Office of Utility Regulation

Mobile Termination Rates

Decision Paper

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1. Introduction

In August 2006 the OUR published a consultation paper entitled “Mobile Termination Rates” (“MTRs”) (OUR 06/14), which was followed by a draft decision paper (OUR 06/19) in December 2006. MTRs are the fees charged to other telecommunications companies by mobile network operators to terminate calls on mobile networks. Mobile termination is a significant input into the provision of retail fixed-to-mobile and mobile-to-mobile services. Consequently it has implications for mobile and fixed call charges

The purpose of the consultation process was to consult interested parties on whether regulatory oversight was required and, if so, which method should be used to establish a set of reasonably efficient mobile voice call termination charges. The need to establish whether regulatory intervention is required should be seen against a background of regulators elsewhere either having already acted or recognising that regulatory action is required and the results of the OUR benchmarking which identified Guernsey MTRs as being among the highest of the 31 countries surveyed. It is important that these charges should not be excessive, so that the benefits of having a competitive retail market in mobile telecoms services are not reduced or cancelled out through uncompetitive rates in the wholesale termination market.

To-date, mainly because of network operators having monopolies over termination services on their own networks, regulators in other jurisdictions have considered in detail the level of charges for this service, and a number of regulators have adopted specific price controls for the service. The Director General (“DG”) was of the view that, given the rates that currently exist in the Guernsey market as identified in OUR 06/14, consideration should be given to assessing whether the present rates are appropriate.

The draft decision paper proposed in the first instance that there was a need for the DG to intervene in setting MTRs within the Bailiwick. In the draft decision paper, the DG proposed that a benchmarking approach is taken, and that the Ofcom rates be used as the basis for such benchmarking. The DG also proposed that the MTR rates apply to voice termination calls only, on both 2G and 3G networks - consistent with Ofcom’s approach. Finally, the DG proposed an MTR of 6.75ppm fixed for three years which would allow all operators time to improve efficiencies over this period. Opinions were sought on these proposals.

Responses were received from three parties, with each respondent setting out its views on the proposals put forward in the draft decision paper.

The DG has decided that the rates proposed in the draft decision paper will apply. The rate of 6.75ppm will be a maximum target average charge (TAC). Each network operator will need to show that its time-of-day rates are consistent with the TAC using the call volumes on its network over the previous year. The new entrant, Guernsey Airtel, will need to use forecast figures for the first year in setting its MTR rates. This forecast will need to be reviewed and approved by the OUR.

The new rates are to come into effect on 1st April 2007. All operators need to submit their proposed MTRs to the DG by 2nd March, along with call volumes per period for the last full year for which data is available to demonstrate compliance with the TAC.

2. Structure of the Decision Paper

2.1. Structure of Decision Paper

The rest of this paper is structured as follows:

Section 3: sets out the legal and regulatory background to the DG's proposals for regulating MTRs;

Section 4: summarizes some of the issues raised in the consultation process, the views of respondents on the draft decision, DG's response to those submission, and the DG's final decision;

Section 5: sets out the next steps for operators to submit their MTRs to the DG.

2.2. Comments Received

The invitation to comment on the proposed decision set out in Document OUR 06/19 was taken up by three parties:

- C&W Guernsey ;
- Guernsey Airtel; and
- Wave Telecom.

The DG wishes to thank those who have responded to the draft decision paper for their contributions. In accordance with the OUR's policy on consultation set out in Document OUR 05/28 – "*Regulation in Guernsey; Revised Consultation Procedures*", non-confidential responses to the draft decision are available on the OUR's website (www.regutil.gg) and for inspection at the OUR's Office during normal working hours.

3. Legal Background & Regulatory Framework

3.1. Legal Background

Section 5(1) of the Telecommunications (Bailiwick of Guernsey) Law, 2001 (the "Telecoms Law"), provides that the DG may include in licences such conditions as he considers necessary to carry out his functions. The Telecoms Law specifically provides that such conditions can include (but are not limited to):

- conditions intended to prevent and control anti-competitive behaviour; and
- conditions regulating the prices, premiums and discounts that may be charged or (as the case may be) allowed by a licensee which has a dominant position in a relevant market.

Under section 10(2)(c) of the Telecommunications (Bailiwick of Guernsey) Law, 2001, a licensee found to be dominant in a relevant market is obliged to provide interconnection and access on "terms, conditions and charges that are transparent and cost-oriented".

In addition, Section 10(4) of the Telecoms Law provides for the DG to require a licensee to justify the costs of and charges for providing interconnection or access and to show that those charges are derived from actual costs.

These provisions allow the DG to regulate MTRs, should there be a need for regulatory intervention.

3.2. Regulatory framework

In OUR 05/12, the DG set out proposed findings on market dominance in Guernsey following a review of the mobile market. He proposed to find both C&WG and Wave dominant in the wholesale mobile telecommunications market on their respective networks.

Following this consultation and the acceptance of this proposed finding by both parties, the DG therefore adopted this conclusion in the final decision, OUR 05/19:

> *"The Director General finds C&W Guernsey Limited dominant in the retail mobile telecommunications market and both C&W Guernsey and Wave Telecom dominant in the wholesale mobile telecommunications market on their respective networks."*

In accordance with these provisions, C&WG's and Wave Telecom's Mobile Telecommunications Licences include the following condition:

"The Director General may determine the maximum level of charges the Licensee may apply for Licensed Telecommunications Services within a Relevant Market in which the Licensee has been found to be dominant. A determination may;

a) provide for the overall limit to apply to such Licensed Telecommunications Services or categories of Licensed Telecommunications Services or any combination of Licensed Telecommunications Service;

b) restrict increases in any such charges or to require reductions in them whether by reference to any formula or otherwise; or

c) provide for different limits to apply in relation to different periods of time falling within the periods to which the determination applies."

This condition therefore allows the DG to regulate the prices that a licensee charges for its telecommunications services in a way and for a time that he deems appropriate, provided the licensee has a dominant position in the relevant market.

An identical clause is included in Guernsey Airtel's recently issued licences. The methodology and logic employed in deeming Wave and C&WG to be dominant on their respective networks would be expected to deliver a similar conclusion for Guernsey Airtel's network, i.e. Guernsey Airtel once it commences the provision of mobile services, will be dominant in the wholesale mobile telecommunications market on their network.

The DG invited comments on the proposal that Guernsey Airtel should be deemed to be dominant (for the same reasons as apply to C&WG and Wave) on its network for the purposes of regulating MTRs.

One respondent commented on this proposal, and agreed that Guernsey Airtel should be deemed to be dominant on its own network for the purpose of regulating MTRs. The DG also noted that Guernsey Airtel's response assumes that the MTR will apply to its tariffs, thereby implicitly assuming that the licence clause cited above will be put into effect.

DG's decision:

The DG deems Guernsey Airtel as dominant in the wholesale mobile telecommunications market on its network

4. Regulating MTRs in the Bailiwick - Summary

Sections 4.1 and 4.2 below summarize the issues around MTRs and the need for regulatory intervention. A fuller discussion of these points, and further review of data from the UK, Europe, and Jersey, can be found in the consultation paper (OUR 06/14) and the draft decision paper (OUR 06/19).

4.1. Is there a need for Intervention?

The consultation paper outlined the history of regulation of termination charging, with respect to the development of the mobile market. In the early days of mobile telephony, mobiles were regarded as a 'luxury'. In these circumstances network operators could set these unregulated charges high and both they and fixed-line operators could pass these costs on to callers, who accepted them as reasonable for the new services.

Since then mobile telephony has become a very standard element of daily life, with near total penetration rates in developed countries. However, while most countries have several network operators competing for customer subscriptions, this competition does not necessarily extend to termination rates. There are several reasons for this:

- firstly, termination charges are generally passed on to the calling party in the cost of their call (under the arrangement known as 'calling party pays' or "CPP") and so do not affect a subscriber being called and therefore do not have a direct effect on the subscriber's decision on which network to subscribe to;

- secondly, callers have no control over which network the person they are calling belongs to; and

- finally, while reciprocated high termination charges will affect the called party indirectly, if all mobile networks have similarly high termination rates then the net uncompetitive effect of these will be neutralised.[1]

Thus, it can be the case that, even in a mature market with significant levels of competition, there remains scope for the tacit maintenance of high mobile termination rates, sustained by the potential losses caused by unilateral deviation from these. While there is often the argument made that the excess returns generated from high termination charges are competed away through low (or even subsidised) prices on handsets and monthly line rental, and that any lowering in termination charges will have a corresponding upwards pressure on another part of the price structure (known as the 'water-bed effect'), such situations are at best opaque and it is generally not satisfactorily demonstrated that this is the most efficient way of structuring charges.

[1] Other effects, such as handset subsidisation for subscribers through high termination rates for off-network callers, will also be attractive to network operators, although again these will cancel each other out when applied by all network operators, resulting in high termination rates all round.

4.2. MTRs in the Bailiwick

The consultation paper set out the current MTRs for C&WG and Wave. These are shown in Table 1 below.

Table 1: Mobile Termination Rates (ppm)

Time of Day	Wave GSM	C&WG GSM
Daytime	12.60	12.60
Evening	9.84	9.84
Weekend	6.82	6.82

Source: Operators.

The table shows that the two operators' mobile termination rates are identical. Based on information received to date from the Bailiwick's mobile operators, the DG had concerns that these rates are not necessarily cost based. Operators were invited to provide updated information to show the extent to which the rates charged are indeed based on costs incurred.

As noted in section 3.2 both C&WG and Wave were found to be dominant in the wholesale mobile telecommunications market on their respective networks and the CPP arrangements in place would indicate that the potential for pricing above cost exists for both mobile operators. Furthermore, the mobile termination rates in the Bailiwick reveal a similarity in the amounts charged that does not necessarily suggest a high level of competitive forces operating in these markets.

The consultation paper included graphs showing the Peak and Off-Peak[2] MTRs for a number of jurisdictions including those within an IRG study. For the Peak charges, C&WG and Wave had the third highest MTR of the 31 jurisdictions. For the Off-Peak charges, C&WG and Wave had the ninth highest MTR of the 31 jurisdictions.

Experience in other markets has demonstrated the need for regulators to intervene directly in the setting of MTRs. In particular, the DG has noted the views of the ERG in this regard.

In addition, it is clear that it has been seen as necessary to regulate MTRs in most European jurisdictions. It would seem reasonable to conclude that the possibility of excessive mobile termination rates is a widespread issue for regulatory authorities. Given this, and in light of the levels of rates prevalent in the Bailiwick in comparison with those in other European countries, the DG in his draft decision proposed to intervene in a proportionate manner in the setting of MTRs by mobile operators within the Bailiwick.

[2] For the two Bailiwick operators, Off-peak rates were calculated as a straight average of Evening and Weekend rates, with the Total figures calculated as an average of Peak and Off-peak rates.

In his draft decision, the DG proposed to adopt the mobile termination approach used by Ofcom as a basis for setting MTR rates for the Bailiwick, with a TAC of 6.75ppm. The Ofcom charge control is on the average of all of an operator's MTR charges for terminating voice calls (i.e. daytime, evening and weekend charges), weighted by the relative call volumes (in minutes) on their network in the previous year. The charge controls required that, during each period of the control, the Average Interconnection Charge ("AIC") set by the each operator should not exceed the Target Average Charge ("TAC") set by the regulator. Operators can set different termination charges for different times of the day or week, providing the weighted average (AIC) of these falls below the TAC.

The DG also proposed that these rates be fixed for a period of three years.

4.3. Responses to Draft Decision

One respondent welcomed the OUR's proposals on both the rate and period of enforcement of MTRs in Guernsey. The respondent stated that the OUR had not suggested a means for applying the time-of-day (TOD) gradient. This respondent proposed that consistent TOD charges should apply for all operators, and suggested that the call volumes terminating on their network should be used as the basis for the TOD pattern. This respondent provided proposed rates for Peak, Off-Peak and Weekend periods, and stated that the gradients could be recalculated if it was felt this was appropriate.

Another respondent was also not clear on whether the OUR was proposing a flat rate across all times or proposing that operators apply their own network usage gradient to get TOD MTR rates based on the TAC of 6.75ppm. The respondent also asked if the DG was proposing to introduce a check process to ensure that the gradients proposed by the operators are correctly calculated to reflect their network usage, and if the DG was proposing to allow changes to the MTR on an annual basis. The respondent also queried how new entrants would set their rates in the absence of any historic traffic data.

This respondent also raised a number of points relating to the transit charges that are payable to interconnect with C&WG's fixed network.

A third respondent was broadly in favour of the decision to set a TAC of 6.75ppm for the period of three years; this respondent was of the view that a reduction to even lower levels would be more beneficial to the market by creating a greater incentive for operators to improve efficiencies. With MTR rates falling globally, the respondent would also prefer to see the rate reviewed annually. This respondent was also of the view that new entrants should be incentivised during the first few years of operation; this could be achieved through the provision of a lower rate for calls that originate on the new entrant's network and terminate on the networks of established operators locally. They recognised however that such an approach is likely to be contentious.

DG’s Response

The DG’s draft decision set out a Target Average Charge (TAC) of 6.75ppm. As the name implies, and as detailed in the consultation paper, this is an *average* charge; operators are free to set MTRs for various periods, so long as the TAC is achieved; the MTRs for each period will be such that the TAC is achieved when the MTRs per period are applied to the volumes per period for the preceding year. Operators may also set MTRs such that the average charge is below the TAC.

The DG will have a check process to ensure that the MTRs for each of the operators are consistent with the TAC. Each operator will need to submit their respective call volumes per period for the previous year, together with the proposed MTRs, to demonstrate that the TAC is thereby achieved. This is a simple yet effective approach. New entrants will not have call volumes for the previous year, and therefore will need to provide forecast data for the first year for review and approval by the DG. The DG will reference such forecast volumes against the volumes of incumbent operators to ensure that those forecasts are reasonable. Operators are free to set reciprocal rates for the various periods if they so wish; again, they will simply need to demonstrate to the DG that the average MTR will be at or below the TAC.

The DG has noted the view of one respondent that new entrants might be incentivised through a different charge for such operators. The DG however is not in favour of setting different TACs for specific operators as part of this review.

Finally, the DG is of the view that the issue of transit charges for accessing C&WG’s fixed network before terminating on C&WG’s mobile network is somewhat separate to the issue of setting a TAC for MTRs. However, should any licensee have specific concerns on this matter they may wish to provide further details to this Office.

4.4. DG’s Decision

As set out in the draft decision paper, the DG sees it as appropriate to adopt the mobile termination approach used by Ofcom as a basis for setting MTR rates for the Bailiwick.

The Ofcom charge control is on the average of all of an operator’s MTR charges for terminating voice calls on their 2G networks (i.e. daytime, evening and weekend charges), weighted by the relative call volumes (in minutes) on their network in the previous year. The charge controls required that, during each period of the control, the Average Interconnection Charge (“AIC”) set by the each operator should not exceed the Target Average Charge (“TAC”) set by the regulator. Operators can set different termination charges for different times of the day or week, providing the weighted average (AIC) of these falls below TAC.

The DG has decided that each operator will be free to set MTRs for different periods, provided that the average charge is at or below the TAC. Each network operator will need to show that its time-of-day rates are consistent with the TAC using the call volumes on its network for the previous year. The new entrant, Guernsey Airtel, will need to use forecast figures for the first year in setting its MTR rates. This forecast will need to be reviewed and approved by the OUR.

In order that an efficient cost standard is used, this rate will not change with inflation. A **TAC of 6.75ppm,** fixed over three years, will allow all operators time to improve efficiencies in line with this rate over the three year period.

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Table 4: Mobile Termination Rates (ppm)

	New Rates; Target Average Charge	Current C&WG	Current Wave
Daytime	**TAC: 6.75**	12.60	12.60
Evening		9.84	9.84
Weekend		6.82	6.82

This TAC will come into effect on 1st April 2007. Operators will need to submit their proposed MTRs by 2nd March 2007, together with evidence that it is consistent with the TAC when based on call volumes terminated on its network for the last full year for which data is available (i.e. the most recent consecutive 12-month period for which data is available).

The DG will review wholesale mobile termination rates at the end of the three year period, and will also consider whether other mobile services (beyond voice) require regulatory intervention at that time. The DG will be guided by developments in the market in this regard.

The DG may also review the mechanism for setting MTR rates if he has reason to believe that relative call volumes in the different periods may be changing significantly from one year to the next.

Decision

The Target Average Charge for MTRs for mobile operators in the Bailiwick will be a maximum of 6.75ppm. This rate will be fixed for three years. This rate will apply to all voice calls terminated on both 2G and 3G networks, and the same rate will apply regardless of the network type the call is terminated on.

The DG requires each operator to submit their proposed MTRs, together with call volumes per period for the last full year for which data is available, thereby demonstrating that the TAC will be achieved when using these volumes. Submissions should be made before 2nd March, with the MTRs to come into effect on 1st April 2007.

5. Next Steps

The revised MTR rates will come into effect on 1st April 2007. Operators now need to submit their proposed MTRs by 2nd March 2007, together with evidence that it is consistent with the TAC based on call volumes terminated on its network over the most recent consecutive 12-month period for which data is available.

Guernsey Airtel will need to provide forecast volumes for the year 2007, and use these to set the MTR. The DG will review this forecast to ensure it is reasonable and an appropriate basis for MTR rates.

The DG believes this approach is straightforward, simple, minimizes the burden on network operators and the OUR alike, while ensuring that the TAC is achieved and compliance demonstrated. The DG believes this approach should ensure that consumers benefit from the reduced MTR rates at the earliest possible opportunity.

ENDS