

SFR Response to the ERG public consultation on a draft Common Position on symmetry of mobile/fixed call termination rates

General questions

- QUESTION G1 :** Do you think that the principles outlined in the general economic introduction cover adequately the underlying economic situation of both mobile and fixed termination markets ?
- If yes, do you think they are sufficiently reflected in the two parts on “MTR symmetry” and “FTR symmetry” and that they are consistently applying the principles?
 - If no, what do you think is missing and which reasoning should be added?

The introduction discussing general economic principles does not properly reflect the actual situation of the fixed and mobile markets and their individual particularities from both a technical and economic point of view. “Convergence of fixed and mobile termination rates” is evoked without supporting analysis as to the “merits” of such an approach in the context of two radically different markets.

As concerns the mobile market, one must stress the real success of GSM in Europe: it is, indeed, one of Europe’s greatest industrial successes, both for manufacturers and for operators, all of whom have been subject to competition right from the start. The mobile market still produces regular innovations, particularly in respect of terminals and services. This situation contrasts notably with the fixed market which developed historically from a monopolistic operator and which demonstrates a slower rate of innovation particularly in respect of terminals.

The ERG document is sometimes ambiguous in respect of the “convergence” being discussed. For example, the ERG states that « *It has been argued especially by the European Commission that NRAs should start to specify convergence of all termination rates towards a single reference* »¹ (emphasis added). Yet, to our knowledge, the European Commission has never come out in favour of a “unique and uniform” termination rate for all operators, fixed and mobile. What the Commission has in fact done is to clearly state its desire for symmetry of mobile termination rates, as can be seen in Annex A of the ERG document setting forth the observations of the Commission with respect to NRA notifications on the mobile termination market.²

The ERG states that « *economic principles tend to recommend the setting up of a unique and uniform termination rate for all network operators* ». There is no analysis presented to support this statement, which is manifestly an arbitrary and theoretical position of principle.

¹ ERG public Consultation, page 5

² ERG public Consultation, pages 91 à 97

It is extremely surprising that this introductory section should discuss, and indeed support, the convergence of fixed and mobile termination rates, given that in its conclusion under the title "Perspectives", the ERG indicates that this question is not dealt with in the document: *« but the scope of this work has excluded another question which is the current asymmetry between fixed and mobile terminating tariffs »*³. Once again, the ERG puts forward a "plausible conclusion" without any real prior analysis, as seen in its arbitrary position: *« a harmonization of these methodologies between MT regulation and FT regulation could potentially induce a reduction of the existing asymmetry (...) leading to positive effects on competition between telecoms players, and ultimately on end-users. »*

There is no analysis presented in support of this suggestion of positive effects for market players and consumers.

Finally, the issue of convergence of fixed and mobile termination rates is a complex question which cannot be treated lightly and in fact requires a full and detailed analysis, in keeping with the significant matters at stake and possible impact on market players and consumers. One cannot and must not in any way take a position of "principle" in respect of such an issue by arbitrarily postulating "positive" results that have not been proven.

A convergence of fixed and mobile termination rates could lead to a sudden reduction in mobile termination rates, with major consequences on the functioning of the mobile market, perhaps even threatening the "calling party pays" billing system and seeing it replaced with the "receiving party pays" system for fixed-to-mobile calls, a change that consumers, who do not like the idea of "paying to be called", would not appreciate.

It should also be noted that the latest decisions of EU regulators in countries comparable to France have led to less significant tariffs reductions than in France, as the ERG graph shows on page 83. For 2008 and onwards, the French regulator is an exception to the rule, manifestly hoping to continue with a strong reduction, placing France's mobile call termination rates significantly below the EU average, as recognised by ARCEP in its most recent decision on this subject.⁴

Last but not least, it's necessary to keep in mind that general economic principles can't be solely NRAs drivers for their intervention, without attention on their decisions impact. In particular, a sudden and strong mobile termination rates reduction, so as to bring them closer to fixed termination rates, could have major consequences on operators financial accounts and *in fine* on sector economy.

³ ERG public Consultation, page 90

⁴ Voir Décision n°2007-810 de l'ARCEP, page 71 : *« de manière prospective, la majorité des régulateurs qui ont annoncé leurs décision pour 2008 ne manifestent pas de volonté de baisse plus rapide.(...) Aucun de ces pays, comparables à la France, n'a donc annoncé de niveaux inférieurs à 7 c€/min, même si certains ont déjà pris des décisions pour des horizons temporels longs, comme celui choisi par l'OFCOM (Royaume-Uni allant jusqu'en 2011). »*

QUESTION G2: Any further comments regarding consistent regulation of both MTR and FTR with regard to symmetry is welcome.

According to the ERG, « currently FTRs do not include access network costs while MTRs do. However, with mobile network operators increasingly competing for fixed customers, this might lead to a competitive disadvantage for fixed operators and a distortion of competition. In the light of this development, possible remedies to this problem need to be considered (i.e. converging fixed and mobile termination rates), e.g. either taking account of the access network costs when calculating the FTRs or not including them in the MTRs. »⁵

This is how convergence of the methods for calculating call termination costs and the levels of fixed and mobile call termination rates is envisaged by the ERG.

The fixed and mobile markets demonstrate significant differences in nature which preclude the application of a single regulatory approach :

- From the point of view of demand, fixed and mobile services are not substitutable. Although some fixed-mobile services are starting to emerge, substitutability between fixed and mobile services remains highly theoretical at this stage and, even in the longer term, largely limited. The only two examples cited by ERG, without any detailed analysis (namely Homezone, and bundles with ADSL access ⁶), illustrate the dangers of any hasty conclusion on this subject, at a time when the economic models for this type of offer are not yet stabilised. From a more general point of view, fixed and mobile services meet very different needs and mobility appears clearly as a particularity with no equivalent on the fixed market. These differences can also be found in terms of the content of certain services: the technologies used for fixed services allow operators to meet more substantial needs in terms of capacity and transmission speed for the carriage of data, than those associated with services offered via mobile broadband.
- The differences in technology, and thus in costs, between a mobile network and a fixed network, in particular the fixed network of an incumbent operator which has long since paid for itself, are incontestable.
- The need to use scarce frequency resources to set up a mobile network is another of the significant particularities of the sector as compared with the fixed one. Mobile termination rates must thus reflect the "scarcity of the resource", lest it be wasted through overutilisation of the mobile network.
- As the ERG itself underlines⁷, mobile operators are subject to coverage obligations in terms of population and/or territory, whereas fixed operators are free to deploy their networks in areas they themselves choose, according to the profitability they anticipate.
- The call termination service is itself different depending on whether it is provided in the fixed or the mobile market : as the ERG points out, the access segment is included in the mobile call termination service, but not in the fixed call termination service where the cost is recovered on the retail market through the monthly subscription fee. To have a comparable perimeter, one would thus need to integrate into the price of fixed termination, the price of the (constantly increasing) subscription (or a portion thereof).

⁵ ERG public Consultation, page 11

⁶ ERG public Consultation, page 25

⁷ ERG public Consultation, page 36



In contrast, it would not be appropriate to subtract any costs from mobile termination, since an evaluation without access costs has no value in the case of mobile markets.

- On the fixed market, the local loop of the incumbent operator was mostly completed under a system of state monopoly and, in respect of more recent past, under a system of private regulated monopoly. By contrast, investments in the mobile sector have been made at the risk of private investors who had no monopoly at all on the market.
- When a client chooses to leave the fixed incumbent operator for an alternative operator, the incumbent continues to receive a monthly fixed revenue paid by the alternative operator for « unbundling » or subscription resale. By contrast, such is not the case with mobile telephony, because if, for example, a client leaves his mobile operator for a competitor, the original mobile operator receives no revenue for access to the client.

QUESTION G3: Finally we would like to ask you to elaborate on the question of converging MTR and FTRs and the time frame you envisage for this.

Convergence of fixed and mobile call termination rates must be avoided, because the perimeter of costs, the costs themselves, and most especially the economic models, are not comparable.

Mobile part

QUESTION M1: Do you agree with the general principle promoting symmetry : *“Termination rates should normally be symmetric”*?

Yes. SFR fully agrees with this general principle of mobile call termination rate symmetry.

| |
|--|
| Exception to take into account exogenous factors, not related to late entrance : |
|--|

QUESTION M2: Do you agree with the exception to take into account exogenous cost differences : *“asymmetry is only acceptable to take into account exogenous factors, outside the control of operators”*? The only example, which is not related to a late entrance, identified by ERG is cost differences due to the spectrum licensing holdings. Can you identify other exogenous factors?

Differences in MTR can indeed only be justified by differences in costs that are objective and exogenous to operators. On this basis, only « residual » differences related to frequency attribution should be taken into account. By way of example, in France, the initial differences in frequency attribution to Bouygues Telecom (which had DCS 1800 frequency resources when first deploying its network) have been « corrected », to use the words of the French regulator itself (see ARCEP Decision n°2007-0810 page 81).



QUESTION M3: Do you agree with the following principle : *“Assuming that cost differences due to different spectrum allocation are properly evaluated, they may justify an asymmetry”?*

The application of this principle necessitates an objective evaluation of the real differences that remain in frequency attribution, both in terms of the possible disadvantages and in terms of the advantages that could also result. Thus the “residual” disadvantage linked to DCS 1800 frequency attribution (compared to GSM 900) may be largely compensated by an advantage linked to deploying 3G at a later date. Although operators may become candidates for 3G licences under similar conditions, regulatory obligations that result can be more advantageous for one operator, as is the case in France for Bouygues Telecom, which has enjoyed less restrictive obligations than SFR or Orange France as regards network deployment and commercial launch.

| |
|---|
| Transitory exception to take into a significantly late entrance : |
|---|

QUESTION M4: Do you agree with the following principle : *“If the level of competition in the mobile retail market asks for measures which create incentives for new network level entry or measures that strengthen the position of small new entrants, substantial differences in the date of market entry can justify asymmetry for a transitory period”?*

Unfortunately, this principle does not seem to be a very “operational” one and remains too theoretical: indeed, everything depends on the practical application which may be adopted in respect of the terms “substantial differences” and “transitory period”. As concerns France, SFR considers that the difference in market entry date for Bouygues Telecom (only 3 years) and the length of time since this entry date (Bouygues Telecom has had a licence for 14 years) cannot justify the maintenance of any “transitional” period of tariff asymmetry in favour of Bouygues Telecom.

If tariff asymmetry in favour of the “3rd entrant” Bouygues Telecom were to continue, even only provisionally (which SFR objects to), the historical situation of the French market should also lead, in this case, to the setting of tariff asymmetry in favour of the “2nd entrant” SFR, given the advantages that Orange France enjoyed upon its entry onto the market and that it still enjoys today, in particular through its commercial network, piggy-backing on the France Telecom group, but also its advantage in terms of image.

This context, peculiar to the French market, may also be “transposable” to other EU countries and the ERG should thus deal with the issue of tariff regulation applicable to the 1st and 2nd entrants on a market when the 3rd entrant is accorded tariff asymmetry: the 2nd entrant is, indeed, doubly penalised by a tariff asymmetry in favour of the 3rd entrant and a symmetry in favour of the 1st entrant, the latter often being the subsidiary of the fixed market’s incumbent operator.

QUESTION M5: Do you agree with the principle of keeping the level of asymmetry “reasonable”?

There is no justification for any tariff asymmetry today in France in favour of the operators Bouygues Telecom and Orange Réunion, the latter enjoying a less stringent obligation than SRR, namely an obligation of « non excessive » prices, even though it cannot be considered to be a “new entrant”.



QUESTION M6 : Do you agree with the fact that an initial level should be accompanied by a glide path towards symmetry?

Yes : a progressive but clearly defined convergence towards tariff symmetry should help avoid a situation where asymmetry, which as the French regulator has been stating for several years was always supposed to be “transitory”, is “indefinitely” renewed.

QUESTION M7 : Do you agree with the fact that national factors should be taken into account to evaluate the length of the transition period?

Certain particularities related to a country (population density, geography...) or its market structure (penetration, number of operators...) can indeed justify MTR differences. However, differences resulting from the individual strategies of operators (in particular as regards their retail pricing policies and the impact these have on the operators’ market share or usage intensity) must not be taken into account.

Transitory exception before MTRs are at cost, to limit distortions created by MTRs above costs :

QUESTION M8 : Do you agree with that in specific market circumstances (MTRs tariffs are significantly above MTR costs, there are high traffic imbalances between mobile operators and benefits of a transitory asymmetry outweigh any short term disadvantages of doing so), a temporary asymmetry may limit competitive distortions?

No. Such « market circumstances » must not be taken into account when they are not exogenous factors justifying a tariff asymmetry. Thus, a significant imbalance in traffic flow may result from the strategic choices of the operator itself, as is the case in France with the “Néo” offer from Bouygues Telecom. Competitors must not be held responsible or indeed penalised by the offer of an operator that creates a traffic imbalance like Bouygues Telecom’s “Néo”, an offer which is moreover highly profitable according to Bouygues Telecom itself. Tariff asymmetry must not lead to “subsidising” of the commercial policy of one or more market players. It is highly paradoxical that the ERG is considering justifying tariff asymmetry for so long as the traffic imbalance can be explained by operators’ strategies, and believes it can conclude that « *this asymmetry will not be justifiable anymore if one of the following conditions is observed : the situation with traffic imbalances disappears or they do not result of operators’ strategies (...)* »⁸.

The theoretical example developed by the ERG⁹ to illustrate a “justification” for asymmetry is particularly contestable. It should be recalled that an operator, whatever its size, does not, as a rule, suffer from a disadvantage if the call termination price level is higher than the “costs”, regardless of the definition of costs that is adopted. Indeed, if a small operator has to make greater payments for outgoing off-net calls, it will in return receive more remuneration for incoming calls. It will even gain an appreciable advantage where a termination price asymmetry is granted to it.

⁸ ERG public Consultation, page 88

⁹ ERG public Consultation, page 86



The situation may of course change when the traffic between operators becomes unbalanced: the financial exchanges then also become unbalanced to the detriment of the operator – implicitly the smaller network operator – which sends out the most outgoing calls. In France, ARCEP has expressed the view that it would be appropriate either to maintain asymmetry in favour of the smaller operator or, ideally, to lower termination rates of all network operators, in order to remedy the situation. ARCEP is even toying with the idea of changing the cost “referential” (by excluding elements which are nonetheless strictly necessary to the completion of incoming calls or even, eventually, by taking into account only “incremental” costs) in order to favour even more the final entrant.

This approach, which amounts to artificially assisting the final entrant, is unjustified, inefficient, and contrary to the objectives of the proper development of the market.

This approach is unjustified because it is based on a supposition which is not supported by an analysis of facts. It has been seen above that there is no fundamental reason for there to be a financial imbalance to the detriment of the final entrant. There is, however, good reason to expect, as a consequence, an imbalance in favour of the final entrant.

Indeed, beyond the fact that termination rate asymmetry creates, by its very nature, a financial imbalance in favour of the final entrant, in theory this imbalance also encourages the development of offers generating more incoming calls than outgoing calls, typically pre-paid offers, which can only improve even more the net sum of payments in favour of the final entrant. The development of pre-paid offers should also allow the increase of the market share of market players and thus the favouring of the “smallest” operator’s growth.

In fact, in France, the final entrant made a strictly opposite strategic choice, which led not only to its having, prior to the beginning of 2006, interconnection flows that were physically simply balanced (and so financially positive, as a result of the termination rate asymmetry) whereas they should have been physically positive (and even more so financially), but also to its market share remaining reduced due to the abandonment of the pre-paid segment. As the French example demonstrates, tariff asymmetry in favour of the operator with the lowest market share is not an « appropriate » remedy for traffic flow asymmetry: Bouygues Telecom has not profited from this asymmetry to develop its incoming traffic, in particular from activity amongst pre-paid customers.

There is thus no true reason for the final entrant to suffer from a flow imbalance to its detriment. The ERG document, at page 86, sets forth a theoretical reasoning to demonstrate that flows can become unbalanced, but this imbalance is caused in this example by a unilateral decision from the final entrant under which it lowered its “off-net” prices! The French example effectively shows that the final entrant can market such an offer in a very profitable way, and with the result of gaining market share: there is thus no reason to subsidise the operator by granting it a call termination tariff asymmetry.

It can no longer be considered – as the ERG’s reasoning implicitly supposes – that the final entrant has no choice for development but to market offers with “off-net” prices close to the “on-net prices” of other operators. First, it should be recalled that smaller operators habitually develop their pre-paid client base, which allows them to gain market share. Second, the alleged “club effect” which supposedly favours larger market players over smaller ones is only theoretical and is contradicted by analysis of the figures. Indeed, in respect of the core of clients interested by “on-net” offers (family subscriptions), SFR has demonstrated from the elements cited by ARCEP that Bouygues Telecom had no such disadvantage: Bouygues Telecom’s market share for this category of client is the same as its overall market share.

This approach is inefficient and goes against market development objectives because it amounts to subsidising the final entrant and encouraging it in its strategy of « small player ». It is particularly inefficient with respect to 2nd operators who must compete with the 1st operator, which has often come from a historical monopoly and enjoys historical, commercial, image and technical advantages (due to its integration with the fixed activities branch), and also subsidise the other operators. Furthermore, if, as ARCEP is envisaging and as the ERG is implying¹⁰, one has to consider that only incremental costs of incoming calls should be taken into account, this would discourage investments (as they could no longer be made profitable over the long term), and, in the end, innovation.

QUESTION M9 : Do you agree that NRAs should first try to set MTRs at costs?

This question does not really make sense if we look at the true and implicit issue: what methodology for the evaluation of costs should be adopted, for the various types of cost involved, in the scope of the monitoring of the obligation of orienting mobile termination rates “towards cost”? It should be noted in this regard that the obligation as properly stated in the EU “Access” Directive is an obligation of “cost orientation of ... prices”¹¹. It is not, therefore, a case of NRAs imposing MTRs “at cost”.

What’s more, limiting these prices to “at cost” is likely to inhibit the operator from profiting from its investment. As stressed earlier (see answer to question M8), taking into account only the incremental costs for incoming calls would discourage investments : such a cost allocation chosen by the regulator and termination price cap at “this” cost level would lead use of an operator’s network more interesting for its competitors than for itself.

Finally, the perimeter of “relevant” costs, defined by NRAs for the monitoring of call termination rates, must remain objective: regulators, whose decisions are key for the future orientation of the market and the position of operators therein, must include all costs contributing objectively to incoming calls and in particular, beyond networks costs, an “equitable” contribution of common costs and commercial costs. Any NRA decision seeking to minimise the perimeter of “relevant” costs could have unpredictable but certainly irreversible repercussions on the organisation of the mobile market, ultimately to the detriment of consumers.

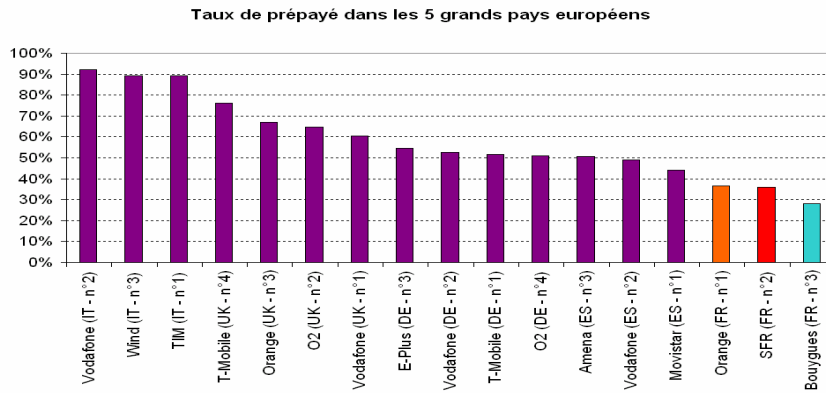
The French example demonstrates the risks that weigh upon mobile operators and their customers should there be an exaggerated reduction of mobile call termination rates : the substantial reductions imposed by ARCEP over previous years can explain the relatively small proportion of pre-paid in France compared with other EU countries, even though these “small consumers” are often modest clients and should therefore receive particular social attention.

¹⁰ ERG public Consultation, page 86 : « When the MTR level exceeds costs incurred to terminate a call (which are costs linked to the additional capacity required to carry the extra-traffic incoming from the smaller operator) »

¹¹ Cf Directive Accès 2002/19/CE article 13



As the graph below shows, the level of pre-paid customers in France is significantly lower than in other, comparable EU countries:



The prepaid market is particularly sensitive to the level of mobile call termination rates because this category of client generates many more incoming than outgoing calls. Too great reduction in revenues on incoming calls can thus destabilise the offer of an operator that targets this clientele, and make the operator limit its development.