ERG Draft Common Position on NGN Charging Mechanisms - Long term termination issues

GSMA Europe response

10 December 2009

Martin Whitehead
Director GSMA Europe

Park View, 4th floor
Chaussée d'Etterbeek 180
1040 Brussels

E-mail: mwhitehead@gsm.org
www.gsmeurope.org

Europe

ERG Draft Common Position on NGN Charging Mechanisms - Long term termination issues

GSMA Europe Response

SUMMARY

- GSMA Europe (GSMA) welcomes the opportunity to comment on the ERG's Draft Common Position on Next Generation Networks Future Charging Mechanisms/ Long Term Termination Issues ("the Consultation").

- The GSMA has a highly diverse range of operator members.
  - There are large differences between operators, including in terms of absolute and relative subscriber numbers, average revenues per user, competitive strategies over time, current market positions and ownership relationships with fixed operators and with operators present in other Member States.
  - There are also significant differences between the mobile markets in which they operate, such as in relation to market size, geography and population density, general income and cost levels and the competitive alternatives available.

- A major change in regulation to implement a BAK regime would therefore affect mobile operators in different ways.
  - Some operators are net acquirers of termination minutes from other operators, while others are net providers and hence the elimination of termination charges can cause significantly different effects on operators' overall revenues and costs.
  - Operators also have different views of the effects of a move to BAK on the level of competition in the respective national markets.

- This response aims to provide a balanced mobile industry view, identifying both areas of agreement across the industry, as well as areas where mobile operators have differing views as to the approach that would best promote overall consumer welfare.

- A large number of operators have serious concerns with the analysis presented in the Consultation.
  - These operators believe that the Consultation has failed to adequately consider the likely upward pressure on mobile retail prices, and that BaK would actually lead to certain European consumers paying much more, not less, for their mobile services, or not having a service at all.
  - This group of operators believes no compelling evidence has been presented that BaK will offer substantial benefits to consumers over the current regime, while, on the other hand, it carries a number of serious risks.

- A minority of operators consider that current termination charge levels are creating a barrier to their growth and that the move to BaK would deliver lower call prices and higher usage, as well as greater competition.

Europe

- The GSMA believes that the migration to all-IP networks and services raises important regulatory questions. Increasing substitutability of services and access platforms calls for a review of existing regulatory obligations, whilst ensuring regulation that is retained, does not distort competition between different technologies, such as between traditional voice providers and new IP-based service providers.

- However, the application of a common set of regulatory principles does not imply a single interconnection charge or, indeed, no charge. Important differences will continue to exist between the cost levels and structures of mobile and fixed networks.

- The GSMA is of the view that BaK requires further analysis and evidence. A number of serious flaws with the ERG's international comparisons have been identified in this response and those problems warrant further research.

- In addition, there are a range of transitional problems and questions that need to be addressed.

    - The implementation of BaK would require regulators to determine a number of difficult technical issues. A failure to adequately resolve these would risk numerous disputes between providers and regulators, as well as harmful distortions to network design and investment.
    - Consumers in countries that move to BaK first could be disadvantaged vis-a-vis consumers in countries that continue a CPNP regime, given that outpayments to CPNP networks would need to be recovered from retail prices by the BaK networks.
    - BaK would shift a proportion of the cost of making a call to the receiving party, which is likely to create a significant growth in nuisance calls and SPIT.
    - While the Consultation focuses on voice services, it omits to address whether BaK is being considered to be imposed on a wider range of services. Such an extension would raise additional questions and serious concerns.
    - It is not clear how BaK would be imposed under the current European regulatory framework from a legal perspective and in a fair way that does not disadvantage some Member States over others or, indeed, over non-EU countries.

- In the mean time, current regulatory processes are likely to lead to further reductions in termination charges. Examining the impact of these reductions may provide useful guidance as to whether the complete elimination of termination charges would be likely to promote welfare or harm consumers and whether the migration to BAK can have any added value in this regard.

- The migration to all-IP networks is also proceeding and the analysis of actual developments in markets and services should be considered when assessing which interconnection charging models are likely to best benefit consumers in the long term.

- The GSMA wishes to contribute positively to the development of a harmonised European approach to the regulation of mobile termination charges and is willing to assist the ERG further in understanding the effects of reductions under current processes and in determining what approach regulators should take in the longer term.

EVOLUTION TOWARDS AN ALL-IP WORLD

Operators are progressing well in the migration to an all-IP world, including through network modernisation and the introduction of new services and applications, although the international economic downturn could entail some delays in investment plans. Migration to IP networks is driving fundamental changes in the telecoms industry structure. Yesterday's industry structure organised by vertical networks will migrate to access independent service provisioning. The all-IP architecture will give customers access to services and content independently and seamlessly across networks and devices.

GSMA welcomes the interest by the ERG to debate the implications for regulation, which objectives should be to ensure regulatory frameworks are conducive to the roll out of next generation access (NGA) networks and the development of innovative new products and services.

In this section, the GSMA wishes to highlight three aspects of the migration to all-IP networks which have been given insufficient attention in the ERG's Draft Common Position.

Migration to an IP-World is increasing competition

For mobile operators, the evolution to all-IP networks means a significant broadening of their competitive landscape:

- Fixed mobile convergence and substitution are driving increasing competition between fixed and mobile networks;
- Alternative wireless technologies are emerging as a potential alternative to mobile networks; and
- Mobile operators face growing competition from an increasing range of internet service providers and other players.

The growing competitive interactions between different platforms and providers have key implications for regulation. First, today's communications services bottlenecks may not be replicated in an all-IP world and therefore regulators should take into account actual and foreseeable market developments which call for the removal of some existing regulation. Second, new regulation or competition law intervention may be required to prevent players with dominant positions in other sectors from being able to use convergence to leverage their dominance into communication services. Third, where regulation is imposed, it will be important to ensure that it is imposed in a neutral way across all competing providers, so as to avoid distorting market developments.

Key differences continue to exist between mobile and fixed technologies

The Consultation notes the transition to NGN networks is leading to lower costs of voice services and that the difference in cost per minute between fixed and mobile is decreasing. However, during the transition phase towards an all-IP NGN world, operators will continue to run parallel fixed and mobile networks, which have commonly recognised differences in the costs of termination. Therefore most operators believe that it is inappropriate to impose a convergence of termination costs across fixed and mobile networks. Rather, in this period of transition, maintaining the existing termination charging models is the appropriate means to ensure continued network investment and development. It will continue to be important for regulation to recognise the fundamental differences between the costs of mobile and fixed technologies and the manner in which those costs are recovered.

A major source of difference is in relation to the costs of the access network. In fixed networks, the access network is primarily composed of local loops that are dedicated to individual customer premises. The cost of the local loop is, traditionally speaking, not sensitive to the amount of traffic it carries. In mobile networks, the radio access network is comprised of base stations, related equipment and the radio spectrum. Carrying higher traffic volumes across mobile networks will generally require an increase in many network elements particularly in the relatively expensive radio access network to avoid network saturation. For example, additional cell sites have to be acquired to support higher traffic volumes given limited spectrum resources. The cost of supporting that traffic will include the opportunity cost of spectrum and coverage capacity that could otherwise have been used to carry other services.

Most operators believe that the supply of mobile termination will continue to result in a significant cost to operators which should be reflected in termination charges. These operators note that regulators' cost models have found that the type of 2G/3G mobile networks that can be expected to remain common across Europe over at least the next 5 years have a significant, non-zero cost of termination. These operators also believe that sound efficiency reasons exist for termination charges to contribute to recovering their share of fixed and common costs.

Other operators believe that while termination services will carry a cost, the existence of calling externalities implies that these costs should be efficiently recovered from a mobile operator's own customers. We examine these efficiency arguments further in Section 2.

Despite the disagreement about the different measures of relevant cost that should be used to calculate termination rates, there is agreement that termination services carry a non-zero positive cost and consideration of BaK type models should not detract from NRA's ability to establish the appropriate costs in each market.

Distinction between "boundary BAK' and 'transit' not applicable to mobile

The ERG proposes a definition of BAK whereby BAK only applies at a certain specified boundary (set of PoIs) of the termination network, and not to transit services. The document stipulates that this removes some of the concerns with moving to a BAK regime. It further explains the importance of setting the appropriate boundary in defining the PoIs.

This proposed approach does not fit the mobile termination model, as it does not have the distinction between origination, transit and termination that is applied in the fixed environment. Indeed, the base station and the Mobile Switch Centre are part of the termination service and no transit services are offered at all. It is unclear how the ERG would address this disparity, which would result in mobile networks not being able to recover costs in the same fashion as fixed networks.

Regulatory-imposed BaK is not the model of today's Internet and carries significant risks

If BAK is taken to mean the absence of interconnection charges as per the consultation document, then BAK cannot be said to be the only model that characterises today's Internet. Rather, the Internet relies on a variety of commercially negotiated charging arrangements. Some networks do exchange traffic between each other without any payments being exchanged; however, this generally requires that the traffic between the networks is reasonably balanced. Retail Internet Service Providers, on the other hand, will generally pay upstream networks for data that is downloaded and will need to recover this cost in their charges to retail customers.

Most operators believe that it would be wrong for regulators to impose BaK on the basis that it is a necessity to provide for parity with the Internet. In particular, operators believe the performance of the Internet, based on its complex charging approach and on the flexibility for payments where traffic is out of balance, does not offer support for the regulatory imposition of BaK as a single, universal charging model. Commercially negotiated interconnection arrangements (as are found for Internet interconnection) provide operators with the flexibility to change their charges as required to support innovative new services and to address risks such as significant traffic imbalances, arbitrage and nuisance calling behaviour. The ability of operators to respond in this way provides a powerful deterrent to service providers engaging in practices that harm consumers and efficiency. We are not aware of any significant experience of BaK being imposed by regulation as the single charging model to apply across fixed and mobile interconnection.

Given the range of risks associated with the regulatory imposition of BaK, such a major shift in the regulatory paradigm should not be carried out unless (i) there is clear evidence that the change would bring significant benefits and (ii) that arrangements can be implemented to address the risks. We consider these issues in the next sections.

ASSESSING BAK COMPARED WITH CURRENT REGULATION

All operators believe that a proposed major change in the interconnection regime should first be subject to a rigorous, evidence-based impact assessment. A substantial reduction in mobile termination revenues can be expected to significantly affect the mobile industry and consumer outcomes in Europe. The ultimate effects will depend on the precise pattern of impacts across individual operators in particular markets. As such, the net impact will be different for each operator, and will differ across Member States.

In this section, we first explore the mechanisms by which changes in interconnection charges (including eliminating interconnection charges altogether) affect operator pricing. We then examine operators' views on the likely impact of BaK against a range of criteria:

- Overall consumer welfare and efficiency;
- Distributional effects as between different groups of consumers;
- The level of competition;
- Effects on investment, cost minimisation and other potential commercial effects; and
- The Cost of regulation.

Mechanisms by which interconnection charges impact retail pricing

The Consultation Paper assumes that eliminating termination charges would bring down the cost of calls and thereby call prices. However, the majority of operators, including a number of smaller operators, believe that they will not be in a position to simply absorb the loss of a large share of their termination revenues. They believe that either other prices will need to rise to avoid losses on individual tariffs and potentially losses overall, or mobile operators will have difficulties in covering their costs with the consequence of deterring new investment.

The majority of operators point to economic theory that shows that changing the margin received from one side of platform (or 'two-sided') markets, like mobile networks, will impact the pricing of the other services provided over the platform. Regulators such as the UK Competition Commission have investigated this issue and accepted that there will be a strong 'waterbed' or rebalancing effect across mobile services, i.e. "*most of the reductions in revenue from termination charges being capped will be recovered from the retail market*".[1] While the Consultation Paper does not mention the waterbed effect, it does make some reference to the "*zero sum nature of termination revenues*" which provides at least some recognition that operators will still need to recover their total costs.

Empirical studies of the impact of reductions in termination charges to date suggest the existence of a strong waterbed effect, in terms of prices for other services being higher than they otherwise would be.[2] This implies that the impact of regulation can only be assessed by

1 UK Competition Commission, Calls to mobiles report, 2003, para. 2.563.

2 Genakos, C. and T. Valletti, "Testing the waterbed effect in mobile telephony", CEP Discussion Paper No. 827, October 2007 (available at http://cep.lse.ac.uk/pubs/download/dp0827.pdf) and K. Andersson

examining the likely pattern of price changes and the consequence of such changes for demand and consumer welfare.

A number of smaller operators, however, agree with the Consultation that lower call prices will be the primary effect of a move to BaK. They believe that the current levels of termination charges have been a key factor inhibiting their growth and their ability to provide greater competitive discipline on the larger operators. Certain later entrants, in particular, find themselves making significant net termination payments to other operators. These operators expect that the proposed cuts in termination charges will lead to significantly lower off-net call prices, which in turn will enable them to compete more effectively for subscribers.

We outline below some of the potential positive and negative price effects that could result from a shift to BaK.

Lower prices to call mobile phones

Operators agree that lower fixed-to-mobile call prices are a likely outcome of lower mobile termination charges, although the exact extent will depend upon the level of 'pass-through' by fixed operators.[3] The effect on off-net call prices is less clear cut and may vary in different markets. Lower termination out-payments will lower the cost of supplying off-net calls. However, the waterbed effect could lead some operators to seek to recover more of their costs in off-net prices to compensate for the lower termination revenues that they receive.

Higher mobile retail prices

If termination rates are reduced, many operators believe that they will need to increase prices, or reduce prices less than otherwise, to cover costs that were previously covered by mobile termination.

This may be implemented in different ways. It could lead to higher subscription charges and/or handset prices. Alternatively or in combination with other effects, some operators believe other mobile retail prices may increase so that they can cover their costs.

In particular, operators may no longer be able to offer the same level of handset subsidies going forward or may be forced to remove some current low-end monthly price plans which are no longer viable to offer. In markets where mobile retail prices are on an underlying downward trend, price rebalancing (particularly if regulatory changes are made gradually) may not result in actual price rises but may lead to prices not falling as quickly as otherwise.

The exact changes are difficult to predict and will vary depending on operator positions and market characteristics. Operators have different views as to the extent of rebalancing and in

and B. Hansen, "Network competition: Empirical evidence on mobile termination charges and profitability".

[3] In this regard, we note that Ofcom found that only two-thirds of previous reductions in termination charges in the UK had been passed through into lower fixed-to-mobile prices (Ofcom, Mobile Call Termination Statement, 27 March 2007, para. 3.22). There is evidence that following the removal of regulation on BT's retail prices, BT has failed to pass-through more recent termination charge reductions in its fixed-to-mobile call prices.

relation to the evidence on the impact of earlier, albeit more gradual, reductions in termination charges.

Impact on pre-paid tariffs

The European mobile communications model has flourished through the development of prepaid market that allows customers the flexibility to purchase telecommunications services as and when they need to without minimum monthly commitments. However, a significant proportion of prepaid customers receive many more calls than they make – indeed, a large number of prepaid customers make very few calls. Current prepaid plans may not be sustainable if termination charges are substantially reduced. Operators might be forced to raise calls prices or impose minimum monthly spend requirements in order to cover their costs.

Difficulties of international comparisons

The case for BaK presented in the Consultation relies heavily on the view that consumer outcomes in countries with BaK-type charging models are superior to European market outcomes.

It is generally very difficult to construct reliable international comparisons, particularly across such diverse markets. For example, the interconnection regime will be only one of many factors influencing market outcomes, together with factors such as general cost and demand differences, the competitiveness of fixed services and the use of SMS as a substitute for calls. These factors should be accounted for in a thorough econometric analysis.

Weaknesses of the international comparisons presented by the ERG include:

- Small sample size of BaK countries. The comparison is based on only three “BaK” countries. None of these countries strictly adopts BaK across mobile and fixed interconnection. Further, Canada has been excluded from the BaK sample. However, Canada may provide a more realistic comparison to the likely impact in Europe compared with Hong Kong and Singapore, which are densely populated city states that are likely to have very low unit costs in supplying mobile services. Canadian GDP per capita (in PPP terms) is also closer to European GDP per capita while Singapore, the US and Hong Kong all have significantly higher GDP per capita.

- Assumptions have great impact on results. The ERG adjusts usage for the known problem that on-net calls are double counted in “BaK” countries where customers are billed for calls made and received. However, the Consultation only adjusts usage assuming that 20% of calls are on-net – this is lower than in many European countries. In the US, where standard tariffs provide for unlimited on-net calls, the share of on-net calls in total calls would be expected to be much higher. The usage figures for BaK countries therefore seem to have been significantly overstated.

- Other factors are likely to explain outcomes. For example, usage in Canada is similar to usage in Europe, so higher usage in the selected "BaK" countries may reflect factors specific to those countries, rather than the interconnection regime.
- The Consultation relies on average revenue per minute as a proxy of prices. However, to the extent that minutes remain overstated in "BaK" countries, average revenue per minute will be understated in those countries compared with CPNP countries. Average revenue per minute comparisons can also be distorted by differences in the mix of services in different countries. For instance, if total revenue from all services is used then differences in the use of data and SMS could result in average revenue per minute being a poor proxy for voice call prices. Even voice revenue comparisons can be impacted by differences in the mix of voice calls consumed (e.g. the mix of peak and off-peak on-net, off-net, local, national, international and roaming calls).
- The Consultation also ignores the result of the CEG econometric study for Ofcom which found that:
  - Mobile take-up is higher, the higher the level of mobile termination charges; and
  - There is no robust statistical evidence of a relationship between termination rates and usage or between termination rates and retail prices.

Given the data problems and the different conclusions reached, the international comparisons do not provide a sound basis for a major change in interconnection regime.

Impact on overall consumer welfare and on different customer groups

Whether a move to BaK promotes or harms overall consumer welfare will depend on whether the benefit of lower prices to call mobiles is outweighed by the cost of higher mobile retail prices. There is a difference between the majority of operators and a small group of operators on this point, reflecting their varying perspectives as to the likely direction of price changes, as well as the consumers' responses to these price changes (i.e. the elasticity of demand for the different services including for mobile subscriptions). Operators also have differing views in relation to the relevance of externalities, with the majority of operators believing that calling externalities are largely internalised by regular calling patterns between customers and hence do not provide a reason for favouring BaK over the CPNP.

It is also likely that different types of customers may be affected in different ways based on their individual call usage.

A majority of operators believe that the distributional effect of a change to BaK should be a serious concern for regulators which cautions against the adoption of BaK. In particular, these operators believe that BaK will primarily benefit high usage customers who make more calls than they receive. For these customers, potentially higher subscription charges could be offset by lower call prices.

On the other hand, BaK is likely to impact adversely low usage customers who mainly receive calls. These customers may face a significant increase in the overall cost of their mobile service as termination revenues from people calling them would no longer contribute to the cost of their connection. Low usage customers are disproportionately likely to be low income customers. Low income customers are also likely to be harmed if current prepaid tariffs are made unsustainable by a move to BaK. The budgeting control offered by current prepaid tariffs which do not require monthly expenditure commitments has been of particular benefit to consumers with limited incomes.

A minority of operators believe that there would not be significant adverse impacts for any group of consumers. This minority of operators believe that BaK will deliver a more efficient pricing structure and will promote competition in mobile markets to the benefit of consumers generally.

Effects on investment, cost minimisation and other commercial effects

The European mobile industry, and the telecoms industry in general, is still in the process of implementing a substantial investment programme. Many operators believe that the incentive to continue high levels of investment will be weakened by the substantial uncertainty that would result from a move to BaK as well as the risk of lower returns arising from an inability to fully or quickly recover lost termination revenues in other charges. On the other hand, a minority of operators believe that overall uncertainty will reduce as a result of elimination of drawn out regulatory processes relating to estimating termination costs.

A majority of operators also disagree with the Consultation's argument that "*moving cost recovery from termination, which is a regulated market, to competitive retail markets increases incentives for cost minimization as more cost are subjected to competitive cost recovery*".[4] This argument ignores that the same network elements are shared by termination and origination and hence the costs are already subject to competitive and shareholder discipline. Further, if the result is that customers switch from relatively low cost fixed services to make a greater share of their calls on mobiles then overall costs may increase.

As well as the assessment of whether a move to BaK would ultimately promote or harm consumer welfare, there are also a host of transitional issues in relation to implementing BaK. We turn to consider these next.

[4] The Consultation, p.6.

ISSUES REGARDING THE TRANSITION PHASE

The GSMA believes that there are substantial issues that would arise from implementing BaK and that these would need to be thoroughly examined and addressed before such a change was carried out. The limited examination in the Consultation of these issues is inadequate and needs to be expanded further, given their potential significant implications,

Revenue loss to non-BaK countries

The Consultation notes a problem that would arise from BaK being implemented in some countries but not others. In particular, the BAK countries would end up subsidising CPNP countries and the Consultation estimates that this would be "*a cash flow to the CPNP domain that is a few percent of all mobile voice revenue.*"

The amount of cross subsidy could be much higher in countries with a higher share of international traffic to CPNP countries. Moreover, even if BaK were implemented across the EU, this would still leave European consumers overall subsidising other countries that retain termination charges. Operators believe that they would not be able to effectively prevent such a loss – it would not be technically or legally possible to discriminate termination rates based on the originating network.

Arbitrage would be likely to arise if charges were imposed on termination services received from some operators but not others. The overall loss of revenues to European operators would need to be compensated by raising more revenues from European consumers.

New technical regulation and the risk of disputes

BaK would require significant new technical regulation. In this response, we discuss three potential issues to illustrate the types of problems that can arise.

First, regulated BaK would effectively offer free access to networks and is likely to encourage many providers with no networks of their own to send traffic without bearing any of the cost of doing so. To prevent network congestion, regulators may then have to define who should be allowed to connect, with such definitions likely to be the source of numerous disputes.

Second, as the Consultation notes, BAK would require regulators to determine the number and location of points of interconnection. This is also likely to be a key source of dispute with each party (in the absence of a return) trying to minimise their cost and shift costs on to the other parties. For instance, a current termination service may contain a transit element so that regulators would be called upon to determine what is the transit element and what cost should the provider be able to recover in respect of this element.

Third, the absence of interconnection charges may lead to investment in capacity being inadequately compensated, with the result that quality of service may be reduced.

Nuisance calls and SPIT/SPAM

BaK fundamentally reduces the cost to the party making the call, while requiring the party receiving the call to bear a proportion of the cost. As a consequence, it risks leading to a growth in nuisance calls, by which we mean any calls that are not wanted by the receiving party. These may be commercial or non-commercial calls, and may be from fly-by-night businesses, for which other sanctions may be difficult to enforce.

Even if it is argued that the receiving party can hang up, the disturbance created by the phone ringing and potentially being answered should be treated as a cost to the receiving party. This is in addition to any receiving charge (or use of minutes in their monthly bundle) they may also have to bear. SPAM text messages were a significant problem in Europe prior to the introduction of SMS termination charges and email SPAM continues to be a major[5] problem.

Legal and regulatory complications

The imposition of BaK across the EU would create significant implementation problems under the established European regulatory framework. First, it is not clear that all voice providers, regardless of technology and market position, would be found to have Significant Market Power requiring the imposition of a charge control of zero.

Second, the ERG document does not address what would be the legal basis to impose BaK. Article 13 of the Access Directive provides for regulators to impose obligations for cost-oriented prices, however, BaK would require operators to provide termination services below cost.

Third, the regulatory period of the regulation currently applying to termination services differs significantly across Member States. This means that it is unlikely that Member States could move uniformly to BaK. However, if some Member States move to BaK significantly ahead of others, they would suffer a loss in revenues to the other markets, with the likelihood that consumers in those Member States would bear the consequences.

Fourth, complications may arise in relation to taxation regimes applicable to electronic communications services. The ERG should assess whether interconnection services may still be liable for VAT or other taxation based on an imputed fair value of the service, even if the service is effectively being bartered for termination services provided by other operators. BaK could require the development of detailed VAT agreements in each country, to prevent disputes with tax authorities on whether or how much VAT is payable on BaK traffic.

Implications for wider interconnection arrangements

While the Consultation focuses on voice services, a relevant consideration is whether BaK should be imposed on other services if it is to be imposed on voice. On the one hand, problems would arise from the regulatory imposition of BaK on voice exclusively. On the other hand, if BaK were to be imposed more widely including SMS and data services, then there would be the need to consider the range of effects of doing so. These are likely to include similar types of effects as would arise from imposing BaK on voice services, although their precise nature and impact on consumers may vary significantly (e.g. the volume and impact of nuisance calls may differ to the volume and impact of SPAM/SPIT).

The widespread application of BaK would also risk a more fundamental problem. The large efficiency and consumer benefits that all-IP Next Generation Networks offer depend on the

[5] Recent traffic analysis show that unsolicited messages amount to 90% of all e-mail traffic on average. See for example the metrics report by MAAWG (Messaging Anti-Abuse Working Group) at http://www.maawg.org/about/MAAWG_2008-Q3Q4_Metrics_Report.pdf

ability to offer services at specified quality levels, so that the type and quality of services demanded by consumers can be matched with the supply of these services in a least cost manner. Realising these gains will require interconnection charging models that support differentiated quality of service. Imposing a uniform charging model risks closing off the development of new services with differentiated quality of service and the consumer benefits they would bring.

The period of transition

A further issue to be addressed is how to determine the appropriate transition period. There are significant differences in current termination charges including between fixed and mobile charges, operators in different countries and operators in the same country. Most operators believe that the likely substantial disruption to current retail pricing and models would warrant a sufficiently long glide path to minimise price shocks to consumers and the risk to operator profitability from trying to impose severe, sharp reduction in charges.

Europe

WHAT SHOULD BE THE REGULATORY APPROACH?

Circuit based and IP based interconnection models co-exist today and the GSMA believes that markets are generally functioning well in the migration to all-IP NGNs. Most operators believe that there is no compelling evidence of a substantial problem with current regulation or that a shift to BaK would result in better overall outcomes.

The uncertainty over the eventual outcomes of BaK calls for a more thorough analysis to be undertaken. The ERG could undertake or commission an independent assessment of market outcomes in BaK and CPNP countries that seeks to address all key data problems. Further work is also needed in designing transitional arrangements that do not risk a large loss of revenues or significant consumer disruption.

In this regard, we note that the European Commission has recently tendered for a study on the future of interconnection charging methods. Such a study is likely to be most useful to the extent that its authors consult closely with industry on the range of issues and would benefit from assessing these issues and questions in further detail.

It is also the case that current EU regulatory processes are likely to lead to further reductions in termination charges over time. The impact of these reductions should be examined as they could provide useful guidance as to whether even lower termination charges would bring net benefits or costs to consumers. The migration to all-IP networks will also proceed and the evidence on new services and commercial arrangements should help inform the assessment of which interconnection charging model(s) are likely to be best for consumers in the longer term.

The ERG could help reduce the cost of current processes through developing guidelines on best practice in implementing cost modelling. Key principles include the use of transparent, consultative processes, evidence-based assumptions, proportionality, a robust impact assessment and ensuring that final decisions are clearly explained. Indexation from current charge levels may also provide an alternative to each regulator re-designing its cost model for each market review.

The GSMA does believe that technological convergence raises important regulatory issues. However, the question of which interconnection model should be applied is only one aspect. Of great importance is to ensure that regulation does not advantage some competing providers over others. This will support the efficient development of markets at a time when the substitutability of services and access platforms is increasing.

Regulators should continue to monitor the development and analyse the effects of the migration to NGNs. NGNs may require significant changes to regulation, however, any changes should be based on evidence of specific problems – and could call for less, rather than more, regulation.

GSMA Europe
10 December 2009