

Outline of Proceedings of the 4th Meeting of the Study Group on the Accounting System in the Telecommunications Service

1. Date: 15:00 to 17:10, Thursday, March 15, 2007

2. Location: Special Conference Room 3, 9th floor, Central Joint Government Building 2

3. Attendees

(1) Members (Entered in alphabetical order of last names, with honorifics omitted)

Hiroshi Obata, Hiromasa Sekiguchi (Deputy Chairperson), Norio Tezuka,
Mikio Tokai (Chairperson), Junichiro Tsuruta

(2) Observers (Entered in alphabetical order of entity names)

Chubu Telecommunications Co., Ltd.; eAccess Ltd.; KDDI Corporation; Nippon Telegraph and Telephone East Corporation; Nippon Telegraph and Telephone West Corporation; Nomura Securities Co., Ltd. (Masuno, Senior Researcher); SoftBank Telecom Corporation; Telecom Service Association

(3) Ministry of Internal Affairs and Communications

Taniwaki, Director of the Telecommunications Policy Division; Ninomiya, Senior Planning Officer of the Tariff Division; Katagiri, Assistant Director of the Tariff Division; Iimura, Assistant Director of the Tariff Division

4. Agenda

(1) Hearing of presentations by observers 2)

(2) Others

5. Outline of proceedings

[Hearing of presentations by observers 2]

<Presentation by SoftBank Telecom Corporation>

- SoftBank Telecom Corporation argued that, in accordance with Document 2, it is important to rationalize interconnection charges through substantial function separation, including accounting separation, by NTT East Japan and NTT West Japan, thereby enriching retail services.
- Major discussions were as given below.

(Member)

The disclosure system for transactions between related parties in the Rules for Telecommunications Business Accounting was amended in keeping with the amendment of the Company Law last year. Is it your company's understanding that the level of disclosure was set back?

(SoftBank Telecom Corporation)

That is correct. In view of the effects on interconnection accounting, it is questionable whether it is appropriate to invariably apply disclosure rules for ordinary companies to NTT East Japan and NTT East Japan.

(Member)

Your company pointed out that administrative departments should be separated from use departments in the case of profit and loss statements, and by service type as well. What points will be specifically clarified by the above?

(SoftBank Telecom Corporation)

We feel that if administrative department costs are clarified by service type, it will become easier to understand items such as expenses and unit costs for administrative departments.

(Member)

Your company pointed out that service types having great effects in terms of competition should be classified. What service types does your company specifically refer to?

(SoftBank Telecom Corporation)

We have in mind service types that are of considerable scale and those that are competitive. However, we have not devised numerical criteria.

(Member)

Your company mentioned internal mutual assistance. Does this mean that more detailed information is needed than that presented in the current service type categories, or does it mean that current service type categories are not appropriate as classifications of monopolized fields and competitive fields?

The conception that internal mutual assistance in competitive fields and monopolized fields does not necessarily constitute a problem may exist. Therefore, it is conceivable that the acquisition of detailed information is not necessarily important. What does your company think about this point?

(SoftBank Telecom Corporation)

You are right about internal mutual assistance in competitive fields. Things would be understandable if total profits were within the range of ordinary business activities.

(Member)

Your company pointed out the matter of the balance between the commissioning expenses of the two NTT companies and the expenses of the group companies commissioned to do work by the NTT companies. In other words, your company referred to the matter of the profits of such group companies. Does your company feel that problems will be solved if more exhaustive information is made public on transactions among group companies in regard to such profits?

(SoftBank Telecom Corporation)

We think so. We believe that it is necessary to verify whether the commissioning expenses paid to the group companies by NTT East Japan and NTT West Japan are at a reasonable level.

<Presentation by Chubu Telecommunications Co., Ltd.>

- In accordance with Document 3, Chubu Telecommunications Co., Ltd. argued, in the capacity of a carrier which itself installs facilities, that it is important to reinforce monitoring for internal mutual assistance, to further disclose accounting information, and to perform depreciation on the basis of legal service life.
- Major discussions were as given below.

(Member)

Your company discusses so-called IP telephone-based services in polar contrast to conventional telephone services and dedicated line services. Supposing that the expenses of IP telephone-based services are disclosed in detail, how do you think fair competition can be ensured?

(Chubu Telecommunications Co., Ltd.)

As mentioned in one of the presentations earlier, the transfer of profits from subscriber telephone service to B-FLET'S service falls under internal mutual assistance in monopolized fields. This fact may be said not to be a problem, but if profits of other departments are appropriated excessively to B-FLET'S service, there is a fear of sound competition being hampered. Therefore, detailed information should be disclosed from the viewpoint of monitoring.

(Member)

Your company pointed out that the calculation of depreciation expenses by using economic service life will lead to fear that a market will be formed where investment cannot be recovered. Does this mean that your company is opposed to the concept mentioned a little while ago by SoftBank Telecom Corporation?

(Chubu Telecommunications Co., Ltd.)

We feel that we still do not have sufficient knowledge for calculating reasonable economic life. We are not supposed to be the only company engaging in facilities competition. We cannot allow models that do not provide us any motivation to perform construction.

(Member)

Is your company of the opinion that legal service life should be applied when interconnection charge costs are calculated? What do you think of service life in terms of the accounting system?

(Chubu Telecommunications Co., Ltd.)

Our understanding is that the discussion held this time pertains not to the Tax Law but to the calculation of interconnection charge costs. If economic service life is used to calculate interconnection charge costs, then discrepancies will arise with respect to the accounting system, and it will take a long time to recover our investment. In this respect, we are skeptical about the use of economic service life.

(Member)

The basic concept of depreciation expenses is that after facilities are laid out, the cash inflow obtained by using such facilities will be made to correspond to amortization expenses. I can

understand your company's desire to shorten service life, thereby realizing early recovery of your investment, but if that is the greatest reason for being in favor of legal service life, I am afraid that this reasoning is a little bit weak in terms of logic.

(Chubu Telecommunications Co., Ltd.)

It is true that what you pointed out is correct, but our situation is as follows. Our company built a business model based on the current legal service life, and we presume that there is no sufficient reason for adopting economic service life in the present circumstances where no accumulated data are available on FTTH services, which have just been started.

(Member)

What is the stance of SoftBank Telecom Corporation? It seems that the opinion of your company is limited to areas related to interconnection charges for fiber-optic networks. What do you think of this matter?

(SoftBank Telecom Corporation)

The opinion of our company is not particularly limited to interconnection charges for fiber-optic networks. We are of the opinion that service life should be brought into agreement with actual service duration.

(Member)

Your company pointed out matters related to the disclosure of information on transactions between group companies. Does your company feel that such information should all be disclosed to the public? I believe that properly speaking, there should be a difference in the amount of detail between information to be reported to administrative agencies and information to be disclosed to the public. What do you think about this?

(Chubu Telecommunications Co., Ltd.)

We presume that, for example, the operating expenses of NTT East Japan and NTT West Japan are related to interconnection charge costs, and that the way that the sales expenses are handled between group companies is related to the reasonableness of charges. We have yet to conduct specific studies on the appropriate extent of disclosure to the public, nevertheless, what we pointed out is based on the above reasoning.

(Member)

Your company pointed out that information should be disclosed via third party organizations. What is the purport behind doing so?

(Chubu Telecommunications Co., Ltd.)

Accounting information of NTT East Japan and NTT West Japan should be made public after being analyzed by third party organizations. In this case, we feel that the objectivity of analysis is important.

<Presentation by Telecom Service Association>

- Telecom Service Association argued that, in accordance with Document 4, it is necessary to

establish interconnection accounting facility categories that correspond to the progress of the changeover to IP telephones and to ensure fair competitive conditions in transactions between dominant carriers and their subsidiary companies.

- Major discussions were as given below.

(Member)

Your association pointed out that facility categories should be established by quality as far as NGN is concerned. Other than this matter, what are the points to keep in mind?

(Telecom Service Association)

It is presumed that the sharing of facilities among different types of services will increase compared to the current situation. We therefore feel that the criteria for cost allocation will become an important issue.

(Member)

Your association pointed out that the provision of bundled services requires ensuring fair competitive conditions. What are the points to specifically keep in mind in terms of accounting?

(Telecom Service Association)

If it is impossible to verify whether fair competition is achieved due to the presence of any dubious area in the process of setting charges, we believe that it will be necessary to have some means of *ex post facto* verification.

<Free discussions>

- A total of three organizations, including a company, gave presentations. Today, after a question-and-answer session, free discussions were held, being participated in by observers as well, who did not make presentations. Major discussions were as given below.

(Member)

As a consequence of today's presentations, what ideas did NTT East Japan and NTT West Japan come to have?

(NTT East Japan and NTT West Japan)

We have Class 1 telecommunications facilities, which are so-called monopolized assets. We will properly do what is necessary to make such facilities open. In this regard, we understand that the user charges that are set, operating expenses, and sales expenses are competitive as long as interconnection rules exist. We therefore presume that such items should not be disclosed to competitor companies. In particular, we feel that service categories in business accounting are too circumstantial, even now, in light of their purposes.

If consolidated accounting is to be implemented, various difficulties are presumed to arise. Moreover, costs will be incurred. If such costs are reflected in interconnection charge costs, it is presumed that those costs will eventually be reflected in user charges as well. It is therefore

necessary to discuss this matter carefully.

(Nomura Securities Co., Ltd.)

If economic service life is to be applied to depreciation expenses, it is presumed that competitive superiority among relevant carriers will undergo dynamic changes. It is therefore necessary to discuss this matter thoroughly.

(SoftBank Telecom Corporation)

In light of user interests, the depreciation method should be established in such a way as to be compatible with the actual use conditions. If this is done, we presume that the number of users will increase and that the facility use efficiency will also increase.

(NTT East Japan and NTT West Japan)

When we put ourselves in the users' position, it is nice for inexpensive and good services to be provided. Nevertheless, it is necessary to be able to recover the costs required for providing services. At the present time, no definite data are available, in reality, that show how many years relevant facilities are to be used. However, it does not matter whether they are to be used for 10 years or 20 years.

(Member)

Recently, the depreciation methods in the Tax Law have been revised, with the result that the discrepancy between the standards in tax accounting and those specified by the Accounting Standards Board of Japan has grown. Under such circumstances, do NTT East Japan and NTT West Japan have any idea of how to set service life from now on?

(NTT East Japan and NTT West Japan)

Frankly speaking, no study is in progress about this matter. There is a principle of continuity in accounting. However, we will develop a full awareness of the status quo and hold consultations with accountants, and then there may be a possibility of changing service life in the future, depending on circumstances.

In connection to this, we go on introducing new facilities such as fiber-optic equipment or whatever. In this regard, we can be aware of actual use conditions only after the use of such facilities. This fact makes it difficult to discuss this matter. In business like telecommunications services, where new facilities are being introduced at all times, we understand that not only our companies, but also other companies, have the same worries.

(Member)

Our understanding is that the Corporation Tax Law has swayed the current practice of depreciation greatly. In the world of enterprise accounting standards, there is no concept that the legal service life is reasonable. The principle is that each company establishing an accounting system should estimate service life. However, in individual companies, it is often the case that technical difficulties are involved when appropriate service life is calculated. Therefore, the current situation is that the service life specified in the Tax Law is used as the next best thing. That the legal service life stipulated in the Corporation Tax Law is economically reasonable is not necessarily verified.

(Member)

When the current accounting system was established, what arguments were made about service life?

(Member)

In those days, the concept was that legal service life equaled economic service life. My understanding is that no particular argument was made.

(Member)

The Rules for Telecommunications Business Accounting was amended in keeping with the amendment of the disclosure system. According to the Enterprise Accounting Standards, any transaction that exceeds 10 percent of the total cost is subject to disclosure. What do the two NTT companies think of the items to be disclosed?

(NTT East Japan and NTT West Japan)

Details are being studied. In any case, we intend to comply with the general accounting standards. We do not feel that we are the only companies faced with this issue. We presume that other companies also have the same worries.

(Member)

In this regard, your companies own bottleneck facilities as dominant carriers. Such being the case, your companies should push forward studies from now on by considering such situations as well.

(Member)

The presentation given by SoftBank Telecom Corporation pointed out the profits of group companies, and the disclosure of detailed information on inter-group transactions was requested. In the presentation given by KDDI in the last meeting, it was pointed out that costs should be understood on a consolidation basis, thereby removing such profits from interconnection charge costs. Personally, I feel that consolidation-oriented arguments will be made to remove such profits from interconnection charge costs, and that detailed information on transactions between parties concerned will be disclosed as supplementary data.

(Member)

As I mentioned during one of the individual question-and-answer sessions, I personally do not believe that monitoring for internal mutual assistance is not directly linked to the act of circumstantially stating the breakdowns of income and expenditure. Are there any other opinions?

(Member)

As regards techniques for internal mutual assistance, I presume that there are various parameters to look at other than user shares, such as brands and possession of bottleneck facilities. Besides, in regard to the necessity of segmentation in controlled accounting, it is necessary, for example, to verify the improvement of efficiency in business management. In addition, it is necessary to hold discussions from now on about the grounds for the additional factors of internal mutual assistance.

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