TELECOMMUNICATION COST AND TARIFF MODEL IN BRAZIL

Rio de Janeiro, May 2006
## Evolution since privatization

<table>
<thead>
<tr>
<th>Indicator</th>
<th>1998</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed access points installed (millions)</td>
<td>22.1</td>
<td>50.3</td>
</tr>
<tr>
<td>Fixed access points in service (millions)</td>
<td>20.0</td>
<td>39.6</td>
</tr>
<tr>
<td>Incorrect accounts per 1000 accounts</td>
<td>9.94</td>
<td>1.64</td>
</tr>
<tr>
<td>Local network digitization (%)</td>
<td>67.6</td>
<td>99.9</td>
</tr>
<tr>
<td>Fixed access points in service per 100 inhabitants</td>
<td>12.5</td>
<td>21.5</td>
</tr>
<tr>
<td>Number of cellular terminals (millions)</td>
<td>7.40</td>
<td>75.5</td>
</tr>
<tr>
<td>Number of cellular terminals per 100 inhabitants</td>
<td>5</td>
<td>41</td>
</tr>
<tr>
<td>Public telephone booths in service per 100 inhabitants</td>
<td>34</td>
<td>69</td>
</tr>
</tbody>
</table>

Note: The 1998 data are for the month of July
The 2005 data are for the month of December
Source: Anatel
Regulatory challenges

- Updating of the regulatory framework: technological convergence
- Strengthening economic and financial regulation: reduce information imbalances
- Stimulating fresh investment, efficiency and passing the benefits on to society
Cost-based regulation context

• Decree 4.733 of 10 June 2003, Article 7:
  • “I – Interconnection and unbundling tariffs will be determined through the adoption of a long-run incremental cost model, with the economic conditions necessary for the ongoing fulfillment of universal service goals by licensees being maintained”.
Cost-based regulation context

• Institutional environment in 2002:
  • Brazil risk (EMBI Brazil):
    » March 2002 = 700 base-points
    » September 2002 = 2400 base-points
    » March 2006 = 230 base-points
  • Society’s reaction to the indexation of tariffs in general and of telephony tariffs in particular
    » IPCA index, May 1998 to May 2005 = 68.72%
    » Monitored prices = 127.58%
    » General Price Index – Domestic Supply = 127.45%
Cost-based regulation context

• Regulation of interconnection tariffs:
• First contractual period: June 1998 to 31 December 2005
  => Maximum prices annually adjusted by the General Price Index – Domestic Supply, less an annual predetermined factor
• Second contractual period:
  “With effect from 1 January 2008, the local network usage tariff will be expressed in values that take account of the long-run cost model established under the terms of the relevant regulations in force…” (§ 25.2 of new licence contracts).
Cost-based regulation context

• From 1 January 2006 to 31 December 2007, the maximum local network usage tariffs will be equivalent to:
  • 2006 => 50% of the public usage tariffs
  • 2007 => 40% of the public usage tariffs
• Local network usage tariffs currently:
  • from R$ 0.03371 to R$ 0.03737 per minute, equivalent to USD 0.014 to USD 0.016
• Long-distance network usage tariffs during normal hours:
  • from R$ 0.08277 to R$ 0.11139 per minute, equivalent to USD 0.035 to USD 0.048
Structure of the Accounts Separation and Allocation Document (ASAD)

- I => Historical cost accounting (HCA) base, whereby costs are allocated to the network elements and products according to the fully allocated costs (FAC) model
  - Allocation methodology: activity-based costing
- II => Current cost accounting (CCA) base
- III => Long-run incremental costs (LRIC)
Current actions

• Establishment of a Cost-Model Commission (CMC). Results:
  • Development of a consultative mechanism for responding to telecommunication operators
  • Development of an interface for electronic submission of the ASAD
  • Elaboration of terms of reference for the hiring of three consultancy firms to deal, respectively, with the areas of: project management; validation of the top-down ASAD; construction of the bottom-up (efficient network) version and reconciliation
Time-frame

- 30 April 2006 => Submission by FSTS licensees of the FAC-HCA => Costs totally allocated on historical bases
- 30 April 2007 => Submission by FSTS licensees of the CCA/LRIC => Costs on current bases/LRIC for use as from 2008 in the definition of local network usage tariffs
- Mobile telephony => Awaiting a resolution from Anatel. May use FAC-HCA and FAC-CCA in defining RVU-M reference usage value for resolution of disputes between companies negotiating mobile network usage tariffs
Challenges/opportunities

- Strategic use of the ASAD by telephony licensees
- Budgetary restrictions
- International experience
- New learning
Thank you!

Jorge Ruiz
jorgeruiz@anatel.gov.br

Vanderlei Campos
vanderlei@anatel.gov.br