RSL COM AUSTRALIA PTY LTD

SUBMISSION

PRICING METHODOLOGY
FOR THE
GSM TERMINATION SERVICE

In response to the ACCC DRAFT REPORT OF DECEMBER 2000

Background

RSL COM makes this submission in response to the Commission's request for comment on its draft paper.

RSL COM seeks GSM Termination access for the purposes of terminating Fixed to Mobile calls. This traffic type is obtained as a consequence of the inclusion of F2M in the bundled preselection basket, and is generally terminated on the three dominant mobile networks.

Additionally, RSL COM resells F2M calls from services that are sold to customers via the Lesseeship Model and Line Management Model. In these instances, the customer is a directly connected Telstra customer who has elected to utilise RSL COM as a reseller.

In some circumstances, a customer may utilise both the RSL COM network and the RSL COM resale service to obtain a single bill, which may include F2M calls from both sources.

As a result of the above, RSL COM is critically interested in the outcomes and application of the principles described in the Commissions paper.

RSL COM does not operate a mobile network, but is a reseller of two mobile networks.

This submission is written from this perspective.

1. Control Over Access and Consumer Ignorance

RSL COM contends that the consumer has no control over the termination of a F2M call. Irrespective of whether the consumer is the called or the calling party, only one mobile network can terminate the call, which is the mobile network that the mobile subscriber has subscribed to.

In the absence of any viable transit arrangements, an SP who has received an F2M call for termination has no choice but to pass the call directly to the mobile subscribers network.

Clearly then, the mobile networks are in a dominant position, retaining all control over access.

The provision of mobile number portability in Sept 2001 does not affect this position. The call still needs to terminate on the destination network.

We do not believe that consumer ignorance is a significant factor in this matter. A customer intending to make a F2M call does so out of need, and does not generally consider which network the called party is with, or what the charge is likely to be.

F2M is a preselectable service. The customer making the call will have already made a determination as to which SP is to carry the call. This decision will have been made on the prices, terms, conditions and perception of the capability and quality of that SP's network, and not on the likely wholesale access prices charged by the various mobile networks. Additionally, F2M termination at the demand side of the market has frequently been used as a loss leader, thereby distorting any perception that the consumer may have regarding the general cost of calling any particular network.

It is our belief that the pervading issue is not the level of customer ignorance, nor what level of control that a consumer may at present have over who terminates the call, but rather the maintenance of higher than reasonable wholesale rates for the termination of F2M calls. It is the maintenance of these rates that prevents substantial competition occurring, and the maintenance of these rates that prevents the consumer from enjoying the benefits of lower F2M rates.

2. Transit Arrangements

In its original submission, (July 2000), RSL COM made the point that the unwillingness of the dominant networks to negotiate viable transit arrangements is a limitation to competition.

Whilst one integrated mobile carrier has been prepared to offer transit rates to RSL COM, these rates have been greater than the rates available for non-transit termination, and therefore are not a viable option.

Significantly, the only method offered for access to GSM termination by the integrated mobile carriers is via their fixed wire networks. This prevents the development of ‘2nd tier” transit carriers, who would potentially be able to develop commercially viable wholesale transit products.

The development of 2nd tier transit carriers would provide for an alternative method of transit that would provide significant competition to the existing mobile carriers.

RSL COM has sought, and been refused, the opportunity to interconnect directly to the mobile networks of integrated mobile carriers, and has therefore not been able to develop a transit product itself. Such an interconnect (direct to the mobile network) has the potential to deliver cost savings by removing the fixed wire network to mobile network component currently provided by (and charged for in the F2M rates) the integrated carriers, and permit the service provider to source this link itself.

No mitigation of control is therefore available, in our view, by available transit arrangements. We do however welcome the development of transit options, and recognise that in a market with well-developed and competitive transit arrangements, these arrangements would have a significant competitive effect.

3. Countervailing Power Of Fixed Line Carriers Seeking GSM Termination

A balance in negotiating power is only available where both parties have similar products and volumes to offer each other. In our experience, an SP without a mobile network has no power, and is totally dependant on the mobile carrier for the provision of GSM terminating access.

Whilst the mobile network would have difficulty in refusing to provide GSM terminating access, it does have the power of a monopolist in respect of the terms, conditions and prices.

The access SP has little or no choice but to accept preselected F2M calls from its customers, and is dependant on the mobile networks to terminate these calls. The mobile network has no similar dependency on the access seeking SP.

4. Control Over Access to GSM Termination in Relation to Fixed to Mobile Calls

From RSL COM’s position in the market, F2M wholesale rates have reduced only minimally since the addition of F2M to the preselection basket.
As discussed in our original paper, it is our belief, (supported by commentary from the integrated carriers), that F2M wholesale rates (and presumably the carriers own

retail rates) provide a significant cross subsidy to support the provision of new connections to the mobile networks.

The argument put forward in defence of this cross subsidy is that without the cross subsidy, the growth in the penetration of mobile services would reduce, and the cost of new connections would rise substantially. This argument does not justify the cross subsidisation of the mobile networks by fixed wire networks. A counter argument could be made that mobile networks should cross subsidise investment in fixed wire infrastructure by a surcharge on Mobile to Fixed calls. Such a cross subsidy would be of great benefit to fixed wire networks wishing to enter into the local loop market. This would also provide some socially desirable outcomes in the form of increased local loop competition.

Looking at new subscription offers available from the dominant mobile networks, it seems that the competition between the mobile networks is primarily based on offers of new handsets at no or low cost, no connection fees, etc. This begs the questions:

- At what point does the financial support of the mobile networks by fixed wire networks cease to be a cross subsidy to assist in the penetration of mobile services (a socially desirable outcome) and become a source of profit taking for the mobile networks (a monopolistic and inefficient use of resource)?

- What is the socially desirable level of penetration that mobile services should achieve before the necessity for support from the fixed wire networks ceases to be necessary?

- Is this cross subsidisation really required, or is it simply a mechanism for mobile networks to maintain artificial profit lines?

- Is it the cross subsidisation of mobile networks that makes investment in such networks attractive, and if so, is this an efficient investment?

From our perspective, it would seem that there is little or no requirement for any subsidisation of the mobile networks, particularly as it appears that market penetration has risen sharply, the number of mobile networks has increased significantly in the last 12 months (indicating that there is a real return on investment available) and the level of competition for new subscriptions has developed to the stage where a new subscription can be free to the new subscriber.

It may also be possible that the relatively high cost of F2M rates is a disincentive to new mobile subscriptions where that new service is going to be predominantly or significantly used for the receipt of F2M calls, such as in parts of the residential market.

5. Comparison of Pricing Methodologies

Forbearance

RSL COM contends that forbearance will simply result in a continuation of the existing outcomes.

These outcomes provide artificially high returns to mobile networks from F2M calls, and are used to subsidise competition within the mobile market. Further, we would argue that this cross subsidisation does not aid competition, as all mobile networks charge similar wholesale F2M rates. In the absence of this cross subsidisation, one would conclude that the levels of competition would, relatively speaking, be the same.

No social benefit is obtained from high GSM termination charges, and it is more likely that the perceived profits available from the mobile networks may lead to inefficient investments, leading to social harm.

Telstra raises the question as to whether regulatory intervention is required, and seems to favour a forbearance approach. We have difficulty in understanding how this approach will ever result in this market segment becoming more competitive, since, as a general principle, " if we keep doing what we're doing, we'll keep getting what we got " In the absence of any compelling evidence that would indicate the willingness of mobile networks to reduce wholesale rates of their own volition, it is apparent that only regulatory intervention will create change.

Clearly, some change is needed if the cost, at both the demand and supply side of F2M, is to reduce to more realistic levels.

With regard to the Commissions statement that

" *this approach would require the commission to have a pricing principle that recommended access prices for gsm termination be set by the market using commercial negotiations"*

The use of commercial negotiations is the preferred mechanism. It is our understanding that whilst the Commission's various access-pricing principles are something that parties should have regard to, the principles are in essence those principles that the Commission would have regard to in any arbitration. The principle that parties should endeavour to achieve a satisfactory outcome by commercial negotiation is already well established. It is a commentary on the effectiveness of monopolies that no mobile network has been prepared to negotiate commercially justifiable wholesale rates.

Marginal/Incremental Pricing

RSL COM is generally supportive of a TSLRIC approach to pricing of GSM termination. In addition to generally meeting the Commission's pricing principle requirements, it also provides for consistency with other access pricing that may be used in conjunction with GSM termination, (in particular, GSM termination for F2M).

It is our belief that consistency in the pricing principles applicable to all preselectable call types is necessary. Without a consistent approach to pricing, inconsistencies in the outcomes will occur and the allocation of common network costs utilised in the establishment of each access price will become distorted.

The arguments used against a TSLRIC approach fail to convince;

- **Inappropriateness.** The mobile marketplace is not unique in the telecommunications industry. The industry as a whole can be characterised by its dynamic and changing nature.

  To say that efficient investment is of paramount importance is no more accurate for the mobile market than for any other market. If, however, efficient investment in this market is somehow more paramount that it is for the fixed wire market (where TSLRIC is used extensively), then one would suppose that the efficiency is detrimentally affected by cross subsidisation from other markets. It is difficult to see how an argument can be sustained for efficient investment in mobile networks when that investment is sustained by a cross subsidy from another network. If the viability of the mobile networks is reliant on this cross subsidy, then the investment can only be viewed as inefficient.

  This also presupposes that F2M calls form part of the mobile market and not part of the fixed wire market. (We would contend that the latter is in fact the case). If F2M calls are part of the mobile market, this can only be because the call terminates on a mobile service. Using this same argument, a M2F call must form part of the fixed wire market, because the call terminates on a fixed wire service. Logically, if the call originates in the fixed wire market, and is associated with the preselectable basket, then the call type forms part of that fixed wire market, and, referring to our previous point, consistency in the pricing principles is sensibly required.

- **Effective Competition** There is no effective competition in the F2M market, and therefore TSLRIC is wholly appropriate.

- **Costly Approach.** This argument, like the first, ascribes characteristics to the mobile market that are simply not unique. Whilst this point may be a potentially valid argument against the use of the TSLRIC model in all circumstances, it is not a good argument for avoiding its use in an F2M pricing model.

Given the age of some GSM Termination disputes, it is apparent that the lack of a set of pricing principles has created costly, adversarial and lengthy delays already.

The application of TSLRIC pricing principles do not become subjective and inapproprite simply because they are applied to F2M costs. If these principles are subjective when applied to F2M, then they must also be subjective when applied to other access pricing situations. To the extent that they may incur any degree of subjectivity, if they are also used in the F2M environment then at least the level subjectivity will be consistently applied.

Retail Minus Methodology

As stated by the Commission, Retail Minus is unlikely to be a suitable option for a network based call type like F2M. Notably, one of the prime differences between LCS and F2M is the opportunity for F2M to be carried in part via an SP's own network, hence the requirement for GSM Termination. LCS on the other hand, is essentially a resale service where the call does not touch the access seekers network.

RSL COM believes that these differences are sufficient, when taken in conjunction with the Commissions comments on retail Minus, to make Retail Minus an unlikely solution.

Benchmarking

Benchmarking is in our view, unlikely to produce the desired outcomes. Principally we envisage administrative problems associated with the establishment of the initial 'start point' and the establishment and maintenance of an averaged retail price.

The possibility exists for retail prices to be maintained by the larger networks. The benchmarking of a wholesale rate against retail rates provides a motivation to minimise any reduction in retail rates. The weighted average of retail rates will be significantly affected by the retail inputs of the larger networks. As the two largest networks are also integrated (mobile and fixed wire) networks, the rate of decline of retail rates may be subject to strategic positioning rather than competitive forces.

Start Point

An initial start point is proposed as the *" average existing access price for GSM termination in relation to fixed to mobile calls levied by Telstra, Cable & Wireless Optus and Vodaphone".*

It is not clear from this statement how this would function in a practical sense.

Would this average for instance, include the internal transfer rates applied by each of the mentioned carriers? If this rate were excluded, then potentially the retail arms of those organizations would enjoy a commercial advantage.

A number of averaging methods present themselves. Averaging could be achieved by summing all charges levied, divided by the sum of all corresponding minutes of traffic. This would provide an average charge per minute.

Alternatively, the wholesale charges currently levied could be summed and divided by the number of charges. This will also provide an average.

The definition of 'start point' provided by the Commission does not clearly define whether each mobile carrier would separately establish the average in respect of their network, or whether the average would be an average of all networks. If it is the average of all networks, then it is difficult to see how each mobile network could legitimately obtain the necessary information to perform the averaging exercise.

In any commercial negotiation, it would be difficult for the access provider to substantiate the rate without potentially breaching commercial confidentiality agreements with other access seekers.

One 'start point' methodology that may be appropriate is the current intra operator rate for Mobile-to-Mobile termination. It is a reasonable assumption that the cost of terminating a call on the mobile network is essentially the same, whether the call originates at a mobile phone or a fixed wire phone. Intra Operator is suggested as more appropriate as this internal transfer rate is likely to avoid cross subsidisation charges and is more likely to reflect true costs that any other available rate. This of course does not include the costs associated with the delivery of the call to the mobile network.

Once a methodology for determining a start point was established, this would have the effect of creating a single rate for all access seekers, irrespective of real costs, volume related benefits, or cost reductions associated with the geographic dispersion of calls.

Retail Price Movement

Earlier in its paper, the Commission expresses the view that competition in the F2M market is weak. In this section however, the Commission suggests that this is an increasingly competitive area.

RSL COM is of the view that this section of the market is devoid of any competitive pressure, and if anything, the benchmarking approach is likely to reduce competitive pressures as stated earlier.

The measurement of retail prices is likely to be an extremely complex exercise. A quick count of one of the integrated carriers price plans reveals 28 different plans and packages, this does not include the potential variables achievable by combining each of the plan and package types. Nor does this include price plans available via 'VPN' type plans available under their mobile network, or any 'special retail arrangements' that may exist with various strategic or large customers (which would presumably remain confidential between the parties, and therefore not included in any calculation), or 'one off specials'

Establishing the % impact that a change in one of these may have is likely to be a long, costly and complex process, that each access seeker would need to endeavour to do if they wished to maintain appropriate downward pressure on wholesale rates.

Multiplying this complexity by three (the number of major mobile network providers) becomes, in our view, so complex as to be unmanageable.

Summary

In summary, RSL COM sees much benefit is maintaining consistency with other access pricing principles used to establish wholesale rates for the other preselectable services. The use of TSLRIC principles tends to achieve this. Bear in mind also that there is a greater degree of familiarity with TSLRIC pricing within the industry than for any of the other methods suggested.

The concept of benchmarking, whilst superficially attractive, does appear to be a costly and complex method.