The Bahamas Telecommunications Company Limited:

Response To

Preliminary Determination on Assessment of Significant Market Power (SMP) in Mobile Call and Short Messaging Termination Services on NewCo2015 Limited's Cellular Mobile Network...

Consultation Document
ECS 17/2016

Legal, Regulatory and
Carrier Services Division
August 15, 2016

Executive Summary

The Bahamas Telecommunications Company Limited (BTC) welcomes the opportunity to respond to the Utilities Regulation and Competition Authority's (URCA) Consultation Document on its Preliminary Determination on the Assessment of Significant Market Power in Mobile Call and Short Messaging Termination Services on NewCo2015 Limited's Cellular Mobile Network in The Bahamas under Section 39(1) of the Communications Act, 2009.

BTC has long held the view that URCA should intervene in the market for call termination services on the networks of all operators, given the positive externalities associated with this intervention in advancing the interest of consumers. This Preliminary Determination is an important step in preventing a Significant Market Power (SMP) operator's abuse of its dominant position by virtue of its absolute control over terminating facilities on its network, and in the absence of regulatory intervention, having the latitude to charge excessive termination rates to other licensees. With no alternatives available to originating operators for the termination of mobile calls and short messaging services, there is a need for regulatory intervention, without such intervention, originating operators will have no choice but to pay excessive charges to allow their customers to communicate with customers of the terminating operator.

Consistent with the argument that the Company has advanced in its Response to the Consultation Document on Wholesale Fixed Call Termination Price Control for SMP Licensees[1] and worth highlighting in the context of this Consultation, BTC supports symmetry of call termination charges, i.e. operators should set their call termination rates at the same level as BTC's call termination charges. The setting of symmetric call termination charges provides predictability and promotes competition. Conversely, asymmetrical rates lead to distortions in the market and suboptimal outcomes. Reciprocal termination rates will ensure both allocative and productive efficiencies in the market and prevent distortions like excessive wholesale charging, high or inefficiently structured retail rates and inefficient market entry. BTC provides ample evidence in this submission from the EU Commission, the European Regulators Group (BEREC), Ofcom and various regional regulators in support of this position.[2]

Finally, BTC is in support of the three (3) stage market review process adopted by URCA in looking at NewCo's provision of wholesale termination services. BTC has paid particular attention to the proposed remedy in the form of wholesale price control to ensure that NewCo's price setting for its termination service meet the objectives of the Communications Act in relation to promoting effective competition and seeking to maximize consumer welfare. BTC is concerned that in the absence of

[1] BTC Response to URCA's Consultation Document ECS 01/2014: Preliminary Determination on Wholesale Fixed Call Termination Price Control for SMP Licensees, April 30, 2014.
[2] Ibid pg. 4 of BTC's Response, April 30, 2014

URCA's intervention for call and messaging termination services, there is the material risk of NewCo engaging in excessive charging of its wholesale termination charges, which clearly will not be in the interest of consumers, who ultimately will absorb these charges by way of the retail prices for the retail downstream products provided.

General comments

BTC supports URCA's Market Review Process

In reviewing the standard three (3) stage process as part of the market review process, BTC is in general agreement with the approach. In defining the relevant product and geographic markets, BTC has no objections to the respective definitions. For stage three (3) of the process, the application of ex ante remedies, BTC is in support of regulatory intervention by way of price control and other measures for NewCo's wholesale termination services to ensure that the latter dies not abuse its position in the provision of upstream services.

BTC supports the case for symmetrical termination rates

BTC fully supports the notion that NewCo's termination rates should be symmetrical to the rates set out by BTC in relation to termination services on its mobile network. BTC supports symmetrical mobile termination rates based on the following:

- Generally promotes allocative and productive efficiencies. Symmetrical termination rates remove the likelihood of price distortions that are created by way of having in place asymmetrical termination rates. The price distortions created by way of asymmetry provides a disincentive for more efficient pricing for termination services.

- Removes the potential for excessive charging for wholesale termination services, which invariably impacts the downstream prices for retail services, with consequential adverse effects for consumer welfare.

- Provides greater predictability, stability and transparency in setting rates. Further, symmetrical rates lessen the burden on operators and regulatory authorities of calculating cost models and call termination rates for each operator.

The counter argument historically advanced by some operators is that asymmetric rates should be used because the cost per minute for new networks is higher than for established networks. BTC wishes to point out that this argument is not supported by either regulatory best practice or economic theory. The capital and operating costs of new networks should be significantly lower for new operators than for incumbent operators because new entrants utilise the latest technology. Further, new entrants are aware in their business plans that for the initial years of operation their traffic levels are low while they establish their networks, and take full account of this in their decisions to enter the market. Hence there is no need to provide additional incentives through asymmetric termination rates.

International precedents for symmetrical termination rates

The position being advanced by URCA has backing in many international precedents. These were some of the same positions that were advanced by URCA in support for symmetrical termination rates as part of its Preliminary Determination on Wholesale Fixed Call Termination. Similarly, some of the responses put forward by BTC in support of symmetrical termination rates in the context of fixed called termination services are also applicable in the context of this response and are certainly worth repeating in the context of this Consultation.

As BTC would have quoted in its response to the Preliminary Determination on Wholesale Fixed Call Termination, the European Regulators Group (ERG, now BEREC) stated[3]:

"Economic principles tend to recommend a unique and uniform TR [Termination Rate], determined with reference to costs incurred by an hypothetic efficient operator, i.e. a termination rate which does not depend on costs effectively incurred by the operators or on their market shares. This efficient TR level indeed is the right signal to give incentives for productive efficiency[4], less efficient operators trying to overcome their inefficiency (in lowering their costs to avoid losses which ultimately result in market exit) and more efficient operators realizing profits over regulated prices, investing and innovating. Gains in productive efficiency put pressure on final services' prices and contribute to end-users welfare."

And in the summary of comments:

"[….] optimal incentives for productive efficiency are given by symmetric termination rates at the cost level of an efficient operator independent of the level of competition. The logic is that allowing asymmetric tariffs to take into account any higher costs does not give optimal incentives to get a market structure that produces at the lowest costs, so it does not give optimal incentives for incentives for productive efficiency."

In other words, allowing any operators to charge a termination rate above the efficient cost level would result in distortions to the incentives to achieve efficiencies, which would in turn distort competition in the retail market. For example, OPTA finds there are two main ways that such a distortion may take place[5]:

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[3] European Regulators Group. ERG Common Position on symmetry of fixed call termination rates and mobile call termination rates, in ERG(07) 83 12 March 2008, page 4
[4] According to economic theory, "productive efficiency" is achieved when firms minimize total cost (given inputs needed and competitive prices of inputs) with respect to technology of production.
[5] OPTA. Consultation Paper - Market analysis fixed and mobile call termination. 26 April 2010.

- It is possible in some markets that the effects of above-cost call termination rates are fully competed away in the retail market, the so-called ‘complete water-bed effect’ – here, above-cost termination rates result in higher retail call charges, which are in turn compensated through lower fixed monthly charges, but the average overall retail tariff level is not affected. The result is inefficient service take-up and call volumes below the efficient level.

- The ‘incomplete water-bed effect’. In this case above-cost termination rates result in average retail rates rising above the efficient level, leading to overcharging of end-users, in addition to the ‘complete water-bed’ effect.

In addition, leaving aside whether cost differences between operators exist, such cost differences should not affect termination rates unless they are outside the control of operators involved. We quote from the EU Commission’s Recommendation on Fixed and Mobile Termination rate and its explanatory document[6]:

“*In setting termination rates any deviation from <u>a single efficient cost level</u> should be based on objective cost differences outside the control of operators. <u>In fixed networks, no such objective cost differences outside the control of the operator have been identified</u>*.” [Emphasis added].

And:

“NRAs should set termination rates based on the costs incurred by an efficient operator. This implies that they would also be symmetric”.

And:

“An important argument for symmetric rates at the level of efficient cost is that asymmetric pricing can foster inefficient behaviour and generate productive inefficiencies. Productive efficiency takes place when a good is produced at the lowest cost possible. Rewarding an operator with a price above an efficient or cost based level can reduce its incentives to innovate and minimise costs. For example, asymmetries based on differences in dates of market entry and scale may discourage innovation and cost efficiency on the part of the later entrant/smaller operator, and may give rise to inappropriate investment incentives and inefficient entry”

And finally:

“Consequently, consumers may end up paying higher prices than would otherwise be the case in a situation of cost-based symmetric termination rates. This is because

[6] Commission recommendation of 7 May 2009 on the Regulatory Treatment of Fixed and Mobile Termination Rates in the EU (2009/396/EC).

the higher termination rates have to be recovered by the originating operators and will presumably be passed onto consumers in the form of higher retail prices. This effectively creates a cross-subsidy from lower-cost operators and their consumers to their less efficient rivals, thereby generating allocative-efficiency concerns. Meanwhile, the less efficient operator benefits from the lower termination rates of its rivals, thus enabling it to lower its retail prices and win customers. As the subsidized operators expand, the negative impact on retail process and consumer welfare is even greater. Given that the stated purpose of the regulation of wholesale termination charges is to prevent excessive pricing and its negative impact on consumer welfare, it is arguably counter-intuitive to apply a remedy that also generates allocative and productive inefficiencies."

Hence BTC considers that symmetrical rates should be required for all terminating operators in The Bahamas. The use of symmetrical termination rates is in line with best international practice, and BTC notes that other regional and international regulatory authorities have considered whether to use symmetrical or asymmetrical termination rates, and have come down firmly on the side of symmetrical rates, for example:

Anguilla

The Public Utilities Commission mandated symmetrical rates in its decision on termination rates in 2007[7], and this was continued in its review in 2012[8].

British Virgin Islands

The Telecommunications Regulatory Commission considered arguments in favour of asymmetric termination rates, but rejected them on the grounds that they would cause distortions in the domestic market.[9]

Jamaica

The Office of Utilities Regulation has implemented a single mobile termination rate for all operators, despite cost models showing different costs per minute.[10]

Trinidad and Tobago

Asymmetric rates were a major issue in the disputes between TSTT and Digicel between 2006 and 2008. The Panel appointed by the Telecommunications Authority of Trinidad and Tobago to investigate the disputes considered that asymmetrical rates could not be justified. While it accepted that a smaller operator may have higher costs per minute because its traffic levels are lower that the incumbent operator, it noted that a new entrant would take this into consideration in its business

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[7] Public Utilities Commission Anguilla, Review of interconnection prices. Telecommunications Decision PUC 2007 – 102. Para 22, Page 6.

[8] Public Utilities Commission Anguilla, Review of interconnection prices. Telecommunications Decision PUC 2012 – 101.

[9] Telecommunications Regulatory Commission, British Virgin Islands. Consultation on market analysis of wholesale call and SMS termination on individual fixed and mobile networks. 30 September 2011. C/02/2011. Para 6, page 10

[10] Office of Utilities Regulation, Jamaica. Mobile Termination Rate: Determination Notice Document No: TEL2012006_DET001 4 June 2012 page 21.

planning. It was concerned that asymmetric rates could encourage inefficient entry, and that these operators would exit the market once rates became symmetrical[11].

Turks and Caicos Islands

In its decision on mobile termination rates, the Turks and Caicos Islands Telecommunications Commission reported that all respondents agreed with the Commission's view that that the mobile termination rate should be set symmetrically[12].

United Kingdom

Reciprocal termination rates were introduced in 1997 on the grounds that they removed distortions in competition and achieved competitive neutrality. They have been maintained during several reviews of wholesale prices between operators since then. This policy was most recently reviewed in detail during 2011, and OFCOM concluded that reciprocal rates were fair and reasonable because they:

- Provide strong incentives for operators to minimise the cost of terminating calls.
- Remove distortions in efficient interconnection arrangements
- Promote competition in transit markets[13].

[11] Telecommunications Authority of Trinidad and Tobago. Report and Decision of the Arbitration Panel. 7 March 2008. Pages 35 – 38.
[12] Turks and Caicos Islands Telecommunications Commission. Decision on the Mobile Termination Rate Review. 24 January 2011, para 2.2.5 page 10.
[13] OFCOM. Fair and reasonable charges for fixed geographic call termination Statement and final guidance. 27 April 2011. Para 3.101, page 36.

Specific answers to URCA's questions

Question 1: Please provide comments on URCA's preliminary view on the relevant product market definition for mobile termination services on NewCo's cellular mobile network.

BTC fully supports URCA's preliminary view on the relevant product market definition for mobile termination services on NewCo's cellular mobile network. Reviewing URCA's analysis of the absence of effective demand and supply side substitutes for calls and messaging services terminating on NewCo's cellular mobile network. As URCA would have outlined in its analysis, a service provider faced with a SSNIP (Significant but Small Non Transitory Increase in Price) in the price for terminating calls on a given network would have no choice but to continue to send calls and or messaging services to the network of the terminating operator. Similarly, there is no supply substitute, as the originating operator has no alternative to terminate the call on the network of the called party.

Further, looking at the indirect constraints, BTC is in general agreement that it is unlikely that an increase in the price of termination services would prove unprofitable due to any switching behaviour in relation to the voice and messaging termination services of the terminating operator.

Based on the above, BTC is in general agreement with the definition of the two (2) product markets, i.e. mobile call termination on NewCo's cellular mobile network; and mobile message termination on NewCo's cellular mobile network.

Question 2: Please provide comments on URCA's preliminary view on the geographic market definition in relation to mobile termination services on NewCo's cellular mobile network.

BTC fully supports URCA's position that for the purpose of this Preliminary Determination, the relevant geographic market is national in scope. As URCA would have pointed out, the relevant geographic markets for mobile call and mobile messaging termination services should not be so narrowly defined to include areas in which NewCo has facilities to provide the product. Further as URCA has pointed out in its Preliminary Determination, NewCo's Individual Spectrum Licence (ISL) requires the company to establish its cellular mobile network throughout virtually all populated areas in The Bahamas, and on this basis, NewCo's facilities for the provision of termination services is national in scope.

In reviewing the other considerations as outlined in Section 5.5.4 of URCA's Preliminary Determination, BTC fully supports URCA's position that the geographic market is national in scope taking into account that BTC and NewCo competes for customers in a single space, defined as the entire Commonwealth of The Bahamas.

Further, as URCA would have pointed out, the spectrum and operating licences granted to NewCo are nationwide in scope.

Question 3: Please provide comments on URCA's preliminary views that NewCo has SMP in relation to the wholesale supply of mobile voice call and or mobile message termination services on its cellular mobile network.

In reviewing the various criteria for the assessment of market power, notwithstanding the influences of the other considerations in assessing the applicability of SMP in the case of NewCo, given that NewCo will have 100% market share in respect of terminating traffic to its network gives rise for regulatory intervention for the provision of wholesale services by NewCo. Given that the party from the originating network has no alternative means to connect to the called party of the terminating network, places the terminating network operator in a monopoly position and therefore subject to regulatory intervention.

BTC concurs with URCA's assessment in Section 6 of the Preliminary Determination in the applicability of SMP in relation to NewCo. Further, the company takes the position that the assessment of SMP in the case of NewCo's provision of wholesale services, particularly in relation to the market share criteria for the assessment of SMP, is independent of any market share argument as it relates to the downstream provision of retail services.

Question 4: Please provide comments on URCA's preliminary view that the wholesale termination markets identified are susceptible to ex ante regulation.

BTC supports URCA's position that the wholesale termination markets identified are susceptible to ex ante regulation. Further, looking at the European Union (EU) three (3) criteria test and in particular the third characteristic, i.e. the likely that ex post intervention is not likely to prevent or mitigate abuse, suggests the need for regulatory intervention in the form of ex ante regulation.

In response, BTC cannot over emphasize the need for intervention particularly in the form of price control measures to ensure that NewCo does not engage in excessive charging for its termination services, which will not be in the interest of consumers, given the resultant impact on the prices that consumers will pay for retail mobile services.

Question 5: Please provide comments on URCA's preliminary views on the main competition problems or market failures that could arise from NewCo having SMP in respect to the provisioning of wholesale call and /or mobile messaging termination services on its own cellular mobile network.

One of the main competition concerns that arise from NewCo's monopoly power for termination services on its own network is that of excessive charging at the wholesale level. BTC supports URCA's preliminary views in relation to the competition concerns raised, i.e. excessive charging and the potential for exclusionary behavior by way of NewCo's refusal to provide upstream wholesale services to competing network operators.

Question 6: Please provide comments on URCA's preliminary view regarding NewCo's publication of tariff and non-price terms and conditions governing supply of wholesale termination services.

Given that NewCo, is providing an essential 'bottleneck' service by way of its termination services for voice and mobile, it is important that there is transparency, not just in relation to the prices that are offered for the wholesale services, but also in the case of the non-price terms and conditions relative to the supply of termination services.

BTC has taken special note of the inclusion of quality of service standards; details of a dispute resolution scheme with appropriate reference to URCA, where the parties are not able to settle disputes based on proposed terms and conditions; and operations and maintenance procedures as part of the minimum published information on the part of NewCo in providing interconnection services.

Question 7: Please provide comments on URCA's preliminary view regarding price regulation of termination services on NewCo's cellular mobile network.

As stated previously, BTC is firmly of the view that NewCo's termination services, i.e. voice and mobile messaging should be the subject of ex ante price regulation. NewCo's termination services as highlighted, are essential services and services of which, the Company exercises a monopoly position. There is a material risk of potential harm to consumers by way of excessive charges for termination services that will ultimately impact retail charges for consumers. To remove or mitigate the potential for consumer harm, it is important that URCA intervenes in the regulation of NewCo's termination charges.

Question 8: Please comment on URCA's preliminary proposal to apply the principle of cost orientation to NewCo's mobile termination rates. If respondents consider that cost oriented mobile termination rates are not appropriate for NewCo, the relevant respondent should describe its preferred alternative approach, with supporting rationale.

Wholesale pricing as in the case of price for downstream products, should be carried out in such a way that it sends the appropriate signals to the market to encourage competitive entry. BTC supports the notion of cost oriented mobile termination rates for NewCo. Setting wholesale charges that are cost oriented, removes or at least mitigates the price distortions that are created by allowing NewCo to charge wholesale termination charges that are in excess of the cost, including a return on capital of providing the respective wholesale charges.

Question 9: Please comment on the merits of allowing NewCo to temporarily charge higher mobile termination rates than those contained in BTC's RAIO.

As part of your response please provide further comment on the appropriate level and time period of any asymmetry in mobile termination rates.

BTC is of the view that there is no objective justification for the introduction of asymmetric termination rates for NewCo cellular mobile network. NewCo's recent public pronouncements on its expectations of quickly gaining significant market, share coupled with mobile number portability (MNP), suggests that there are no barriers for expansion in the case of NewCo. There is no empirical justification that would support the introduction of asymmetric termination rates on mobile networks either for a short or transitional period of time. As BTC has stated in the previous Public Consultation for fixed termination rates, it is not the role of the regulator to facilitate market entry by way of incentives like asymmetric termination rates but rather the incentives should come by way of the enabling environment that fosters efficient market entry and effective competition.

In reviewing the Preliminary Determination, URCA states that there are three factors that may justify the introduction of asymmetric termination rates. The first factor, exogenous and objective cost differences outside the control of SMP licensees, 'might significantly impact NewCo's initial unit cost of termination relative to BTC's unit costs'. In looking at potential exogenous and objective cost differences that may impact NewCo's unit costs for termination services, URCA has examined the list of potential exogenous factors, i.e. network topology/technology; geographic footprint of the networks; access to sites; and spectrum holdings and associated fees and have found that each of these considerations are not likely to have any appreciable impact on termination costs to justify putting in place asymmetric termination rates for NewCo. URCA has correctly pointed out that SMP licensees having different sizes in relation to customer base is not an objective, exogenous consideration for asymmetric termination rates.

BTC supports URCA's position as outlined in its Preliminary Determination that given the significant share of prepaid mobile subscribers, who would generally have a low switching costs, particularly given MNP at the start of the process and BTC's postpaid subscribers on the minimum one (1) year contracts, are additional considerations that would suggest that there are no significant barriers to expansion for NewCo that would justify asymmetrical termination rates.

In looking at the other two (2) factors that can potentially influence the setting of asymmetric termination charges, i.e. barriers to entry and expansion; and significant traffic imbalances, as per URCA's Determination, it is only the factor, barriers to entry and expansion that weigh more heavily in relation to the other factors in impacting the need for asymmetric termination rates.

Barriers to entry and expansion

In looking at barriers to expansion in the case of NewCo, URCA did not weigh into the discussion the impact of Mobile Number Portability (MNP) and how MNP can potentially impact NewCo as a new entrant in its ability to gain market share quite rapidly. MNP at the start of competition in mobile lowers the transaction costs for switching at the same time provides an impetus for the new entrant to quickly gain market share. BTC was hard pressed in finding references elsewhere where MNP was introduced at the start of competition. This is a consideration that URCA has not weighed into the balance in looking at NewCo's ability to expand fairly quickly and achieve minimum efficient scale.

Without prejudice to the arguments that BTC has been advanced in support of symmetrical termination rates, in response to URCA's question on time period of any asymmetry in mobile termination rates, BTC is of the view that any transitional arrangement for asymmetrical rates, should be based on market share and not exclusively time based. Consistent with URCA's parameters of market threshold for minimum efficient scale of 15-20% market share[14], the Company is of the view that any transitional arrangement for asymmetry of mobile termination rates for NewCo should be removed, once NewCo has achieved 15% market share, and or not more than fifteen (months) following the issuance of licence, whichever comes first.

The setting of symmetrical termination rates should be based on the URCA approved mobile termination rate (MTR) for BTC. In direct response to URCA's question in this section, any consideration for asymmetrical rates should not only be based on market share, i.e. 15% market share threshold, or not more than fifteen (15) months from the date of the issuance of the licence, whichever is achieved first, but the level of asymmetry should be between 1.4 to 1.5 of BTC's MTR, i.e. between 40% to not more than 50% higher than BTC's mobile termination rate.

Conclusion

BTC is of the view that this Preliminary Determination undertaken by URCA in relation to Significant Market Power for call and messaging termination services termination services is an important undertaking. Clearly, there is recognition on the part of URCA that in the absence of this intervention vis-à-vis the regulation of termination services in the case of NewCo, there is the material possibility of excessive charging and an overall reduction of consumer welfare as customers are faced with the potential of higher retail charges for communicating with customers of the terminating mobile operator, NewCo.

The Company supports symmetrical termination rates. The absence of which can lead to distortions within the market for the provision of termination charges. Ultimately, the cost of these distortions will be borne by customers. BTC as highlighted in its response to this Preliminary Determination supports the arguments that URCA has advanced for symmetry of rates. These rates as BTC has stated should be symmetrical to the URCA approved termination rates for BTC.

[14] URCA's Preliminary Determination on Assessment of SMP in Mobile Call and Short Messaging (ECS 17/2016), p. 42.

Finally, as BTC would have stated in its response, notwithstanding its support based on international precedents for symmetrical termination charges, asymmetrical termination charges should be allowed to exist until NewCo would have achieved 15% market share or for 15 months from the date of issuance of the licence, whichever is first, after which, any transitional arrangements based on asymmetry of rates should be removed.

Reservation of rights

BTC has addressed the issues but reserves the right to comment at any time on all issues and states categorically that the decision not to respond to any issue raised in this Consultation in whole or in part does not necessarily represent agreement in whole or in part with URCA's position, nor does any position taken by BTC in this consultation mean a waiver of any of BTC's rights in any way. BTC expressly reserve all its rights.

Respectfully Submitted

Bahamas Telecommunications Company Limited