Why Charging Higher than Regulated Termination Rates to Traffic Originating Outside the European Economic Area (EEA) is Not Justified

Introduction

Over the last years a growing number of EEA telecom providers have been charging higher (mobile and fixed) termination rates for voice traffic originating outside the EEA as opposed to the regulated (cost-based) rates for traffic within it, and in most instances with the implicit or explicit support from the relevant National Regulatory Authority (NRA) and the European Commission (EC).

This paper outlines why such differential rates are unjustified, damaging, and may well be violating the EU telecommunications rules, general competition rules and the WTO General Agreement on Trade in Services (GATS).

The rationale for this practice seems to be a desire to compensate for higher termination rates charged by some non-EEA providers, as a sort of "retaliation" measure. This approach is particularly questionable when applied to traffic originating in countries where rates do not seriously exceed the EEA rates or are even lower, such as the United States (US).

Facts

Call termination services are interconnection services provided by telecommunications operators to other telecommunications operators. Such services allow for the completion of a call initiated on another telephone network. Call termination services can be provided for traffic originated in-country or abroad. Termination can also be provided over fixed or mobile voice networks.

Originally termination rates were regulated by the NRAs regardless of where traffic originated from. The same cost-oriented rates were mandated for all traffic, no matter where it came from.

Nonetheless, since 2014 an increasing number of EEA providers have started charging higher rates for traffic originating outside the EEA. In most cases these practices were introduced with the implicit or even explicit consent of NRAs. Some NRAs decided to limit their regulatory competence to traffic originating inside the EEA, thus implicitly allowing higher rates for traffic from elsewhere. Moreover, some NRAs explicitly allowed higher rates to be applied horizontally to traffic originating outside the EEA, as a response to high rates in some non-EEA countries.

Consequently an increasing number of EEA providers have been charging much higher rates for traffic originating outside the EEA as opposed to the regulated (cost-based) rates for traffic within it. Whilst some European providers are (rightly) exempting US originated traffic from these higher termination rates many others simply apply one higher termination rate for all traffic from outside the EEA, as is illustrated by the chart in Annex 1.

These practices result in substantial cost increases for Verizon's US originating traffic to the EEA and affect its ability to provide affordable voice services to US consumers calling the EEA.

Regulatory Analysis

The higher rates for non-EEA traffic do not appear to reflect incremental costs for termination of such traffic and there is no other fact-based justification for these higher rates. These practices may therefore well be violating EU sector specific telecommunication rules and general competition law rules as well as the GATS.

Violation of EU sector specific telecommunication rules

In most if not all EU member states NRAs have determined that mobile and fixed terminating providers have Significant Market Power (SMP) and are therefore obliged to apply cost-based rates in a non-discriminatory fashion. The calculation of the cost-based rates in most instances follows the BU-LRIC cost-methodology as recommended by the EC.

We have strong doubts that the application of differential rates depending on whether the traffic originates inside or outside the EEA complies with the principles of non-discrimination and cost-orientation.

Violation of competition law

Under EU competition law mobile and fixed providers are considered to be dominant in the termination of voice calls on their network and it may well be that the application of higher prices for traffic from outside the EEA as opposed to traffic from within the EEA will constitute an abuse of a dominant position.

The charging of higher termination rates to traffic originating outside the EEA may be considered to be excessive and discriminatory pricing, as these higher rates are clearly excessive related to the "economic value" of the service, and the underlying costs do not differ depending on the country in which the traffic originates.

Violation of GATS

The application of differential termination rates may well be in violation of the WTO GATS in three ways, which is outlined in more detail in Annex 2:

1. A key principle of the WTO and the GATS is Most Favored Nation (MFN) that prohibits measures treating the service suppliers of one Member less favorably than any other.
2. Article 5(a) of the Annex on Telecommunications requires Members to "ensure that any service supplied of any other Member is accorded access to and use of public telecommunications transport networks and services on reasonable and non-discriminatory terms and conditions".
3. The "Reference Paper" requires "major suppliers" to interconnect with rates being cost oriented, transparent, and reasonable.

Conclusion

We strongly believe that the regulated cost-based termination rates of EEA providers in principle should equally apply to traffic originated in any country, in a non-discriminatory manner.

This is even more relevant for traffic originating in countries that do not apply high(er) termination rates than in the EEA, such as the US. It would be a good step forward if cost-based rates would also apply to traffic originating from such countries as some EEA NRAs and providers have already decided.

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Annex 1 – Country Overview

Country	Mobile (MTR) or Fixed Termination (FTR)	Surcharge in place	Surcharge in place since / as of	Surcharge applies to traffic that originates from	Surcharge allowed by NRA?	Comments
Austria	MTR	Yes	Apr 2016	Non-EEA, except US & White List	Yes, but only on a reciprocity basis	RTR draft decision would allow surcharge for calls originating in EU/EEA-countries where BULRIC model is not yet implemented
	FTR	Yes	Apr 2016	Non-EEA, except US & White List	Yes, but only on a reciprocity basis	
Belgium	MTR	Planned	Q4 2016	Non-EEA, except US & White List	Yes, by explicitly allowing differential/higher rates for non-EEA	According to Draft Market Review Decision only - Pending full BULRIC implementation
	FTR	Yes (but only Proximus)	Apr 2016	Non-EEA, except US & White List	Yes, by explicitly allowing differential/higher rates for non-EEA	According to Draft Market Review Decision only
Bulgaria	MTR	Yes	Jul 2016	Non-EEA	Under assessment	Lower surcharge for US origination from Vivacom BTC and Mtel
	FTR	Yes	Jul 2016	Non-EEA	Under assessment	Lower surcharge for US origination
Croatia	MTR	Yes	Apr 2015	Non-EEA	Yes, by only regulating rates for EEA	
	FTR	Yes	Apr 2015	Non-EEA	Yes, by only regulating rates for EEA	
Czech	MTR	Yes	Sept 2014	Non-EEA	Yes, by only regulating rates for EEA	
	FTR	Yes	Aug 2014	Non-EEA	Yes, by only regulating rates for EEA	
Denmark	MTR	No				
	FTR	No				
Estonia	MTR	Yes	Jun 2016	Non-EEA	Under assessment	
	FTR	TBC	TBC	TBC	Under assessment	
Finland	MTR	No				
	FTR	No				
France	MTR	Yes	Q1 2014	Non-EEA, except US & White List	Yes, but only on a reciprocity basis	
	FTR	Yes	Q1 2014	Non-EEA	Yes, but only on a reciprocity basis	Orange and BouygTel still applying surcharge on FTR for non-EEA including US origination. SFR and Free exclude US
Germany	MTR	Yes (but only E+ and O2)	Feb 2013	Black List (Serbia, Morocco, Russia, Turkey, Ukraine)	No - but BNetzA might allow operators to block traffic from specific countries under certain conditions, with prior approval	E+ & O2 consider their approach in line with the market analyses of BNetzA; MTR Market Review currently underway
	FTR	No				
Greece	MTR	Yes	July 2015	Non-EEA	Yes, by only regulating rates for EEA	
	FTR	Yes	Sept 2015	Non-EEA	Yes, by only regulating rates for EEA	
Hungary	MTR	Yes	Nov 2015	Non-EEA	Yes, by only regulating rates for EEA	
	FTR	No				
Ireland	MTR	No			No	regulated MTRs also apply to traffic that originates from outside the EU/EEA
	FTR	No				
Italy	MTR	Yes	Q3 2015	Non-EEA, except US & White List	Yes, by only regulating rates for EEA	Draft decision only at this stage
	FTR	No				
Latvia	MTR	Yes	July 2016	Non-EEA	Under assessment	
	FTR	Yes	July 2016	Non-EEA	Under assessment	
Lithuania	MTR	Yes	Jan 2016	Non-EEA	Under assessment	
	FTR	Yes	Jan 2016	Non-EEA	Under assessment	
Luxembourg	MTR	No				
	FTR	No				Introduction of surcharge considered under ongoing 3rd round Market Review
Netherlands	MTR	No				
	FTR	No				
Poland	MTR	Yes	Apr 2016	Non-EEA	Yes, by only regulating rates for EEA	
	FTR	No			Yes, by only regulating rates for EEA	
Portugal	MTR	Yes	Sept 2015	Non-EEA	Yes, by only regulating rates for EEA	
	FTR	No				
Romania	MTR	No				
	FTR	No				
Slovenia	MTR	Yes	Jun 2016	Non-EEA	Under assessment	Lower surcharge for US origination from Telekom Slovenije (PTT)
	FTR	Yes	Jun 2016	Non-EEA	Under assessment	Lower surcharge for US origination from Telekom Slovenije (PTT)
Spain	MTR	No	sept-16	Non-EEA, except US & Canada	Under assessment	Surcharge applied by Orange Mobile Spain only to date
	FTR	No				
Sweden	MTR	No			No	regulated MTRs also apply to traffic that originates from outside the EU/EEA
	FTR	No			No	regulated FTRs also apply to traffic that originates from outside the EU/EEA
United Kingdom	MTR	No				
	FTR	No				

EEA: European Economic Area = European Union + Iceland, Lichtenstein, Norway (Switzerland membership not ratified)

Bosnia	MTR	Planned		TBD		
	FTR	Planned		TBD		
Norway	MTR	Planned		Non-EEA	Yes, by only regulating rates for EEA	
	FTR	Planned		Non-EEA	Yes, by only regulating rates for EEA	
Switzerland	MTR	Yes	Dec 2015	Black List (countries that surcharge Swiss mobile origination - US exempt)	Under assessment	
	FTR	No				

Annex 2

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The EEA'S Discriminatory Telecommunications Termination Rates Violate the General Agreement on Trade in Services

Introduction

- One main cost component of connecting an international circuit from the United States to another country is the rate a foreign telecommunications operator charges a U.S. operator to "terminate" the call on the foreign operator's network and deliver it to the local consumer.
- The U.S. Trade Representative (USTR) has identified telecommunications termination rates as a foreign trade barrier imposed by European Union (EU) and European Economic Area (EEA) countries (hereinafter EEA).
- According to USTR, "several suppliers in EU Member States . . . are charging higher rates for the termination of international traffic originating outside the EU, or in some cases outside the European Economic Area . . . than for international traffic between sovereign states within the EU or EEA." These differential rates "do not appear to reflect incremental costs for termination of such traffic."
- The EEA's actions violate the GATS in three ways:
    - A fundamental principle of the WTO and the GATS is Most Favoured Nation (MFN). MFN (Article II) prohibits measures treating the service suppliers of one Member less favourably than any other.
    - Article 5(a) of the Annex on Telecommunications requires Members to "ensure that any service supplied of any other Member is accorded access to and use of public telecommunications transport networks and services on reasonable and non-discriminatory terms and conditions."
    - The Telecommunications Services Reference Paper, adhered to by all EEA countries, requires (Section 2.2) "major suppliers" to interconnect with rates being cost oriented, transparent, and reasonable.

Facts

- The (EU), its Member States and (EEA) countries are signatory Members of the WTO General Agreement on Trade in Services (GATS), and took no relevant exemptions in the GATS telecom markets to these commitments.
- A critically important telecommunications service here is cross-border termination, where networks of one service supplier are connected to another service supplier in a different country. Termination sometimes occurs between service suppliers of two EEA nations; in other cases, it occurs between a service supplier terminating traffic in an EEA country that originated outside the EEA, such as from the United States.
- A growing number of EEA carriers are charging higher (mobile and fixed) termination rates for telephone traffic originating outside the EEA as opposed to the regulated (cost-based) rates for traffic within it.
- This imbalance began with price increases in late 2014; additional increases have taken effect in 2015 and 2016.

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- EEA termination rates for traffic originating outside the EEA have risen to as much as € 0.3450 (Portugal Mobile). By comparison, the average termination rate for traffic from the EEA to US is € 0.003. There is no cost justification for the higher termination rates on non-EEA originated traffic.
- The Office of the United States Trade Representative has singled out this discrimination in 2015 and again in 2016. Unequal termination charges "raise concerns" about the EU's compliance with GATS and the Telecommunications Annex, *see* USTR 2015 Section 1377 Report at 11-14, and "appear to endorse, explicitly or implicitly, a two-tier approach to the termination of international traffic", in violation of the Reference Paper, *see* USTR 2016 National Trade Estimates (NTE) Report at 165.

Arguments

These Discriminatory Interconnection Rates Violate GATS Article II MFN

- Differential interconnection rates are *prima facie* evidence of disparate treatment of GATS Members, in violation of MFN treatment, nullifying and impairing the benefits of other WTO Members.
- Interconnection is a basic telecommunications service covered by GATS Article II. See *Mexico – Measures Affecting Telecommunications Services*, WT/DS204/R, ¶¶ 7.277-88 (April 2, 2004) (where principal issue concerned Telecom Reference Paper) (hereinafter "*Mexico Case"*).
- The EEA's actions constitute "measures" under Art I(3) of the GATS:
    - The European Commission's Recommendation on Fixed and Mobile Termination Rates (2009/396/EC) required harmonization and common cost-based approach for setting termination rates within the EU, while omitting any mention of external rates. This is itself a "measure", to the extent it failed to prevent violations of MFN.[1]
    - Following that, some national EU telecoms regulators (Croatia, Czech, Portugal, Poland, etc.) - with the implicit consent of the European Commission - approved clear "measures" i.e. termination rates less favorable for traffic originated outside the EEA than the regulated (cost-based) rates for traffic originated inside the EEA.

The EEA's Actions Violate Article 5 of the Annex on Telecommunications

- The EEA's actions also violate Article 5(a) of the Annex on Telecommunications, which requires Members to "ensure that any service supplied of any other Member is accorded access to and use of public telecommunications transport networks and services on reasonable and non-discriminatory terms and conditions. . ."
- "The term 'non-discriminatory' is understood to refer to most-favored-nation and national treatment as defined in the Agreement, as well as to reflect service-specific usage of the term to mean "terms and conditions no less favorable than those to any other user of like public transport networks or services under like circumstances." (Telecom. Annex, Art. 5(a) n.15.)

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[1] Under GATT and GATS precedent, a "measure" also encompasses a Member's failure to act to prevent a violation. *Guatemala – Cement*, WT/DS60/AB/R, ¶ 69 n.47 (Nov. 2, 1998) (GATT) ([a] measure can . . . be an omission or a failure to act on the part of a Member.") (citations omitted). Similarly, "de facto" actions can constitute a measure. *European Commission – Biotech Products*, WT/DS291/R, ¶ 4.254 (Sep. 20, 2006) (panel report).

- The EEA's rates clearly discriminate, contrary to the Annex's obligation that Members continue to ensure "access and use" of telecom networks on "reasonable and non-discriminatory terms."
- EEA Member States cannot justify higher rates for traffic originated outside the EEA. The fact that some countries, mostly in Africa, are charging very high termination rates does not excuse rate increases for the rest of the world. Nor does the absence of CLI on some foreign-originated calls increase the cost of routing, as certain EEA operators have claimed. There has been no cost or other fact-based analysis justifying the higher tariffs.
- Further clarifying the point, Annex 5(b) says "each Member shall ensure that service suppliers of other Members have access to and use of any public telecommunications transport network or service offered within *or across the border of that Member*" (emphasis added). *See also Mexico Case*, WT/DS204/R, ¶ 7.288.

The EEA's Actions Also Violate the Reference Paper on Basic Telecommunications

- The Reference Paper, adhered to by the relevant parties here, specifically addresses cross-border interconnection between different suppliers of telecommunications networks (Section 2.1) (*Mexico Case* WT/DS204/R ¶ 5.48, 5.52.
- The Reference Paper requires (Section 2.2) "major suppliers" to interconnect:
  - At any technically feasible point;
  - Under non-discriminatory terms;
  - Including technical standards, and costs, no less favorable than provided to itself or to non-affiliated providers;
  - With rates being cost oriented, transparent, and reasonable.
- Many if not all of the terminating EEA carriers have been recognized under local law as having "significant market power", i.e., being "major suppliers." As set forth above, the terms of the cross-border interconnection are patently discriminatory.
- USTR made this very point in its NTE Report, noting although EEA countries agreed to ensure "a major supplier is not able to gain an unfair competitive advantage from terminating foreign or competitive calls," several suppliers were charging higher rates for international termination despite the absence of any differences in incremental cost.
- As a result, the Members in which Verizon is seeking to interconnect are nullifying and impairing U.S. benefits under the Reference Paper by permitting different prices for EEA and non-EEA interconnection.
- Further, Members are likely using higher rates on non-EEA originated traffic to prolong low interconnection rates within the EEA – which could be considered anti-competitive cross-subsidization, forbidden by Section 1.2(a) of the Reference Paper.

Conclusion

- We believe that the EU/EEA's actions violate the GATS, Annex 5 and the Telecommunications Reference Paper.
- USTR already is aware of the issue and identified it as a concern in both in 2015 and again in 2016.
- The EU should remedy this situation rapidly to avoid the need to raise it further as a trade issue.

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