services. However, BTC reiterated the viewpoint that any advantages that it may gain from being a USP are reduced on islands that are serviced by both CBL and BTC.

BTC proposes to use domestic migration data as published by the Department of Statistics in order to estimate the rate of migration from uneconomic to economic islands. This value can then be adjusted using the fixed telephony penetration rate in order to estimate the number of BTC fixed line subscribers that move to economic islands.

Using the previous estimate, BTC then intends to calculate the number of subscribers that are likely to renew their subscription with BTC using its market share as a proxy. BTC intends to utilize a probability factor to reflect the importance of the USO compared to other factors such as size, history, superior prices, products and services.

Finally BTC suggested that a value be placed on customer retention due to ubiquity. BTC proposes to measure this value by the difference in the average cost per line between uneconomic and economic islands. BTC noted that several European regulatory agencies have found that the benefits of ubiquity are negligible.

#### **URCA's response**

URCA does not agree that BTC's USP advantage as it relates to ubiquity (as an intangible benefit) is reduced on islands that are serviced by both CBL and BTC. BTC is known by consumers for having national coverage. There is no other electronic communications provider with the same span in terms of provision in the country.

As it relates to customer migration, URCA reiterates that BTC may adopt approaches in implementation that differ slightly from those that are suggested in the Final BTC NAC Guidelines because of data availability or technical requirements provided that the approaches remain consistent with the principles set out in those Guidelines

#### **URCA's final decision**

**The BTC NAC Guidelines which have been proposed by URCA are indicative. BTC may very well determine elements of the net cost of its USO using a different approach as long as that approach is sufficiently robust and consistent with the principles set out in the Final BTC NAC Guidelines.**

#### **2.2.18 Life cycle benefits**

BTC supported URCA's proposal to exclude life cycle benefits from USO calculations.

#### **URCA's response**

URCA considers that this benefit is already captured in the estimated net cost of the USO if the analysis is done at an island level.

#### **URCA's final decision**

**Life cycle benefits should be excluded from estimates for net cost of the USO if the analysis is done at an island level.**

### **2.2.19 Marketing**

BTC supported URCA's proposal to exclude marketing benefits from USO calculations.

#### **URCA's response**

URCA notes BTC's response.

#### **URCA's final decision**

**Marketing benefits are to be excluded from USO net cost estimates.**

### **2.2.20 Timing**

BTC suggested that URCA set out a schedule and procedure for processing USO applications and making a final decision. BTC notes that this will enable the operators to plan their cash flows as well as provide greater transparency with respect to the process.

BTC appreciates that a proposed schedule will be considered indicative until all stakeholders have gained practical experience of USO applications.

#### **URCA's response**

URCA is not opposed to establishing timelines for the administration of the application for funding from the USF. However, that issue is outside of the scope of this document and will be addressed during the development of operating procedures for the USF. URCA proposes to give an indicative timetable when an application is made by the USP.

#### **URCA's final decision**

**Timelines for the administration of USO funding applications will be contemplated during the development of operating procedures for the USF.**

### **2.2.21 Unfair financial burden**

BTC has previously expressed its concerns about the use of a market share as a measure of whether a USP can bear the financial burden of the USO. BTC notes that few other national regulatory authorities have taken this approach. However, BTC welcomes URCA's clarification that the relevant market is the access market share. BTC considers that its market share in the access market is below 80%.

BTC supports in principle URCA's proposal to assess whether the value of the net transfer to the USP is disproportionate to the cost of administering the fund. However, it believes that URCA should define the term 'disproportionate' as it relates to this exercise. BTC believes that this assessment which is to be done by URCA should only apply if the cost of administering the fund exceeds the net transfer.

In addition, BTC considers that mobile activities should be excluded from any calculations that URCA may use to test whether the USO is an unfair financial burden. At present, BTC's mobile business may cross subsidise its fixed network business. This cross subsidy is likely to be removed through the introduction of competition in the mobile market. BTC stresses the importance of judging the profitability of the fixed line business when assessing whether the USO costs present an unfair financial burden.

Finally, BTC notes that perhaps the most important change will be the imminent introduction of competition in the mobile market. In BTC's opinion this will likely have a major impact on BTC's margins and on its ability to fund its USO in the future.

#### **URCA's response**

URCA notes BTC's response, but questions the assertion that its applicable market share is below 80%. URCA has statutory responsibility for deciding how it will assess whether an unfair burden exists according to circumstances that currently exist and changes that are expected to occur.

URCA will consider all licensed activities in the event that it has to determine a fair rate on capital employed (ROCE). Mindful of the limitations associated with a static view of a USP's profitability, URCA will also conduct an assessment of a number of other criteria (as indicated in the consultation document) that contribute to a USP's ability to sustain a USO positive net cost.

#### **URCA's final decision**

**URCA will consider all licensed activities of BTC when determining BTC's ability to fund its USO.**

### 3. CBL's RESPONSES TO THE CONSULTATION DOCUMENT

In this Section, URCA summarises and responds to the substantive comments received from CBL on the consultation document [ECS 15/2014].

#### 3.1 Tariff Rebalancing

At Section 3.1 of its response, CBL referenced its June 29, 2012 response to URCA's Consultation Document on the "Framework for the Clarification and Implementation of Existing Universal Service Obligations (USO) under Section 119 and Schedule 5 of the Communications Act 2009" [ECS 12/2012].<sup>5</sup> In that response, CBL noted that it was seriously concerned with the absence of any discussion regarding the perceived need for BTC to rebalance its tariffs for basic fixed telephony services prior to the consideration of need for any form of subsidy.

CBL contended that there is a significant risk of inefficiencies, market distortion and other negative consequences in the absence of full tariff rebalancing.

CBL further referenced a USO Consultation Document that was issued in March 2009 by the Committee for the Privatisation of The Bahamas Telecommunications Company Ltd. This document indicated that the government at the time:

- (i) considered the various options available in the event a USP demonstrated an access deficit to URCA's satisfaction;
- (ii) indicated its preference for tariff rebalancing; and
- (iii) stated that it wished to see all operators move to a more cost reflective tariff regime.

CBL also referenced URCA's January 2013 Statement of Results and Final Decision on the "Framework for the Clarification and Implementation of Existing Universal Service Obligations (USO) under Section 119 and Schedule 5 of the Communications Act 2009" [ECS 01/2013].<sup>6</sup> URCA there acknowledged comments regarding tariff rebalancing that were made in the Statement of Results on the "Consultation on a New Price Regulation Regime for the Communications Sector" [ECS 16/2009] regarding tariff rebalancing.<sup>7</sup>

In CBL's opinion, the means for calculating and, more importantly, the assessment of a USO funding claim, cannot be considered in isolation of tariff rebalancing. CBL continues to be strongly opposed to the establishment of any USO financing mechanism that it believes would contribute to any claimed access deficit by BTC due to unbalanced tariffs.

CBL proposed in an Annex to its response the addition of specific text to Section 8.3 of BTC's proposed NAC Guidelines in ECS 15/2014 which sought to amend the unfair financial burden test as proposed by URCA. While CBL acknowledged that tariff rebalancing does not apply to it, CBL was not opposed

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<sup>5</sup> <http://www.urcabahamas.bs/download/013910600.pdf>

<sup>6</sup> <http://www.urcabahamas.bs/download/012155400.pdf>

<sup>7</sup> <http://www.urcabahamas.bs/download/033197200.pdf>

to the inclusion of the proposed text in the corresponding Section (7.2) of its own NAC Guidelines for the purpose of symmetry.

### **3.2 USO Funding Requirements**

At Section 3.2 of its response, CBL stated its opinion that in the absence of a full tariff rebalancing process, there is a significant risk that BTC could apply for inordinate USO funding for the provision of its fixed voice telephony USO. CBL feels as though this would cause financial burden to the sector and distort the market among other negative consequences. CBL therefore proposed wording changes for BTC's NAC Guidelines. CBL is not opposed to the inclusion of the proposed text in its own NAC Guidelines for symmetry.

### **3.3 Application of the Unfair Burden Test**

At Section 3.3 of its response, CBL reiterated that in the absence of a full tariff rebalancing process, there is a significant risk that an inordinate financial burden could be placed on the sector which would lead to negative consequences for the market.

CBL proposed amendments to Section 8.3 of NAC BTC's Guidelines and the corresponding Section 7.2 of its NAC Guidelines.

### **3.4 Other Matters**

At Section 4 of its response, CBL contended that there were numerous discrepancies in terminology and general descriptive content between the proposed BTC NAC Guidelines versus the proposed CBL NAC Guidelines probably attributable to the different USO services of each USP. CBL requested URCA to ensure that all sections of the Final NAC Guidelines that are not service-specific would be harmonised as appropriate.

### **URCA's responses to CBL's comments**

URCA considers the issue of tariff rebalancing to be beyond the scope of the consultation document. However, URCA assures CBL that URCA will give further consideration to the issue of tariff rebalancing in its forthcoming consultation paper on price cap design and implementation for BTC's fixed telephony services.

In light of this decision, URCA does not accept CBL's proposed amendments to Section 8.3 in ECS 15/2014 and, therefore, does not propose to make the changes suggested by CBL in the Final BTC NAC Guidelines.

Regarding the harmonisation of terminology and general descriptive content in the Final NAC Guidelines for BTC and CBL, URCA will endeavour to ensure that the terminology and general descriptive content in all sections of the Final NAC Guidelines for both BTC and CBL that are not service-specific are harmonised as much as possible and as is appropriate.

**URCA's final decision on CBL's comments**

**Tariff rebalancing will be considered by URCA under a separate consultation process on price cap design and implementation.**

**URCA will not adopt CBL's proposed changes to Section 8.3 in ECS 15/2014 to the Final BTC NAC Guidelines.**

**URCA will endeavour to ensure that the terminology and general descriptive content in all sections of the Final NAC Guidelines for both BTC and CBL that are not service-specific are harmonised as much as possible and as is appropriate.**



#### **4. NEXT STEPS**

The following aspects of the universal service framework must now be developed by URCA:

- Establishment of a register of specified institutions
- Implementation plans for USO for BTC and CBL
- Guidelines for measuring the affordability of USO
- Consumer awareness of consumer rights under the Universal Service Obligations

The implementation plans and affordability guidelines will be developed in consultation with BTC and CBL as part of the ongoing development of the universal service framework. URCA continues to assess each USP's overall compliance with their existing statutory universal service obligations.