Mobile Termination Rates in Jersey

Case Number T843J

Initial Notice

Proposed directions to mobile network operators

Document No: CICRA 12/01 **16 January 2012**

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Contents

1. Introduction

Mobile termination rates ("MTRs") are the fees charged to other telecommunications companies by mobile network operators ("MNOs") to terminate calls on mobile networks. They are a key component of the retail charge that mobile customers ultimately pay for their mobile phone services. In Jersey, the current MTR is 5.6 pence per minute ("ppm").

The issue of the level of MTRs and the need to ensure such charges are set at levels that reflect the efficient and cost-effective provision of terminating services is a matter currently under review by regulators in many European countries. There has been good progress in reducing MTRs in recent years within the EU, with further progress expected as the European Commission increasingly focuses its attention on charges in the mobile sector.

The Body of European Regulators for Electronic Communications ("BEREC") is also actively engaged in this area and publishes a MTR snapshot on a regular basis which provides very valuable benchmarking data of the MTRs charged by mobile operators from across thirty-three European countries. The European Commission has also set out its view that National Regulatory Authorities ("NRAs") in the EU should increasingly set MTRs based on LRIC (i.e. Long-Run Incremental Cost) and it is anticipated that this will further reduce MTRs in the coming years.

In Guernsey, the Office of Utility Regulation ("OUR") has carried out two separate reviews of MTRs since 2006. The first review determined that an average MTR of 6.75ppm should be put in place from 1st April 2007 and a further review in 2009 led to all operators agreeing to set their MTRs at a flat rate of 4.11ppm (including any transit charges). As a result, an identical MTR rate is being applied by the three MNOs in Guernsey for a three year period running until 31st March 2013. The OUR intends to review further the approach to determining MTRs in light of international developments, such as the move to LRIC based pricing, before deciding whether any further change is required from 1st April 2013.

In Jersey, there are three mobile operators currently providing mobile services: Jersey Telecom Limited ("JT"), Cable & Wireless Jersey Limited ("CWJ") and Jersey Airtel Ltd ("JAL"). Currently the MTR applied by all three operators is 5.6ppm and it has been at this level for some considerable time. The Jersey Competition Regulatory Authority ("JCRA") has been reviewing the charges applied by JT for all interconnection services and this Initial Notice sets out the JCRA's proposals with regard to MTRs only. The JCRA will separately consult on its proposals for the level of charges for fixed interconnection services provided by JT.

In this Initial Notice, the JCRA is proposing to cap MTRs for all Jersey MNOs at 4.11ppm. It is also proposed that the MTR cap of 4.11ppm would be back-dated to 1st July 2011. This would be a flat rate (i.e. no time of day or weekend distinction) and calls would be charged on a per second basis (no minimum call charge or call duration). This would in effect put in place a common MTR across the Channel Islands. It is proposed that this cap would remain in place until 31st March 2013 when it is intended that a further revised MTR will be determined for both Jersey and Guernsey.

This document summarises the issues involved, and sets out:

- the direction that the JCRA proposes to issue to JT under and Condition 34.1 of the Class III licence issued to JT by the JCRA under Article 14(1) of *Telecommunications (Jersey) Law* 2002 (the "Telecoms Law");

- the direction that the JCRA proposes to issue to CWJ under Condition 27.1(c) of the Class II licence issued to CWJ by the JCRA under Article 14(1) of the Telecoms Law; and

- the direction that the JCRA proposes to issue to JAL under Condition 27.1(c) of the Class II licence issued to JAL by the JCRA under Article 14(1) of the Telecoms Law.

It constitutes the Initial Notice of the proposed directions under Article 11(1) of the Law. The JCRA is now inviting comments on its proposed directions.

2. Structure of the Initial Notice

2.1 *Structure of Initial Notice*

This Initial Notice is structured as follow:

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

Chapter 4: sets out the developments in other jurisdictions in regulating MTRs;

Chapter 5: sets out the proposed directions with respect to MTRs for Jersey; and

Chapter 6: sets out the next steps.

2.2 *Timetable for Responses to Initial Notice*

Responses to this Initial Notice should be submitted in writing and should be received by the JCRA before 9.00am on 16th February 2012. Written comments should be submitted to:

JCRA,
2nd Floor, Salisbury House
1-9 Union Street
St Helier
Jersey
JE2 3RF

Or by email to **info@cicra.je**

In accordance with the JCRA's policy, non-confidential responses to the Initial Notice will be made available on CICRA's website (www.cicra.je). Any material that is confidential should be put in a separate annex and clearly marked so that it can be kept confidential.

3. Legal Background & Regulatory Framework

3.1 Legal Background

Article 16 of the Telecoms Law provides that the JCRA may include in licences such conditions as it considers necessary to carry out its functions. The Telecoms Law specifically provides that licences can include:

- conditions for the prevention or reduction of anti-competitive behaviour; and
- conditions allowing the JCRA to make determinations.

A Class III licence also includes conditions relating to the requirement to provide interconnection services and the production of a reference offer for interconnection services ("RIO"). The JCRA has previously issued directions to JT on the production of a RIO[1].

3.2 Regulatory framework

In April 2010, following a review of the markets for telecoms services in Jersey[2], the JCRA made the following decision with respect to significant market power ("SMP") in markets relevant to this Initial Notice:

- ***Voice call termination on individual mobile networks:*** *Each mobile operator, that is, JT, CWJ and JAL has SMP in the market for terminating calls on its own network;*

Condition 33.2 of the licence issued to JT provides that:

> *"The JCRA may determine the maximum level of charges the Licensee may apply for Telecommunications Services within a relevant market in which the Licensee has been found to be dominant. A determination may:*
>
> *a) provide for the overall limit to apply to such Telecommunications Services or categories of Telecommunications Services or any combination of Telecommunications Service;*

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1 *Direction of the JCRA 2004/3 Re: Jersey Telecom Limited's Reference Interconnect Offer,* 29 April 2004, see http://www.cicra.gg/_files/040429%20Initial%20Notice%202004-3.pdf

2 *Response to the Consultation Paper 2009 – T3, "Review of the Telecommunication Market in Jersey" and Decision on the Holding of Significant Market Power in Various Telecommunications Markets*, 21 April 2010, see http://www.cicra.gg/_files/100420%20market%20review%20decision.pdf

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

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

This condition therefore allows the JCRA to regulate the prices that JT charges for telecommunications services in a way and for a time that it deems appropriate, provided that JT has a dominant position in the relevant market in which those services are supplied.

Condition 34.1(c) of JT's licence is designed to protect fair competition in the markets in which JT operates, and provides as follows:

The Licensee shall:…

(c) comply with any direction issued by the JCRA for the purpose of preventing any market abuse or any practice or arrangement that has the object or effect of preventing, restricting or distorting competition in the establishment, operation and maintenance of Licensed Telecommunication Systems or the provision of Telecommunication Services.

This condition allows the JCRA to give directions to JT, including in relation to the prices that it charges.

As noted above, both JAL and CWJ have also been found in April 2010 to be dominant (or to possess SMP) in the provision of termination services on their networks. Part IV of their licences provide for the JCRA to impose further obligations in the event the JCRA determines the operator has SMP in a specific market. Those obligations include a Fair Competition condition (condition 27), part of which is in the same terms as Condition 34.1(c) of JT's licence, set out immediately above.

4. Regulation of MTRs in other jurisdictions

As mentioned earlier in this Initial Notice, regulators in a number of jurisdictions have in recent years imposed specific regulatory measures aimed at requiring mobile operators to reduce MTRs. The following provides some background on the measures adopted in a number of jurisdictions.

4.1 UK

The UK regulator Ofcom has been very active on the issue of MTRs. In 2011, it published its most recent decision on MTRs[3] and has implemented a price control which will see MTRs decline from 4.180ppm in 2010/11 to 0.690ppm by 2014/15 for the four main UK mobile operators (O2, Vodafone, Everything Everywhere and H3G (H3G's 2010/11 MTR was slightly higher than the other 3 main operators)).

Ofcom stated that it believed its approach would limit the MTRs of the four national mobile communication providers and limit all other designated mobile operators to "fair and reasonable" rates. In most cases, Ofcom's decision will result in a single wholesale charge for mobile operators on different networks, falling sharply each year. Ofcom believes this approach will deliver a simpler regime which will benefit consumers by promoting competition, and make it easier for operators to comply with Ofcom's rules.

Figure 1. Ofcom's Proposed MTRs (ppm)

	2010/11	**2011/12**	**2012/13**	**2013/14**	**2014/15**
Vodafone / O2 / Everything Everywhere	4.180	2.664	1.698	1.083	0.690
H3G	4.480	2.664	1.698	1.083	0.690

In determining these rates, Ofcom adopted a charge control for the four mobile operators based on pure-LRIC, as, in its view, such an approach best:

- promotes efficiency; and
- promotes sustainable competition in the retail mobile market in the UK,

and confers the greatest possible benefits on end-users of public electronic communication services.

Ofcom also stated that such an approach was consistent with the EU 2009 recommendation to NRAs on determining MTRs.

[3] http://stakeholders.ofcom.org.uk/binaries/consultations/mtr/statement/MCT_statement.pdf

Ofcom's decision is currently being reviewed by the Competition Appeal Tribunal and the Competition Commission.

4.2 EU Approach to MTRs

The European Commission in 2009 published a Recommendation on the Regulatory Treatment of Fixed and Mobile Termination Rates in the EU[4]. This recommendation is non-binding on NRAs within the EU; however, they are obliged take utmost account of it. The recommendation called for termination rates to be set based on a bottom-up "pure LRIC" cost model by the end of 2012. This "pure LRIC" cost model differs from the LRIC models that have previously been developed by regulators and operators (sometimes referred to as Long Run Average Incremental Cost (LRAIC) models), in that only traffic-related incremental costs can be recovered via the termination rate. All other incremental costs which are not related to traffic (e.g. coverage, spectrum and capacity related costs) cannot be recovered according to this new methodology.

NRAs have on the whole adopted the EC Recommendation as they have reviewed the call termination markets. However, many regulators have set later implementation dates than required by the Recommendation and others have indicated that they will not review termination rates until after the recommended deadline for implementation. Moreover, Ofcom, when reviewing BT's fixed termination rate in September 2009, decided not to implement the Recommendation:

> *"Ofcom acknowledges that the NCC [Network Charge Controls] cost model is not wholly consistent with the recommended approach set out by the Commission in its Recommendation, and that the ending of the new NCC (30 September 2013) falls nine months after the end date for transition to the Commission's recommended approach (31 December 2012).*
>
> *The Commission Recommendation sets out that termination service charges should be set by reference to pure long run incremental costs (LRIC) and costs modelled on the basis of next generation network (NGN) infrastructure whereas the NCC has been set using a hypothetical ongoing network model."*[5]

The EC Recommendation itself provides details of what regulators should do if they are unable to implement the recommended Pure LRIC model due to lack of resources. In such circumstances, NRAs can set prices based on an alternative approach (e.g. benchmarking), provided that this methodology *"results in outcomes consistent with this Recommendation and generate efficient outcomes consistent with those in a competitive*

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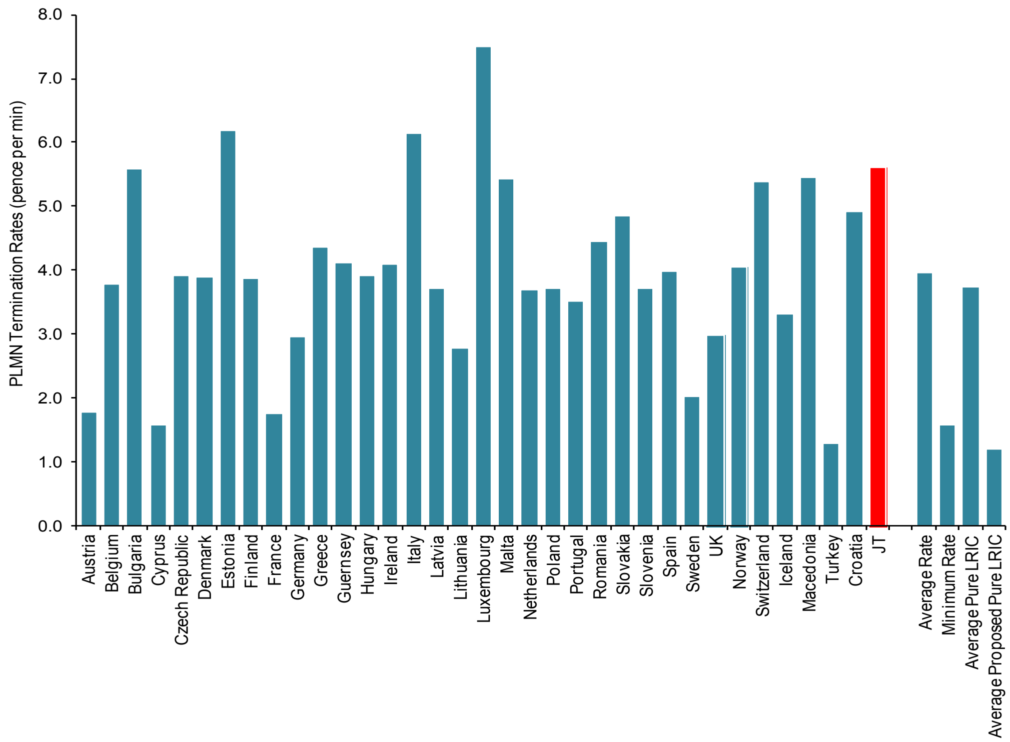
[4] Commission Recommendation of 7.5.2009 on the Regulatory Treatment of Fixed and Mobile Termination Rates in the EU, Brussels, http://ec.europa.eu/information_society/policy/ecomm/library/recomm_guidelines/index_en.htm

[5] Ofcom, *Review of BT's Network Charge Controls: Statement*, 15 September 2009, paragraph 1.13 and footnote 7

market" and the outcome *"should not exceed the average of termination rates set by NRAs implementing the recommended cost methodology"*[6].

Separately, as noted above, BEREC regularly publishes a 'snapshot' of MTRs in 33 European countries[7]. The report notes that the average MTR in the 33 countries in July 2011 was 4.5 euro cents per minute (or approximately 3.76ppm at current exchange rates). By comparison, the current Jersey MTR would rank as the 31st highest of the countries covered by the BEREC snapshot.

Figure 2 Comparison of Peak MTRs, 1st July 2011



Source: *BEREC MTR snapshot*

4.3 Guernsey

In February 2007, the OUR published a decision on MTRs in which it set a new maximum target average charge (TAC) for MTRs of 6.75ppm. This allowed each MNO the opportunity to charge different time of day MTRs so long as the average charge met the TAC specified by the Director General. This rate was fixed for a three year period until April 2010.

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6 Commission Recommendation of 7.5.2009 on the Regulatory Treatment of Fixed and Mobile Termination Rates in the EU, Brussels, 07.05.2009, paragraph 22

7 http://erg.eu.int/doc/berec/bor_11_35.pdf

In 2009, the OUR undertook a further review of MTRs, the objective of which was to set rates that were more closely related to actual costs than though a benchmarking approach. However, as the quality of the financial information from the three operators (C&W Guernsey, Wave Telecom and Airtel-Vodafone) varied significantly, following discussions with the three operators, all three agreed to implement a new lower flat rate MTR of 4.11ppm from 1st April 2010, a 40% decrease on the previous MTR charge. It was further agreed that no additional charge would be applied for any on-island transit of a call to be terminated on a mobile network as this was to be subsumed into the new MTR charge. Finally the new MTR would be billed on a per second basis effective from the first second, and would apply to the termination of voice calls in the individual mobile operator networks in Guernsey on a technology-neutral basis (which subsumes both 2G and 3G mobile network termination) and irrespective of the origin of the traffic.

5 MTR Proposal for MNOs in Jersey

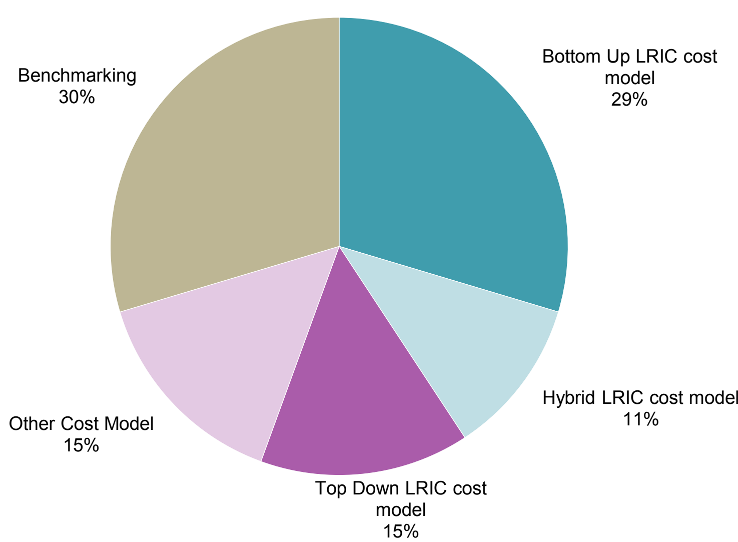
The JCRA has reviewed how MTRs in Jersey should be determined. It is mindful that in setting MTRs there is a need to balance the requirement for sufficiently sound data to support a fully cost-justified charge with the demands such obligations place on certain operators. Currently, JT is required to prepare regulatory accounts; however, CWJ and JAL are not subject to the same obligation.

5.1 Level and calculation method for the MTR

The JCRA is currently reviewing JT's interconnection charges for all services. That review has identified that JT currently calculates the cost of providing termination on its mobile network to be 4.469ppm yet charges a significantly higher rate to other mobile operators (who in turn reciprocate by charging the same rate to JT and each other). While the JCRA notes that the calculated cost is lower than the rate currently being charged by the MNOs, it is unclear that this lower charge is reflective of the efficient cost of providing mobile termination services. Therefore the JCRA is not inclined to rely upon it for determining MTRs.

In light of these issues, the JCRA has decided to use a benchmarking approach to determining MTRs for the three Jersey mobile operators. Benchmarking is already used by a number of NRAs in Europe to set MTRs

Figure 3 Methods used to set Mobile Termination rates in the EU



Source: KPMG analysis based on information from NRAs

The JCRA has had regard to the most recent BEREC benchmarking 'snapshot' which shows an average MTR for the 33 countries surveyed of 3. 91ppm (exchange rate of £1 = €1.1530 – the average exchange rate for the preceding 12 months from the date of this IN). While the JCRA believes such a rate might be justified in a Jersey context, it believes there is greater merit, in particular having regard to the interests of adopting a pan Channel Island approach to regulating mobile telecommunications services, to instead propose a rate cap of 4.11ppm, which is the MTR currently applied in Guernsey by the sister companies of the three Jersey mobile operators. It is proposed that this MTR cap would remain in place until 31st March 2013.

5.2 How should MTRs be charged?

The JCRA also proposes to apply the same terms to the application of MTRs in Jersey as in Guernsey; namely:

- there will be no additional charge applied for any on-island transit of a call to be terminated on a mobile network;
- mobile termination will be billed on a per second basis effective from the first second;
- the MTR will apply to the termination of voice calls in individual mobile operator networks in Jersey on a technology-neutral basis (which subsumes both 2G and 3G mobile network termination) and irrespective of the origin of the traffic.

Finally, in keeping with an understanding reached between the JCRA, JT, CWJ and JAL in January 2010 in relation to interconnection charges, it is proposed that the capped rate of 4.11ppm, applied on the terms described above, would be back-dated to 1st July 2011.

5.3 Is it appropriate for the JCRA to issue directions to JT, CWJ and JAL under the Fair Competition licence condition?

As noted in section 3 of this Initial Notice, Condition 34.1(c) of JT's licence, and Condition 27.1(c) of the licences of both CWJ and JAL, entitle the JCRA to issue directions "for the purpose of preventing any market abuse or any practice or arrangement that has the object or effect of preventing, restricting or distorting competition in the establishment, operation and maintenance of Licensed Telecommunication Systems or the provision of Telecommunication Services".

As stated, the JCRA has previously found that JT, CWJ and JAL are all dominant (or possess SMP, which the JCRA has regarded as synonymous with dominance for these purposes) in the markets for terminating calls on their own mobile networks.

Absent regulation, the JCRA considers that it is inevitable that there will not be effective competition in these markets, and that a likely outcome of such a lack of effective competition is that MNOs will have both the incentive and the ability to set excessive MTRs. At present, we observe that, even based on its own figures, JT sets its MTR at a level above cost (see note in paragraph 5.1 above), and while we do not have access to detailed cost information for CWJ and JAL, we think that an equivalent position is also likely in relation to those MNOs. Moreover, the fact that these operators voluntarily adopted an MTR of 4.11ppm for their networks in Guernsey in 2010, where those networks and operations would typically be smaller in scale than in Jersey (at least for JT and JAL), provides strong evidence that the cost of providing voice termination services for an efficient MNO in Jersey would be no more than 4.11ppm.

Ofcom, in its decision in relation to mobile call termination, noted that excessive MTRs can cause economic inefficiency and lead to competition concerns, even if MTRs were to be largely 'recycled' to consumers through handset subsidies[8]. In relation to competition, it observed that excessive MTRs could act as a barrier to entry of new MNOs, given that they will be much smaller than existing rivals, and might "also likely lead to higher (retail) charges for off-net calls than for on-net calls and create competitive distortions to the disadvantage of smaller networks"[9]. Ofcom also expressed concern that excessive MTRs would distort competition between fixed and mobile networks, thereby hampering the potential for increased competition between fixed and mobile services.

On balance, then, we have concluded that charging excessive MTRs (i.e. MTRs at a level above efficient cost) is a practice that could have the effect of preventing, restricting or distorting competition between MNOs, or between fixed and mobile networks. We have therefore provisionally determined that it would be appropriate to make directions under the Fair Competition conditions of the licences of JT, CWJ and JAL to cap their respective MTRs. For the reasons set out above, we have decided in the directions to adopt the MTR currently used by these MNOs in Guernsey.

The JCRA has considered whether it would be more appropriate for it to issue a determination in respect of JT's MTRs under Condition 33.2 of JT's licence. While the JCRA is confident that it is empowered to make a determination on JT's MTRs under Licence Condition 33.2, it is of the view that it would be preferable to proceed on the same legal basis when setting MTRs for each of the MNOs.

[8] See footnote 4 above; at paragraph 5.8ff.
[9] Id, at paragraph 5.11.3

6 Proposed directions

The JCRA proposes to issue a direction to JT under Condition 34.1(c) of JT's licence, and directions to CWJ and JAL under Condition 27.1(c) of their respective licences, as follows:

- The rate charged by the relevant licensee for voice call termination on its mobile network in Jersey ("the mobile termination rate") shall be no more than 4.11 pence per minute;

- there shall be no additional charge (other than the mobile termination rate) applied by the relevant mobile network operator for any on-island transit of a call to be terminated on a mobile network;

- the mobile termination rate shall be billed on a per second basis effective from the first second; and

- the mobile termination rate shall apply with respect to all voice calls terminated by the relevant mobile network operator in Jersey on a technology-neutral basis (i.e. on both 2G and 3G mobile networks) and irrespective of the origin of the traffic.

The directions shall be deemed to have come into effect on 1 July 2011, and shall expire on 31 March 2013.

7 Next Steps

The proposed directions will take effect on 17 February 2012, unless representations or objections are received in relation to them, in which case the relevant date will be set out in a Final Notice published under Article 11(5) of the Telecoms Law.

Representations or objections in relation to the proposed directions can be made in accordance with the arrangements set out in section 2 of this Initial Notice.

The JCRA and OUR intend to undertake a further review of MTRs in both Guernsey and Jersey during 2012, as it is recognised that significant reductions in MTRs are planned in a number of European countries in the near future and it is important that consumers in the Channel Islands similarly benefit. While it is noted that EU regulators are moving increasingly to rely (with the encouragement of the European Commission) on more sophisticated costing models upon which to base more cost-reflective termination charges. However, the JCRA and the OUR wish to assess whether, in the context of the Jersey and Guernsey markets, the development of such costing models would be proportionate or whether the continued use of benchmarking would be a more suitable approach.

The JCRA will also shortly be publishing proposals on fixed interconnection rates for JT and it is similarly intended that the effective date of any amended rates contained in such proposals will be back-dated to 1 July 2011.