Vodafone's response to BEREC's report on Special Rate Services (SRS)

February 2012

1. Summary

Vodafone welcomes the public consultation by BEREC on Special Rate Services (SRS). As BEREC notes in the introduction to the report, there is a need for guidance to NRAs in circumstances where competition problems arise in the provision of calls to special rate services on a national level. It is essential that the guidance developed by BEREC is a complement to robust and rigorous competition/market analysis rather than a substitute for such work. Vodafone believes that a simplified approach to SRS would be beneficial. At present, the proliferation of number types, charging mechanisms and transparency measures contribute to confusion and uncertainty for consumers. BEREC's final report should not only provide guidance on the charging regimes, but should also provide guidance as to how these mechanisms can feed through to greater consumer confidence in relation to SRS.

Our main findings are as follows:

- The presence of high prices at either a wholesale or retail level is not a problem under competitive conditions. When consumers place different values on different call types the expected competitive market outcome is differentiated prices rather than homogenous ones. We should not assume market failure simply because prices are high or different.
- In the case of a special rate service where both the originating operator and service provider earn revenue (i.e. not freephone), the split of revenue between the two will be determined by a number of factors and there should be no presumption that any particular distribution of revenue is 'competitive' or optimal. The BEREC report does not provide any evidence that high wholesale prices for highly valued services – to the extent they might be present – are suggestive of a market failure. In its final report BEREC should stress that NRAs must fully analyse retail and wholesale markets before coming to any conclusions as to whether market failure exists at any level within the SRS value chain.
- Vodafone does not agree that the provisions set out in the revised Authorisation Directive give NRAs the powers to set **retail** prices for calls to number ranges.
- Vodafone supports the objective that freephone numbers should be free to callers from all networks. To make this possible, freephone service providers should pay competitive origination charges based on the different types of originating network
- The level of origination payment should be consistent with average retail revenue per minute to ensure there are no free-rider/arbitrage opportunities
- It is not possible to advocate a unique pricing regime for origination charges given the wide variety of services offered in member states and the different competitive pressure that are exerted across the SRS value chain. In some member states a one-part charge (either SfSm or S') will be preferable. In other member states a two-part charge will be preferable. In these markets the A+S pricing regime will yield better market outcomes than BEREC's proposed C+S approach

- If a two-part charging regime is a significant departure from current practice, NRAs should be careful to ensure that any transition to a new regime is only enforced if it makes customers better off through lower prices for end customers. NRAs will also need to consider practical aspects of implementation such as the need for billing system development and new commercial settlement models across industry to ensure migration timescales are realistic and the costs proportionate to the expected benefits.

Vodafone would also like BEREC to extend the scope of such guidance to cover the following areas:

- Rules and regulations for SRS providers to ensure better consumer protection
- Promotion of consistent policies in relation to international freephone numbers

Our response is set out as follows. In section 2 we set out our proposals for the different types of SRS – freephone, general SRS and Premium Rate Services. In section 3 we examine the legal basis for regulatory intervention. In section 4 we set out some other issues in relation to SRS that should be subject to BEREC guidance.

2. Vodafone's proposals for the different types of SRS

Freephone numbers

Vodafone agrees that there should be a number range that allows free calls for all users. BEREC has correctly identified a particular market outcome in relation to freephone numbers – namely that in many member states they are not free for calls from mobile networks. However, BEREC hasn't identified one of the causes of this outcome. Some providers of freephone numbers do not want calls to be free from mobile networks as this enables them to avoid the higher cost of calls originating on mobile networks. This allows the freephone providers to achieve positive branding through the provision of a freephone number without actually having to bear the full cost of such a service.

BEREC's guidance should encourage NRAs need to implement three decisions with respect to freephone services:

1. Implement the rule that freephone must be free-to-caller on all networks[1]
2. All calls to freephone numbers will generate an origination charge to the originating operator which will differ depending on the network type
3. The origination charge should be at a competitive rate reflecting the different network types (see below) and recognising that freephone services are effectively a substitute for the originating operator's retail revenue

[1] There is an exception in relation to roaming. When customers are roaming it is not possible to guarantee that calls to freephone numbers will be free. In member states where calls to freephone numbers are free to a caller from a mobile network, these numbers should also be free to inbound roamers. Likewise, inbound roamers should also be able to make free calls to international freephone numbers. Inbound roamers will not be able to make free calls to freephone numbers in their home country due to the complexity of wholesale arrangements that this would entail.

A competitive charge for freephone origination on mobile networks

Vodafone believes that the optimal market outcome is for the origination charge to be the product of competitive forces. NRAs will need to determine whether regulatory intervention is required through a market analysis process. Where service providers and originating operators are able to agree commercial terms, either bilaterally or through intermediaries, there may be no need for regulatory intervention..

It is important to note that origination services to freephone providers are not equivalent to wholesale origination services provided to other access seekers such as MVNOs. In the case of MVNOs many aspects of service provision are no longer provided by the originating operator to the MVNOs' customers including:

- Handsets
- Billing/Prepay platform management
- Customer care
- Customer data retention

In the case of origination services to a freephone provider, all of the above aspects of service provision remain unchanged. Even with respect to billing for post-pay customers, the billing system will still be processing the same amount of information – but for freephone calls they will be zero-rated. In addition, the presence of billing arrangements with freephone service providers will add to the originating operator's wholesale billing costs.

Given that origination access services for freephone services are functionally comparable to retail origination services, there should be no *a priori* expectation that the competitive outcome will yield per minute rates that are significantly different to the existing per minute rates for retail origination services. The opportunity cost of providing a freephone origination minute is a retail origination minute. This is broadly consistent with the approach proposed in The Netherlands (although Vodafone disagrees with some aspects of the Dutch proposals) and implemented in Belgium where the rates for freephone origination are based on a measure of average retail revenue per minute.

It is only when NRAs identify a competition problem in relation to origination charges to freephone providers they will they need to intervene and set the origination rates. It is essential that the rate takes into account the complexity of pricing for mobile services. The provision of freephone services must not allow free-rider and/or arbitrage opportunities. In order to achieve this, the origination rate should be set in accordance with the principles outlined above[2].

In some member states there is a high prevalence of freephone numbers for non-commercial organisations including charities and helplines. Originating operators should have discretion to charge lower rates to particular classes of service provider in appropriate cases. This could either be achieved through a separate number range for such organisations or through voluntary action on the part of the originating operators.

[2] The BEREC report refers to the case of Malta where the origination charge is set based on the mobile termination rate. This is not reasonable given that the freephone origination is not comparable to wholesale termination services.. Going forward when MTRs will be set on a pure-LRIC basis it is even less reasonable. The pure-LRIC methodology assumes that the termination service is treated as the last service and only the costs avoided with the removal of that service are relevant. By definition calls to SRS cannot be treated in the same way as it is not possible to have more than one service treated as the last service (unless the computed costs are marked-up for common and joint cost, which is not the case with respect to MTRs).

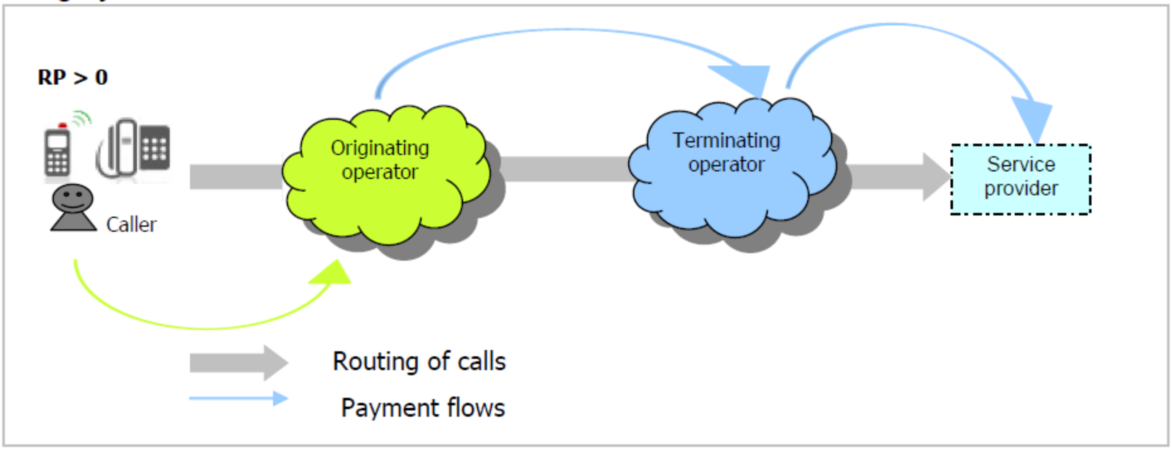
Other issues relating to freephone

BEREC's guidance should also cover over the top VOIP providers that use number ranges. Vodafone believes that the same regime should apply and freephone must be free for end users of VOIP services. The freephone number provider would need to pay an origination charge at the competitive level to the VOIP service provider, although it is expected that the competitive rate of such operators will be significantly lower than the rate for either mobile or fixed networks.

General SRS numbers

We define general SRS numbers as any number range for which the retail price of calls to end users is not 0. This is consistent with the second type of SRS in BEREC's report as per the diagram below. There is a sub-category of SRS – Premium Rate Services – which should not necessarily have the same rules as general SRS. These services are considered in the next section.

Category 2



The BEREC report favours a C+S model whereby the amount retained by the originating operator (the 'C' element) is equal to the price for a call to a landline. The report then recognises that a commercial commission could be retained by the originating operator to reflect billing, cash collection, bad debt insurance and customer information but gives no guidance as to how that retention should be set. Vodafone does not believe that a two-part charging regime will always be appropriate. In some member states a one-part charging regime will be optimal. Under this approach it is preferable for the amount retained by the originating operator to be agreed through commercial negotiation. Only when there is a clear market failure should NRAs intervene. The decision as to which regime should apply depends on a variety of factors and will need to be determined on a market-by-market basis.

The factors that might lead to a NRA concluding that a one-part charge for SRS is optimal include:

- the benefits from greater consumer certainty in relation to end prices outweigh the benefits that derive from two-part charging regimes
- there are sufficient competitive pressure across the SRS value chain to avoid market failure with respect to both (implied) wholesale and retail charges
- the costs associated with moving away from the existing pricing regime are not justified given the benefits that are expected to accrue from a two-part regime

In some markets the presence of a transit operator exerts a significant constraint on the originating operators. In these cases, the combination of consumer certainty over retail prices under a one-part charge and the lack of any expectation of market failure at any level of the SRS value chain would be considered more optimal than the A+S model.

In markets where a one-part charge is applied, NRAs should not prejudge the level of retention that is appropriate for any of the players within the SRS value chain. In the case of services that consumers are willing to pay extra for, the best solution is for the market to determine how that revenue should be distributed. BEREC's report assumes that under a one-part charge model the wholesale rate should be low. This implies that under such an arrangement the Service Provider retention should be high. There is no reason why this would be the expected competitive outcome for all different types of SRS.

In markets where a two part charge for calls to SRS numbers is deemed optimal, the A+S model should be adopted rather than the C+S model. This will allow the 'A' element to be subject to competitive constraints and the 'S' element can be set according to minimum and maximum prices associated with different number ranges. Vodafone also believes that it is preferable for the commercial commission costs to be included in the 'A' element of the A+S charging regime – and therefore subject to competitive forces - rather than as a deduction from the 'S' element of the C+S model which would necessitate on-going negotiations between the originating operator and service provider. The A+S model would result in the pricing of A and S elements being almost entirely independent. As explained below, the S element should be subject to (wholesale) pricing ranges and as such the originating operator would be able to set the A element taking into account its understanding of the specific costs associated with each number range including bad debt. A single access charge based on calling a landline would be detrimental for two reasons:

- The specific costs associated with SRS including bad debt would need to be recovered from other services.
- Different types of SRS have different levels of specific costs: Premium rate services, which are higher priced are most prone to fraudulent behaviour and bad debts, should attract a higher access charge than other SRS.

An additional benefit of the A+S model compared to the C+S model is that it allows originating operators to set the price for its services – i.e. the communications element – according to the demand preferences of its customers. This is a better outcome than the C+S model which assumes that customers have the same demand preferences for calls to landlines and special rate numbers. The S element of the price would be set by the service provider which will be added to the retail price charged by the originating operator and passed through to the service provider via a wholesale payment.

The A+S model also avoids some of the issues that have been encountered when a maximum retail price has been set. For example, for the 1850 number range in Ireland customers could only be charged a once-off amount limited to a maximum of a five minute call national geographic number[3] even though call duration was unlimited. This led to bypass to international destinations which resulted in the average call duration increasing from 2.5 minutes to over 10 minutes. The result was the requirement for the originating operators to increase the origination rate which had an impact on the corporate customers who provided customer care lines in that number range. This would not have materialised under an A+S regime. This example demonstrates the importance of analysing the different types of SRS before determining which pricing regime is optimal.

[3] ComReg Document D1117 section 10.7.5

Only where there is a market failure will NRAs need to intervene and set origination prices. The same issues relating to origination for calls to freephone numbers are relevant in the context of calls to SRS when the caller has to pay. It is essential that the origination rate is not set at a level that creates arbitrage opportunities or free-rider issues. The competitive origination rate will need to be consistent with the originating operator's competitive retail pricing including recovery of handset costs, customer care, retail service provisioning etc.. Origination charges for SRS must not be used by NRAs as a means to achieving carrier per-select style services based on the network cost per minute in the absence of market failure in access and origination markets.

Transparency

Transparency measures will need to be adapted to the pricing regime adopted on a case-by-case basis. Where a one-part pricing regime is used the onus will be on either the originating operator or the service provider to clearly advertise the rate that will apply depending on which party sets the price for end users.

In order to ensure consumers are sufficiently aware of the prices associated with different number ranges, NRAs should ensure that there are not too many different ranges. Given legacy arrangements for SRS number ranges in each of the member states, BEREC cannot be over-prescriptive. BEREC should advise NRAs to assess how many different number ranges (in terms of pricing ranges) strikes the right balance between consumer confidence and pricing flexibility.

In its report, BEREC includes the following table as an example of a transparency measure[4].

Number range	Service	Price from fixed networks	Price from mobile networks
0800	Free	0 €/min	0 €/min
0802	National number	Up to an average national fixed call	Up to an average national mobile call
0803	Premium rate level 1	Between X1 and X2	Between Y1 and Y2
0804	Premium rate level 2	Between X2 and X3	Between Y2 and Y3
.....	.....	....	....
080N-1	Premium rate level N-1	Between XN-1 and XN	Between YN-1 and YN
080N	Premium rate level N	More than XN	More than YN

Table 2. Numbering plan that sets bands.

Vodafone believes that such a table is in principle a good idea but it should be adapted to reflect the A+S charging regime. Under this regime there will need to be different levels of communication to enhance transparency, potentially including:

- Literature provided by the NRA setting out the different number ranges and the range of allowable 'S' for each number range
- Tariff information provided by operators setting out the 'A' that is charged for each number range. The 'A' will not necessarily be consistent across all tariffs and there may be different 'A's for different

[4] Numbering plans as shown in the table only apply to voice services. The need to limit the number of ranges should not necessarily apply to other services such as innovative SMS services that are used for micro payments and depend on more flexibility in pricing and can be combined with pricing information at the time of purchase.

number ranges to reflect the different costs of specific number ranges (e.g. bad debt associated with premium rate services) and different consumer preferences in relation to different types of SRS

- Service Providers will need to clearly state the level of 'S' that they charge and that an additional charge will be applied by the originating network operator

The exact specification of transparency measures needs to be determined on a market-by-market basis. Many aspects of transparency could be addressed through self-regulation as has happened in Italy In some cases operators have voluntarily established codes of conduct. This should be encouraged as operators have the best understanding of the publicity materials that consumers pay attention to.

An additional benefit of the A+S regime is that NRAs have sufficient powers under the framework directives to stipulate the range of prices for the 'S' element for each of the number ranges. The framework directives do not give NRAs power to set retail prices (either for the end-to-end service or the 'A' element) in the absence of evidence of market failure. This is explained in more detail in section 3.

Premium rate services

Within the general category of special rate services is the sub-category of premium rate services. The regulation of these services – in terms of consumer protection rules - differs from country to country and we believe this is something that should be addressed by BEREC in addition to its focus on the charging regimes.

In many member states the mobile originating operator charges an implicit wholesale rate to the premium service provider on commercially negotiated terms through revenue share arrangements. Vodafone believes that NRAs should be especially careful when seeking to regulate these services for two reasons:

1. The cost to the originating operator for these services is significantly higher due to the higher incidence of fraud and bad debt
2. If the implicit wholesale origination charge was reduced through regulatory intervention there is a strong possibility of consumer detriment. Compared to the status quo, the most likely outcome from a forced reduction in the wholesale rate to the originating operator would be:
    a. No change in the retail price for premium rate services
    b. Higher margins to the operators of premium rate services
    c. Lower margins on premium rate services for the originating operators
    d. Higher prices for other services provided by the originating operators to make up for the shortfall in margin on premium rate services (the waterbed effect)

    It should be noted that this is less of a concern in markets where SRS prices are set on a A+S basis as explained in the previous section

With these two effects in mind, Vodafone believes that a new wholesale regime for premium rate services should only be put in place if the NRA ensures pass through of lower prices to customers.

3. The legal basis for regulating SRS

The BEREC report sets out the legal instruments that would allow NRAs to enact the guidance. In Paragraph 92 BEREC states:

> *Part C of the Annex to the revised Authorisation Directive as amended by the revised EU Framework, specifies the conditions which may be attached to rights of use for numbers. In particular, paragraph 1 of Part C provides for: "Designation of service for which the number shall be used, including any requirements linked to the provision of that service and, for the avoidance of doubt, tariff principles and maximum prices that can apply in the specific number range for the purposes of ensuring consumer protection in accordance with Article 8(4)(b) of Directive 2002/21/EC (Framework Directive)."*

BEREC presents this provision as giving NRAs the right to set the maximum retail price for calls to any number range without having to go through a market analysis process. Vodafone does not agree with such an interpretation. For a detailed analysis of the relevant legal instruments, please refer to Annex 4 of Vodafone UK's submission to Ofcom's consultation on Non-Geographic Numbers[5]. In this annex we explain that the imposition of maximum prices can only apply to the number range – i.e. on a wholesale basis. This is logical given that the wholesale element of calls to specific number ranges are not subject to competition and the *ex ante* imposition of a maximum price is proportionate and reasonable. This is consistent with the wording of the directive which makes it clear that the requirements relate to the provision of service associated with the number. The number is only used for the terminating element of the service and not the retail element. The retail element of calls to specific number ranges are not inherently independent of competitive forces and there can be no *a priori* assumption that price controls should be imposed for consumer protection purposes. The imposition of price controls at a retail level can only be considered justifiable when the market within which the services are purchased has been assessed and deemed to be uncompetitive.

In the absence of a clear legal basis for setting the retail price of the originating operator, NRAs will not be able to impose the C+S solution advocated by BEREC.

BEREC also refers to dispute resolution as a potential means for regulating SRS. The dispute resolution process should be limited to facilitating negotiations to ensure they are carried out in good faith. The dispute resolution process should not be extended to price setting in the absence of market failure as it may lead to providers not negotiating in good faith and/or competitive distortions in the market.

4. Other issues in relation to SRS on which BEREC should provide guidance

International freephone/00800/116

There is very little harmonisation of international freephone and the 116 number range across member states.

There are two different number ranges that could be considered international freephone – 00800 (commercial freephone) and 116 (harmonised European helplines). These numbers are not identical in that

[5] http://stakeholders.ofcom.org.uk/binaries/consultations/simplifying-non-geo-numbers/responses/Vodafone.pdf

00800 number range is provided through a combination of service providers, termination operators, international transit operators and originating operators. The 116 range is managed locally by NGOs who use a terminating operator to provide the service.

00800 number range

In principle, we believe the pricing regime for commercial international freephone numbers should be the same as for national freephone plus an allowance for any additional costs associated with service provision. The calls should be free for all users and the international freephone provider should be required to pay an origination charge to the originating network. Due to the additional wholesale relationships present within the international freephone number range, BEREC will need to assess each level within the value chain to determine whether any market failure exists. If the origination charge is set in the same was as domestic freephone (assuming that originating operators handover the call in-country to an international transit operator) BEREC would need to focus on the wholesale relationships from transit operator to terminating operator to service provider. We believe that a degree of international co-ordination will be required and BEREC would be best placed to fulfil this role.

116 number range

In principle, the same applies for the 116 number range although the routing of the calls is different as they are managed locally. At present there is low consumer awareness of the 116 number range despite the EC's promotional efforts, and therefore it is delivering only limited social value. BEREC should clearly set out the criteria which would need to be met in order to qualify for a 116 number. Thereafter NRAs in all member states should be responsible for ensuring that operators make calls to this number range free for all callers including inbound roamers. The operators of the 116 number range would need to pay origination charges to the originating operator. In principle the origination charge should be the same as for domestic freephone numbers, although a lower charge (or even no charge) could apply given that the 116 number range is restricted to help services that provide social value. It is essential that strict qualification criteria are established to avoid non-essential services diminishing the value of the 116 number range.

Other rules and regulations for premium rate services

A number of different rules and regulations have been established in member states in relation to premium rate services. Examples of the rules and regulations that Vodafone is aware of include:

- Maximum call holding time
- Maximum call durations
- Maximum retail price per call
- Requirement for (free) pre-call pricing announcement
- Default blocking of calls to PRS – i.e. service has to be actively enabled
- Requirement on service provider to terminate the call if no service is provided

As part of BEREC's report guidance should be provided on the rules and regulations that enhance consumer protection and the circumstances when they might be applied.