



DRAFT
Regulatory Framework on
Accounting Separation

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1. INTRODUCTION

- 1.1 The Telecommunications Act (the "Act") states, in its Article 3, that the telecommunications sector shall be regulated to ensure, among other objectives, "the creation of a favorable atmosphere to promote and encourage fair competition in all fields of telecommunications."
- 1.2 Article 12 of the Telecommunications Bylaw (the "Bylaw") allows the Communications and Information Technology Commission ("CITC") to impose certain conditions on individual licenses to implement the objectives of the Act. The list of such conditions includes "the level of segregation of telecommunications services for accounting and regulatory purposes as may be determined by the Commission".
- 1.3 Pursuant to Article 29 of the Bylaw, and in relation to competition among service providers in telecommunications markets in the Kingdom, CITC must, among other duties:
 - 1.3.1 promote efficient and sustainable competition for the benefit of end-users; and
 - 1.3.2 monitor and prevent abuses of a service provider's dominant position.
- 1.4 CITC also has the power to intervene, case-by-case, against abuses by dominant service providers (Article 31 of the Bylaw) or other anti-competitive practices (Article 32 of the Bylaw) and impose appropriate ex post remedies including, among other measures, the provision of periodic reports to CITC (Article 34 of the Bylaw).
- 1.5 Accounting separation obligations can contribute significantly to the promotion and encouragement of fair, efficient and sustainable competition in telecommunications, as well as to other objectives of the Telecommunications Act.
- 1.6 The existing Accounting Separation obligations imposed on the Saudi Telecommunications Company ("STC") are based on the designation of the STC as a dominant service provider, by CITC Decision No. 1/1423 and the adoption of the Accounting Separation Policy in 2004.
- 1.7 Since the adoption of these measures, the ICT market in Saudi Arabia has evolved significantly, with the introduction of competition in mobile communications and the more recent opening of competition in the fixed telecommunications and data markets. These developments have led to the entry of several new service providers and the expected entry of more service providers in the near future. As a result of these developments, CITC is conducting a review of the determinations in Decision No 1/1423.

- 1.8 For the above reasons, the 2004 Accounting Separation Policy is being replaced with the present, updated, Regulatory Framework for Accounting Separation in order to reflect the evolution of the Kingdom's ICT markets and international best practice.

2. DEFINITIONS

- 2.1 The terms and expressions defined in the Act and the Bylaw shall have the same meaning in this Regulatory Framework.

- 2.2 Notwithstanding Article 2.1, the following terms and expressions shall have the meaning assigned to them hereunder, unless the context requires otherwise:

2.2.1 **"Accounting Separation"** or **"Separated Accounts"** shall mean the preparation of accounting information (including costs and revenues) related to regulated and non regulated activities of a Designated Service Provider, at a level of detail that allows CITC, or a third party appointed by CITC, to trace back and forth all internal and external transactions and ensure compliance with the Designated Service Provider's relevant regulatory obligations. Accounting Separation uses Regulatory Accounts or cost models to provide the required information.

2.2.2 **"Accounting Separation Guidelines"** shall mean Guidelines prepared and approved by CITC, defining the detailed requirements for implementation of this Regulatory Framework.

2.2.3 **"Accounting Separation System"** shall mean a system able to produce Accounting Separation information.

2.2.4 **"Designated Service Provider"** shall mean any service provider licensed in the Kingdom and designated by CITC to prepare Separated Accounts in accordance with this Regulatory Framework.

2.2.5 **"Dominant Service Provider"** shall mean any service provider designated as such by CITC pursuant to Chapter 4 of the Bylaw.

2.2.6 **"Principle of Proportionality"** shall mean that the measures applied in a decision are appropriate and limited to what is necessary to achieve the pursued regulatory objective.

2.2.7 **"Regulatory Accounts"** shall mean accounts prepared for regulatory purposes.

- 2.2.8 **“Regulatory Accounting”** shall mean record keeping rules and processes used for the preparation of accounts and reports for regulatory purposes (e.g. for the verification of cost-based pricing obligations).
- 2.2.9 **“Remedies”** shall mean the specific measures imposed by the CITC on a Dominant Service Provider to counter, control, mitigate or neutralize the impact of its market dominance.
- 2.2.10 **“Statutory Accounts”** shall mean the audited statutory financial accounts prepared by a Designated Service Provider in satisfaction of the Saudi Regulations of Companies, Exchange law of Saudi Arabia and the Capital Market Authority (CMA). Statutory Accounts shall be prepared in accordance with accounting standards generally accepted in the Kingdom of Saudi Arabia by the Saudi Organization for Certified Public Accountants (SOCPA).
- 2.2.11 **“Statutory Financial Statements”** shall mean the audited financial statements (such as a balance sheet) prepared from Statutory Accounts.

3. CONSIDERATIONS

- 3.1 The Accounting Separation Policy of 2004 required STC to separate its accounts on the basis of four pre-defined business segments: fixed, mobile, data and other. By contrast, the separation of accounts under this Regulatory Framework shall be based on (i) the definition of distinct relevant markets, (ii) the designation of one or more service providers as dominant in each of these defined markets, and (iii) the imposition, modification or withdrawal of appropriate remedies on the Designated Service Provider(s), as determined by CITC from time to time.
- 3.2 Accordingly, as a rule, Accounting Separation obligations to be imposed under this Regulatory Framework shall aim to provide CITC with the information necessary to review a Designated Service Provider’s compliance with the Remedies imposed on this Designated Service Provider or its other obligations in place by virtue of its dominant position in a relevant market.
- 3.3 CITC’s determination of separate services and products for which Separated Accounts must be prepared need not necessarily coincide with any associated relevant service and product markets that may be defined by CITC.
- 3.4 Service providers designated as dominant in one or more telecommunications markets may be also operating in other markets, in which they have not been designated as dominant. The Separated Accounts to be prepared pursuant to this Regulatory Framework shall

concern, in the first place, a service provider's operations in one or more regulated markets in which it has been designated as dominant.

- 3.5 In order to ensure proper implementation of a Designated Service Provider's obligations, CITC may also request accounting information, including Separated Accounts, for markets, in which this Designated Service Provider is active but not dominant. Such information may be necessary to ensure, e.g., the proper allocation of costs common to the regulated and unregulated markets in question, or the coherence of data. In such cases, CITC may accept that Separated Accounts for unregulated markets are reported only at aggregated level and in less detail than the ones required for the associated regulated markets, if this is sufficient for the effective review of the Designated Service Provider's obligations in the regulated market(s).

4. REGULATORY FRAMEWORK

Purpose and Scope of Accounting Separation

- 4.1 Accounting Separation obligations imposed by CITC on a Designated Service Provider pursuant to this Regulatory Framework shall aim to allow or help CITC
- 4.1.1 verify a Designated Service Provider's adherence to its obligations of non-discrimination, objectivity, cost-based pricing and transparency set down in the Bylaw;
 - 4.1.2 ensure the Designated Service Provider's compliance with specific obligations imposed on it by the CITC;
 - 4.1.3 understand a Designated Service Provider's costs and revenues at the required level of detail;
 - 4.1.4 identify and prevent abuses of dominance or other anti-competitive practices by a Designated Service Provider; and/or
 - 4.1.5 ensure implementation of any associated objectives of the Act.
- 4.2 Through their Accounting Separation, Designated Service Providers shall provide the evidence required by CITC for the purposes of Article 4.1 above, in line with the requirements of this Regulatory Framework and the Accounting Separation Guidelines.
- 4.3 Designated Service Providers must disaggregate information on their costs and revenues relating to each relevant market in which the Designated Service Providers operate, regardless of whether they have been designated as dominant or not in each of these relevant markets.

- 4.4 CITC may require a Designated Service Provider to disaggregate information relating to its costs and revenues on a level other than that of the market(s) concerned including, without limitation, on the level of distinct services or products, distinct business or functional units, or corporate affiliates, whether or not these belong to the same market if, under the circumstances, this is necessary or appropriate to fulfill the regulatory objectives listed in Article 4.1 above.
- 4.5 The level at which Separated Accounts must be prepared shall be determined by the CITC as further specified in the Accounting Separation Guidelines and may take into account factors such as configurations or products of the services concerned.
- 4.6 The accounting information provided by a Designated Service Provider must be no less detailed than necessary to fulfill the purposes of the Accounting Separation obligation imposed on that Designated Service Provider and, in particular, to demonstrate its compliance with its associated regulatory obligations.
- 4.7 CITC may allow Designated Service Providers to provide aggregated or less detailed information with regard to any market in which they have not been designated as dominant, if this does not obstruct or complicate CITC's ability to ensure the Designated Service Providers' compliance with their regulatory obligations in the markets in which they are designated as dominant and/or any other purpose for which CITC has imposed Accounting Separation on these Designated Service Providers.
- 4.8 Separated Accounts under this Regulatory Framework shall be prepared for the purposes of reporting to CITC in regular periods determined by CITC, such as a financial year, a calendar year, or shorter periods.
- 4.9 In addition, CITC may require Designated Service Providers to prepare Separated Accounts and submit related information at any time, on an "ad hoc" (individual case) basis, in particular if this is justified to allow CITC to examine current or past instances of possible anti-competitive conduct by the Designated Service Provider and, if necessary, impose appropriate ex post remedies, under Article 34 of the Bylaw. CITC shall determine the scope of such ad hoc accounts and the amount of information required. Designated Service Providers shall take the necessary measures to ensure a timely response to such "ad hoc" requests, as further specified in the Accounting Separation Guidelines.
- 4.10 In all processes and procedures related to the preparation of Separated Accounts and Regulatory Accounting Systems, Designated Service Providers shall comply with the regulatory principles, regulatory accounting principles and preparation principles set out in the Accounting Separation Guidelines.

4.11 Without prejudice to any of the principles referred to in Article 4.10 above, Designated Service Providers shall ensure maximum possible consistency and conformity of their Separated Accounts with the Saudi Arabian Generally Accepted Accounting Principles (GAAP), to the extent that these are applicable.

Cost Accounting Convention and Related Issues

4.12 Designated Service Providers shall prepare Separated Accounts using each of the Historical Cost Accounting ("HCA"), Current Cost Accounting ("CCA") and Long Run Incremental Cost ("LRIC") cost conventions.

4.13 Designated Service Providers shall follow any relevant Commission instructions set out in, or issued in accordance with, the Accounting Separation Guidelines with regard to the interpretation and implementation of Article 4.12.

4.14 The instructions contained in the LRIC Model Guidelines shall be also applicable for the purposes of this Regulatory Framework, unless otherwise required under any provision of this Regulatory Framework or of the Accounting Separation Guidelines.

4.15 On a case-by-case basis, and consistent with the Principle of Proportionality and after consultation with the party involved, CITC may allow a Designated Service Provider to postpone the implementation of its above obligation with regard to one or more of the cost accounting conventions referred to in Article 4.12.

Preparation of the Accounting Separation System

4.16 Any information prepared by a Designated Service Provider under the HCA, CCA and LRIC cost conventions must be prepared and structured in a way that renders it possible for a third party to trace each allocation step and stage back to that Designated Service Provider's original accounts and information systems.

4.17 Designated Service Providers shall prepare their Accounting Separation System consistent with the cost and revenue attribution stages and relevant requirements set out in the Accounting Separation Guidelines.

Reporting Requirements

4.18 Unless otherwise required by CITC, Designated Service Providers shall submit two separate sets of Accounting Separation documents: one intended for publication and one for internal use by CITC and the auditor(s).

4.19 The Accounting Separation documents must comprise at least the data, reports, manuals, statements and any accompanying materials specified in detail in the Accounting Separation Guidelines.

4.20 Unless otherwise required by CITC, Designated Service Providers shall submit the above Accounting Separation documents at least annually, in accordance with the requirements, procedures and deadlines set out in the Accounting Separation Guidelines.

Publication

4.21 The version of the Accounting Separation documents prepared for publication must provide transparency on the Separated Accounts and Account Separation system, demonstrate the Designated Service Provider's compliance with respect to the Accounting Separation principles, and be consistent with the publication requirements in the Accounting Separation Guidelines.

4.22 The Designated Service Provider must publish the Accounting Separation documents prepared for publication. Without limitation to the Designated Service Provider's responsibility for this publication, CITC may publish directly any information from the Accounting Separation documents that meets the conditions for publication set out in Article 4.23-4.25 below.

4.23 The Accounting Separation documents prepared for publication may omit or summarize information contained in the version intended for internal use by CITC and the auditors if all of the following conditions are met:

4.23.1 the information concerned qualifies as "confidential information" under Article 4.24 below;

4.23.2 the Designated Service Provider has submitted a properly reasoned written request to CITC justifying this information's confidential treatment under this Article; and

4.23.3 CITC does not conclude that a disclosure of the information concerned would be in the public interest pursuant to Article 4.25.

4.24 Information shall qualify as confidential for the purposes of Article 4.23 if it is

4.24.1 a trade secret or secret know-how protected as such under the laws of the Kingdom; or

4.24.2 financial, commercial or business information on the Designated Service Provider or its operations, treated consistently as confidential by the Designated Service Provider and not accessible to the public;

and its disclosure to the public can reasonably be expected to cause material economic damage to the Designated Service Provider or otherwise materially prejudice its rights or legitimate interests.

4.25 CITC may conclude that the publication of information qualifying as confidential under the previous Article is in the public interest if the advantages of such publication for the purposes of the Accounting Separation in question outweigh any harm to the Designated Service Provider. In its determination on the merits of such disclosure CITC may consider, among other factors, the extent to which

4.25.1 this confidential information is important for the purposes of transparency and verification of the Designated Service Provider's compliance with its Accounting Separation obligations; and

4.25.2 the publication of a summary or redacted version of the information concerned, prepared by CITC or proposed as an alternative by the Designated Service Provider, would be sufficient under the circumstances.

Audit and Review

4.26 The Designated Service Provider's Accounting Separation System and related Separated Accounts must be reviewed by an independent auditor, who shall provide a relevant auditor's report to CITC.

4.27 CITC shall undertake, directly or through a third party appointed by CITC, a conformity check of the Accounting Separation system and related documentation.

4.28 CITC may approve without conditions, approve conditionally or reject the Accounting Separation documentation in accordance with the procedures and with the consequences set out in the Accounting Separation Guidelines.

Final Provisions

4.29 This Regulatory Framework shall replace the Accounting Separation Policy of 2004 upon its entry into effect.

4.30 CITC shall issue Accounting Separation Guidelines addressing in more detail the provisions of this Regulatory Framework, as well as any issues that may arise in the context of its implementation.

4.31 The Accounting Separation Guidelines may be amended at any time by CITC, following a public consultation. The Accounting Separation Guidelines and any amended version thereof shall be posted on CITC's website.

- 4.32 Failure, by a Designated Service Provider, to comply with the Accounting Separation Guidelines shall be considered by CIRC a violation of the Act, the Bylaw and/or this Regulatory Framework, and shall be referred to the Violations Committee.
- 4.33 Where and for as long as a Designated Service Provider fails to provide CIRC with any information required under the Accounting Separation Guidelines, the CIRC may refuse, suspend or withdraw its approval of any services, products and tariffs whose approval is linked to CIRC's access to, or approval of, the missing information.
- 4.34 CIRC's powers with regard to Accounting Separation under this Regulatory Framework shall be without prejudice to any of its powers under any Commission statute.