2011 Section 1377 Review

On Compliance with

Telecommunications Trade Agreements

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Results of the 2011 Section 1377 Review of Telecommunications Trade Agreements

Introduction

USTR annually reviews the operation and effectiveness of U.S. telecommunications trade agreements and the presence or absence of other mutually advantageous market opportunities, pursuant to Section 1377 of the *Omnibus Trade and Competitiveness Act of 1988*. The Section 1377 Review ("Review") is based on public comments filed by interested parties and information developed from ongoing contact with industry, private sector, and foreign government representatives in various countries. This year USTR received comments from twelve companies and trade associations and reply comments from one company and one foreign government. All public comments are available at the following web-site: www.regulations.gov, docket number USTR-2010-0034.

Summary of Findings

This 2011 Review addresses several general themes: **increases in fixed and mobile call termination rates** in Ghana, Jamaica, Tonga; **problems relating to access to major supplier networks** in Chile, Germany, India and Mexico; **issues relating to licensing, transparency and regulatory requirements** in China, Costa Rica, and India and **issues affecting the telecommunications equipment trade** in Brazil, Chile, China, Costa Rica, India, Israel, and Mexico.

Although several of the issues in the 2011 Review have been discussed in past Reviews, USTR considers it appropriate to continue to raise these issues and encourage our trading partners to implement appropriate solutions. The 2011 Review describes practices or measures of U.S. trading partners that USTR will actively monitor throughout the year and with respect to which, if warranted, USTR may take further action.

Discussion of Key Issues

INCREASES IN FIXED AND MOBILE CALL TERMINATION RATES

Tonga – Termination Rate Increase

In last year's Review, USTR urged the government of Tonga to follow through on its pledge to rescind the mandated rate of US$ 0.30/minute rate that it had unexpectedly announced in August 2008. U.S. carriers were previously paying a termination rate of approximately US$ 0.13/minute and were in the process of renewing their interconnection agreements with the country's major supplier, the fixed-line operator

Tonga Communications Corporation (TCC) when the increase was announced. U.S. carriers refused to pay the new government-mandated rate, which they believed was unacceptably high, and TCC cut off the circuits used to deliver their traffic. TCC maintained that it was simply increasing the rate in order to comply with the government's rules. Tonga (which owns TCC) claimed that the rate increase is justified as a means to cover TCC's costs.

Although Tonga did effectively rescind the mandatedUS$0.30/minute rate as of April 1, 2010, USTR recently learned that Tonga replaced that mandate with a new requirement that will ensure that the rates remain artificially above cost. The government of Tonga is apparently now requiring its carriers to pay the government 5.1 U.S. cents for each minute of international incoming calls, without providing any information regarding why the payment is necessary or indicating the use of the collected funds. Additionally, it has instructed its two carriers TCC and Digicel to negotiate rates in accordance with "prevailing market conditions." At least in the case of TCC, this instruction could be inconsistent with Tonga's GATS commitments on basic telecommunications including the WTO Reference Paper, which contains a commitment to ensure cost-based interconnection with major suppliers. It is also important to note that TCC is the sole fixed-line operator in Tonga, and that only one other company provides mobile services.

USTR has tried to engage with the government of Tonga to address these issues, but Tonga has not moved forward in finding a solution to this issue. At present, U.S. carriers are still unable to negotiate an interconnection agreement with the carriers in Tonga and are forced to send traffic through third countries, which further increases their costs. Although Tonga is a small destination in terms of total U.S. traffic, its policies raise concern about its compliance with its obligations under the Reference Paper, and also serve as a dangerous precedent that other countries could follow.

Indeed, in the last two 1377 Reviews, we have been following the emergence of a troubling trend whereby some foreign operators are increasing termination rates due to measures implemented by their governments. These actions are adversely affecting the ability of U.S. telecommunications operators to provide low-cost, quality services to U.S. consumers and may raise questions regarding those governments' international trade obligations. In some cases, the major supplier benefits from the increased rates; in others, the governments in question use the revenues to fund universal service programs or programs unrelated to telecommunications, or do not account for use of the funds adequately if at all. Even where these measures do not provide additional revenue to the local operators, the result for U.S. operators and consumers is the same—higher costs and, consequently, for both the United States and foreign country, lower calling volumes. When Tonga first moved to implement the US$ 0.30/minute rate, it appeared that TCC and Digicel would be the main beneficiaries. Now the government of Tonga is seeking to retain a portion of the increase, and at the same time allow its carriers to increase the rates without any cost justification.

USTR urges the government of Tonga to ensure that its major supplier negotiates cost-based rates for the termination of international traffic. USTR will continue to seek to engage Tonga in meaningful dialogue with the objective of reconnecting the international circuits in the short term. Depending on the results of these efforts, USTR will consider taking additional action.

Ghana - Termination Rate Increase

Similar to the case of Tonga, in late 2009, Ghana mandated an increase in the termination rate for incoming international calls. Act 786 of 2009 requires all telecommunications operators to charge a US$ 0.19/minute rate to terminate incoming international calls, with 32% (US$ 0.06) of that rate to be collected by the telecommunications regulatory authority and deposited into the government's main bank account. The government of Ghana has indicated several reasons for the rate increase including: the opportunity for increased revenues in Ghana, the stabilization of international rates to Ghana, the provision of universal access/service, and the financing of modern monitoring equipment.

The mandated increase is problematic for several reasons. First, the fee does not appear to be related to the costs associated with terminating calls. Ghana's commitments under the WTO Reference Paper require it to ensure that its major suppliers provide cost-based interconnection and information indicates that the US$0.19/minute rate is not based on a cost analysis. FCC data (2008) suggests that U.S. carriers were paying an average of 10 cents/minute for calls to Ghana, which would be attributed to a somewhat lower rate for termination on fixed networks (for example, approximately US$ 0.07/minute) and somewhat higher rates for termination on mobile networks (for example, approximately US$ 0.14/minute). Increasing the rate arbitrarily to US$ 0.19/minute sharply increases costs for U.S. operators, which will lead to increased rates for U.S. consumers and a likely reduction in the amount of traffic sent to Ghana. Ghanaian government officials have noted that this rate is within the FCC's "benchmark" rate for low income countries. However, the fact that a rate is within the "benchmark" rate is not determinative of whether the rate is cost-based. Indeed, the FCC recognized in its order establishing benchmark rates that, "benchmark settlement rates will continue to exceed, usually substantially, any reasonable estimate of the level of foreign carriers' relevant costs of providing international termination service."1 Furthermore, in a subsequent order, the FCC noted that "establishing rate floors, even if below benchmarks, that are above previously negotiated rates" would serve as indicia of potential anticompetitive conduct.2 In any event, the existence of the FCC's benchmark ruling is unrelated to the Reference Paper commitments to ensure that major suppliers charge cost-based rates.

Second, it will be difficult to verify whether the portion of the fee that will be given to the government of Ghana (through its National Communications Authority) actually goes to covering the costs of universal service, since the money is to be deposited into the government's consolidated fund. The Reference Paper requires that any obligations regarding universal services be administered in a transparent, non-discriminatory and competitively neutral manner and that they not be more burdensome than necessary for the kind of universal service defined by the Member. The government of Ghana has not provided sufficient information about the manner in which part of the increased fees will be used directly for universal service. This raises questions about compliance with its Reference Paper commitments in this regard.

Finally, we do not agree with Ghana's assertion that illegal (or "grey") traffic is responsible for any decrease in international termination revenues into Ghana. As has been seen in most countries around the world, competition tends to reduce inbound termination rates toward more cost-based levels, but at the same time stimulates the volume of inbound and outbound traffic, to the benefit of consumers and operators in both countries. In 1997, the year before Ghana adopted its WTO basic telecom commitments, U.S. carriers paid carriers in Ghana an average per minute termination rate of $ 0.39/minute resulting in 50,269,789 minutes of U.S. – Ghana calling and total payments to carriers in Ghana of US$ 19,638,574.[3] In 2008, ten years after Ghana's WTO commitments became effective, U.S. carriers paid carriers in Ghana an average per minute termination rate of US$0.10/minute, resulting in 346,672,164 minutes of U.S. – Ghana calling and total payments to carriers in Ghana of $ 36,248,834.[4] Therefore, downward competitive pressure on rates led to reductions in termination rates,

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[1] *See*, *e.g.*, *In the Matter of International Settlement Rates*, IB Docket No. 96-261, Report and Order, FCC 97-280, 12 FCC Rcd 19806, 19816 ¶ 19 (1997) (*Benchmarks Order*); Report and Order on Reconsideration and Order Lifting Stay, 14 FCC Rcd 9256 (1999) (*Benchmarks Reconsideration Order*); *aff'd sub nom. Cable & Wireless P.L.C. v. FCC*, 166 F.3d 1224 (D.C. Cir. 1999).

[2] *See International Settlements Policy Reform; International Settlement Rates*, IB Docket Nos. 02-324, 96-261, First Report and Order, FCC 04-53, 19 FCC Rcd 5709, 5730, ¶ 44 (2004) (*2004 ISP Reform Order*)

[3] *See* FCC International Traffic Report for 1997, Table A1 at http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/Intl/4361-97.pdf

[4] *See* FCC International Traffic Report for 2008, Table A1, at http://www.fcc.gov/ib/sand/mniab/traffic/files08/CREPOR08.PDF.

ushering in tremendous increases in both amounts of traffic and amounts of money paid by U.S. carriers to carriers in Ghana. The government of Ghana's argument that the new mandated rate is necessary to combat illegal traffic is simply not supported by the latest available traffic statistics from the FCC. Moreover, it is difficult to see how increasing the termination rate sharply would do anything to combat illegal bypass; rather, it would only tend to encourage it. Increasing the termination rate for all carriers by government order simply operates to squelch legal and beneficial price competition.

The U.S. strongly encourages Ghana to remove the mandated US$ 0.19/minute termination rate to ensure that rates below that it does not discourage the establishment of cost-oriented rates that are consistent with Ghana's WTO Reference Paper commitments.

Jamaica - Universal Service Surcharge

Since 2005, Jamaica has been levying a surcharge on the termination rate paid by international operators to send international telephone calls to Jamaica (a US$.02/minute and US$.03/minute surcharge for calls terminating on fixed and mobile networks, respectively). Jamaica explains that the purpose of the surcharge is to fund its universal service program administered by the Universal Access Fund Company (UAFC). This fund seeks to provide funding for domestic operators to provide telecommunications services to underserved areas that are not commercially viable. USTR has expressed concerns about this surcharge in several past years' Reviews, placing particular focus on the lack of details regarding how the funds collected had been used. The government of Jamaica has stated that between June 1, 2005 and December 31, 2010, the amount collected through this surcharge has totaled J$7.5 billion, which is roughly equivalent to US$88 million dollars[5]. The audits that have been completed for the UAFC for the years 2005-2010 are not yet all publicly available.

USTR supports efforts to ensure universal telecommunications service; however, levying a surcharge solely on international calls places an unfair burden on foreign operators and consumers, both of whom are at best only marginally able to benefit from the domestic universal service program through expanded network capacity in Jamaica. U.S. operators and consumers have born the bulk of the expense, given that 80 percent of Jamaica's incoming calls originate in the United States.

[5] http://www.xe.com/ucc/convert/?Amount=7500000000&From=JMD&To=USD

Jamaica's WTO Reference Paper obligations require it to ensure that universal service obligations are administered in a transparent, non-discriminatory manner, and that they be no more burdensome than necessary to achieve its universal service goals. Jamaica's Universal Access Fund continues to grow and the Jamaican government appears to be using the fund's reserves largely, or at least disproportionately, for items not specifically related to expanding broadband network capacity. The surcharge instituted in 2005 is scheduled to expire on May 31, 2011. That date is quickly approaching, and although Jamaican authorities indicate that a review is underway to determine whether or not to renew the fee, they have signaled that renewal is likely, at least until their new Information and Communications Technology (ICT) Policy is in place. Jamaica indicates that the draft ICT Policy is currently undergoing public consultation and includes a plan to develop a universal service fee that has a broader collection base; however the draft reviewed by the United States appears ambiguous as to the actual collection of funds. Additionally, the timeline on adopting the policy is not clear, and could potentially take years, during which time U.S. carriers and consumers would continue to bear the burden of a program from which they can neither benefit from nor shape.

Jamaican authorities have recently said that it is incorrect to depict their universal access fund as being fully funded by foreigners, because a higher rate of general sales tax is levied on Jamaican telecommunications services than on other types of services, and some of this money is also used for universal service purposes. However, this argument has not been previously advanced by the government of Jamaica, and it does not appear that the revenues raised through the sales tax are allocated to any specific fund in the way that the international telephone call surcharge is, so there does not appear to be any way to determine how much of the domestic sales tax revenue is actually being used for universal service. Absent concrete information about how the sales tax revenue is collected and allocated for universal service, USTR must continue to conclude that U.S. operators and consumers are primarily bearing the burden for universal service in Jamaica and will continue to do so for some indefinite time, at least until the new ICT policy is in place.

USTR strongly urges Jamaica to allow the surcharge to expire as scheduled at the end of May 2011, and to utilize the funds already collected in the interim while it works to implement a more broad-based approach to universal service through its planned ICT Policy. USTR will continue to engage with Jamaica on this issue, and will review the UAF audits once they are all made publicly available. Depending on the outcome of those engagements, USTR may consider additional action.

Concerns Regarding On-Net/Off-Net Mobile Termination Rates

As commenters have noted in past years, and one commenter again noted in this review, certain mobile operators are increasingly using a strategy of pricing the retail rates for calls their customers make to competing mobile networks ("off-net calls") significantly higher than what they charge for calls to users of their own networks ("on-net" calls). Although operators may have legitimate cost advantages in pricing on-net calls (for example, they do not have to pay another operator mobile termination rates), charging significantly higher for off-net calls as a way to discourage such calling and hinder the ability of customers of other networks to receive calls can distort the market and hinder competition.

As the U.S. government noted in a recent submission[1], "High mobile termination rates in combination with deep on-net/off-net price differentiation (i.e., charging higher retail prices for off-net calls than for on-net calls) leads to increased network effects (i.e., club effects) which may reduce competition in the long-term." Last year a commenter raised this issue with respect to New Zealand and that country's regulatory authority took steps to address the issue. This year, a commenter notes similar issues in both Mexico and Chile. In Chile, the issue is being investigated by the Competition Commission. It is unclear whether Mexican authorities will be able to address this issue, as operators have so far mounted legal challenges to all attempts to regulate pricing of mobile services.

PROBLEMS RELATING TO ACCESS TO MAJOR SUPPLIER NETWORKS

Chile – Mobile Infrastructure Proposal

One commenter described the potential negative impact of a law now under consideration by Chile's Congress to regulate the construction of new antennae for commercial mobile operators. The bill originally sought to reduce the impact to the community of new tower construction by including an obligation to require existing operators to share their infrastructure with new entrants. With incumbent operators now resisting any sharing obligation, the extensive rights afforded to local communities (any resident in a radius of 1.5 times the height of an antennae would have veto power over any construction) could seriously hinder the ability of new entrants to build out their own infrastructure, as they are obliged to do under the terms of their licenses. As existing operators already have established antennae infrastructure, and would not be subject to the proposed new law for such infrastructure, it is essential that the law either include sharing obligations, or a more expedient process for addressing community

[1] CITEL March 15 2011 Submission, "Background Document on Mobile termination Rates"

concerns. This will help to avoid seriously diminishing competitive opportunities by potentially locking out new entrants or by seriously slowing their ability to install the towers they need to supply their services.

USTR has been in communication with Chile's regulatory authority, which is fully cognizant of the problem and working with the legislature to ensure that the final version of the law does not unduly hinder competitive opportunities for new entrants. USTR will continue to closely monitor this issue.

<u>Germany – Access to IP Multicast Product Offering</u>

Competitive carriers continue to claim that there are market access barriers in Germany because of restrictions on access to incumbent operator Deutsche Telekom AG (DTAG)'s network. In last year's Review, commenters claimed that competitive carriers needed access to IP-Multicast, a wholesale service optimized for video distribution that would enable them to provide Internet Protocol television (IPTV) in order to compete with DTAG's IPTV service. At that time, DTAG indicated that it did not have a standard multicast platform that it could offer to competitors. Commenters claim that the situation has now changed, that DTAG now has a subscriber base of more than 1 million subscribers, and that it should therefore be required to provide a standard offer for this service. Germany's telecom regulator BNetzA is currently reviewing the adequacy of the reference interconnection offer DTAG submitted for approval last fall, and is slated to make a decision shortly, following a public comment period. BNetzA could determine that there is sufficient commercial demand to meet the "reasonable request" standard that would require BNetzA to mandate that DTAG include this wholesale product in its reference interconnection offer. However, if this does not happen, the German government indicates that companies are also able to request a "direct access order" from the BNetzA, but that no such request has yet been made. USTR will continue to follow-up on this issue, closing monitoring any specific cases involving U.S. companies interested in accessing this product.

<u>India – Access to Submarine Cable Systems</u>

Commenters in this year's Review again cite problems in obtaining competitive access, in a timely fashion, to the cable landing stations (CLS) located in India. In past Reviews, the United State has urged the Telecommunications Regulatory Agency of India (TRAI) to conduct a public consultation to determine if there are deficiencies in the Reference Interconnection Offers (RIOs) submitted by the companies that control access to the CLS. Unfortunately, TRAI does not appear to have taken an action in this regard.

A new aspect raised by the commenters this year relates to the timing of the presentation by the CLS operator of its RIO for approval to TRAI. Commenters note that it is important for CLS operators that are installing new submarine cable facilities to present a RIO to TRAI in advance, in order to ensure that the RIO is reviewed and approved prior to commencement of operations at the CLS. Presenting a RIO for approval well in advance of opening the CLS will ensure that there is a level playing field for both the CLS owner and for those carriers seeking access to the CLS facilities.

USTR will seek to discuss this issue again with India, and encourage a public consultation procedure that will help to ensure competitive access to submarine cables – India's goal when it decided to mandate non-discriminatory and reasonable access to these network facilities several years ago.

Mexico – Restrictions on Competitive Access to Incumbent Networks

In previous 1377 Reviews, USTR has expressed concerns regarding competitive access to the networks of Mexico's incumbent telecommunications fixed line operator Telmex and its mobile line affiliate Telcel. For the first time, Telmex and Telcel participated in the 1377 process through comments submitted by parent company America Móvil, as well as through meetings with USTR. America Móvil asserts that there is robust competition among fixed-line providers given the entrance of Mexican cable companies that offer a "triple play" service of voice, broadband internet and television services, and that Telmex has lost market share due to regulatory barriers that prohibit the company from distributing television through its infrastructure. It also asserts that both Telmex and Telcel are subject to onerous requirements not imposed on other carriers, such as price caps on retail rates, universal service obligations and geographic rate averaging requirements.

This year USTR received multiple filings that highlight issues related to competitive carriers' access to the Telmex and/or Telcel networks including: difficulty in obtaining local interconnection and long-distance termination into certain rural areas of Mexico; retaliatory actions taken by Telmex in a yet-to-be resolved dispute regarding interconnection rates; and a claim that Telcel's mobile termination rates are significantly above cost. Mexico has adopted the Reference Paper on Pro-Competitive Regulatory Principles in its GATS commitments and has obligations to ensure that its major suppliers provide interconnection at any technically feasible point of its network at cost-based rates, and to maintain appropriate measures to prevent its major suppliers from engaging in anti-competitive practices. The ability of U.S. affiliated Mexican carriers to obtain non-discriminatory, cost-based access to the networks of Telmex and Telcel is of increased importance given that Mexico is the number one destination for calls from the United States (according to the latest available FCC data (2008)). In 2008, U.S. consumers sent 11.75 billion minutes to Mexico, compared – for example – to 9.3 billion minutes sent to all of Western Europe. Therefore, increased access costs have a significant indirect impact on the prices paid by U.S. consumers to call Mexico.

Both Telmex and Telcel have been cited in numerous sanction cases currently under review by the Secretariat for Communications and Transportation (SCT) in Mexico, related to the issues mentioned above. The sanction recommendations have been submitted by Mexico's telecommunications regulatory agency, the Federal Telecommunications Commission (COFETEL), and are currently in different stages of review by the SCT. Hopefully some will be resolved in the near term and may help to alleviate some of the problems mentioned by commenters this year. However, the structure of the Mexican legal system, which allows for extensive opportunities to challenge government rulings, may be an impediment to progress in these areas. This is particularly true with respect to rulings resulting from COFETEL intervention in interconnection disputes, as further discussed below.

Interconnection in Non Equal Access (NEA) areas

Although Mexico formally opened its entire country up to local and long-distance competition more than a decade ago, Telmex appears to have succeeded in maintaining a de facto monopoly on the provision of telecommunications service outside of major urban areas. Mexican regulatory authorities deem certain areas as "non-equal access" areas, meaning that subscribers in those regions could not choose a competitive long-distance provider ("presubscription") – they were required to use Telmex. These areas, encompassing approximately half the calling areas in Mexico, but only about 11 percent of the fixed lines in Mexico, are mainly rural areas; nonetheless, U.S. operators report that up to 25 percent of calls from the United States terminate in such regions, underscoring the importance to U.S. operators and consumers.

In addition to the absence of pre-subscription for outgoing calls in those areas, Telmex also declined to offer cost-based termination for incoming calls from other regions (including the United States). Thus, not only do subscribers in such regions not have a choice of competitive long-distance operators, but callers from other regions using a competitive carrier cannot benefit from the ability of a competitive carrier to terminate calls into these regions at cost-oriented rates. Telmex would terminate such calls, but would only offer a 25 percent discount off its large-volume retail rate – resale or "reventa" rate more than six times greater than the regulated long-distance interconnection rate in the rest of Mexico. The resale rate into non equal access areas is almost US$ 0.07/minute, compared with the regulated long-distance interconnection rate of a little more than US$ 0.01/minute in the rest of Mexico.

Telmex asserts that it is neither obligated to offer price-regulated interconnection in such regions, nor is it technically able to do so, because it does not maintain any switches that are necessary for interconnection in such areas (an assertion that competitors contest and something that requires further investigation). Even if switching were not available in such regions, but only in an adjacent locality, that condition would not appear to obviate the obligation to offer interconnection at the technically feasible point, at cost-oriented rates consistent with both Mexican law and WTO commitments. As Mexico's telecommunications regulatory authority has established a nationally applicable termination rate, based on its own cost study, it is unclear why Telmex should not be offering that rate for NEA interconnection, even if the physical interconnection occurs outside the region. Presumably, Telmex's choice of not installing switches in such regions (if indeed this is the case) was based on commercial considerations, but its choice of foregoing investment ought not to be a justification for imposing an even higher rate on competitive carriers.

At least one U.S.-affiliated operator has sought to establish its own presence in an NEA region to provide local service. Telmex has not appeared willing to negotiate an interconnection agreement in such regions; and has refused to supply leased lines the company ordered to reach locations in such regions. Although Telmex has cited an unrelated commercial dispute as the basis for not providing the leased lines (a service covered under Mexico's commitments relating to the GATS Telecommunications Annex), it is unclear why this would be relevant, as leased lines are typically purchased in advance, subject to tariffed rates.

In last year's 1377 report, USTR noted efforts of the regulator to narrow the scope of this de facto non-competitive region by consolidating calling areas and absorbing some non-equal access regions into larger competitive regions. Telmex appealed COFETEL's ruling, and the consolidation has not been completed. America Móvil asserts that Telmex has onerous requirements to provide coverage to high-cost rural areas and that it is actually losing money in the non-equal access areas when charging the reventa rate, since it does not receive universal service funding that would help to offset that cost. While establishment of such a universal service fund may be justified, high costs in particular regions do not justify an unregulated cross-subsidy obtained through interconnection, since this type of cross-subsidy has the effect of diminishing competition (e.g., as Telmex does not charge itself the reventa rate, it can (and reportedly does) underprice any competing supplier seeking to terminate calls into such regions.)

Concerns regarding high interconnection costs in Mexico are pervasive. On March 3rd of this year, 25 Mexican companies (including two with U.S. ownership) and trade associations bought full page advertisements in five Mexican newspapers of national circulation urging the Mexican government to institute procompetitive regulation in interconnection, to create a level playing field to compete against Telmex and Telcel. Telmex also announced that it intended to create a separate legal entity named Telmex Social that would cover some 46 percent of Mexico's geographic area, to separate the high cost areas from the areas where more competition exists, in an effort to clearly show that it is spending more in rural areas that no competitive carriers wish to serve. Given that Telmex claims it has no switches in these regions, it is unclear what services such an entity could provide.

Retaliation by Telmex

One U.S. trade association has submitted information for this year's Review that suggests that Telmex has retaliated against a U.S. affiliated Mexican operator who sought a lower interconnection rate in equal access areas, based on a most-favored-nation clause in its interconnection agreement with Telmex. The issue has been in the Mexican courts for some time, with the U.S. affiliated carrier winning an initial decision and Telmex winning a decision on appeal but now under a judicial stay (amparo) while the case goes to final appellate review. Although the case has not yet been definitely resolved by a court, Telmex has inserted a recording into the calls that originate from that carrier's network and terminate on the Telmex network. In the recordings, Telmex informs consumers that the competitive carrier it is using is not paying the correct interconnection rate and could subsequently be subject to disconnection by Telmex. Telmex has claimed that inserting the recordings into the calls is not an anti-competitive move, since the recording does not mention Telmex, nor does it try to steer the customer towards the purchase of a Telmex service.

The use of the competitive carriers' customer information for these purposes raises concerns about Mexico's compliance with the WTO Reference Paper, which defines using information obtained from competitors with anti-competitive results as a prohibited anti-competitive practice. The fact that the recording does not specifically suggest that customers should switch to the Telmex network does not reduce the damage that such a recording has to the business of the competitive carrier. The potential to destroy the business of any disfavored competitor and thereby reduce competition in the market can be viewed as an anti-competitive practice depending on the extent of the anti-competitive results. COFETEL has submitted a sanction recommendation to the SCT for this particular case, and is still awaiting resolution by the SCT.

Mobile Termination Rates

A U.S. affiliated mobile carrier has submitted comments in this year's proceeding claiming that Telcel's mobile termination rates (MTR) are significantly above cost and are not in line with recent decisions by COFETEL that have established rates that are lower than those reached through commercial negotiation. In October 2010, COFETEL, using a long run incremental cost (LRIC) model, ruled that the MTR should be .42 Mexican pesos (approximately US$.04). In December 2010, Telcel, Telmex and Telefonica (the three largest mobile carriers) agreed to establish a much higher MTR amongst themselves that would gradually be reduced from .95 Mexican pesos (approximately US$.10) in 2011 to .69 Mexican pesos (approximately US$.07) in 2014. In a filing to USTR, America Movil stated that establishing a rate of .40 Mexican pesos (as was suggested by the U.S. affiliated mobile carrier) would make Mexico a "low-end" outlier among calling-party-pays countries, making their rates lower than nearly all companies in Europe. However, in February 2011, 6 Mexico's Federal Competition Commission stated that the mobile rates applied in Mexico are 43.5% higher than the average that are applied in the OECD countries that have the calling-party-pays system (as is the case in Mexico).

At the writing of this report, developments surrounding COFETEL's ability to establish interconnection rates in the event of a dispute continued to unfold. On March 16, COFETEL - in resolving an interconnection dispute between Telcel and a Mexican fixed operator – set an MTR of .39 Mexican pesos (approximately US$.04) for 2011, a rate much lower than those established by incumbent operators through commercial negotiation. Telcel announced that it will challenge COFETEL's decision in court. COFEMER (Mexico's regulatory improvement agency – Comision Federal de Mejora Regulatoria) also approved COFETEL's cost model for interconnection, which COFETEL intends to use to settle disputes between operators that occur in 2012 and beyond. COFETEL plans to publish the cost model in the Mexican Federal Registry by the end of March 2011.

COFETEL's attempts at intervening in interconnection disputes are invariably met with multiple legal challenges launched by telecommunications operators. The operators typically seek an amparo – a constitutional action that opposes certain acts or laws because the claimant considers them unconstitutional. Although an amparo does not always lead to a suspension of the acts or laws, in the telecom sector, it is common that COFETEL's actions are suspended while the amparo is under review, something that can take years. If a company ultimately prevails under the amparo, the particular act or

[6] *See* Comision Federal de Competencia – Oficio PRES-10-096-2011-033, page 7.

law in question does not apply to that specific company. USTR understands that Mexico's Supreme Court will shortly review whether or not interconnection issues should be subject to amparos that suspend COFETEL's regulatory actions. According to news reports,7 the Mexican Supreme Court will consider two lower court rulings - one that issued a stay because the dispute was between private parties and another that declined to issue a stay because the modification of interconnection rates has an impact on consumers, which made it an issue of public interest. The outcome of this Supreme Court proceeding will be very important for the future of Mexico's competitive landscape in the telecommunications sector.

Mexican regulatory authorities are currently investigating all issues noted above. USTR supports these efforts, and will keep in close touch with Mexico's regulators, given our interest seeing these longstanding problems resolved. Although Telmex has historically aggressively defended its interests through the Mexican court system, it may have an interest in finding a more expedient resolution given that it seeks to enter the market for video services, but may be prohibited from doing so if certain interconnection disputes remain unresolved.[8] Given the U.S. interests involved, USTR looks forward to seeing those disputes resolved expeditiously as well; and if unsuccessful, will consider further trade options.

ISSUES RELATING TO LICENSING, TRANSPARENCY AND REGULATORY REQUIREMENTS

China – Classification of Value-Added Services

Commenters again noted this year that China's failure to authorize certain value added services in its domestic licensing regime seriously undermines market access opportunities in that market and devalues the commitments China made upon accession to the WTO in 2001. In particular, China's telecommunications regulator has declined to reverse a 2002 decision that classified a corporate data service called IP-VPN as a value-added service, thereby relegating this commercially important service into a licensing category (basic service) with lower foreign equity rights, fewer opportunities to find Chinese partners, and significantly higher capitalization requirements. The United States has raised this issue with China's telecommunications regulator repeatedly and will continue to do so, with the goal of encouraging China to follow

[7] *See http://www.radioformula.com.mx/notas.asp?Idn=164412*

[8] Telmex has challenged COFETEL's "Fundamental Technical Plan for Interconnection and Interoperability" claiming that neither COFETEL nor the SCT has jurisdiction to impose the interconnection obligations. Telmex's refusal to adhere to COFETEL's interconnection plan is what is currently preventing Telmex from distributing video.

norms established in other markets open to competition and market entry by suppliers of other WTO members.

Costa Rica – Licensing of Internet Services
One commenter complains that it has been attempting to obtain a license to provide Internet services via satellite in Costa Rica for nearly two years, and has encountered serious delays in obtaining the required authorization from the Costa Rica regulatory authorities. Under its CAFTA-DR commitments, Costa Rica committed to issuing licenses for Internet services.

Costa Rica's telecommunications regulator, the Superintendencia de Telecomunicacines (SUTEL) has indicated that there are a number of technical issues that need to be resolved in order to grant an authorization to this U.S. company and to others that have applied for the right to supply Internet via satellite in Costa Rica. These technical issues include those related to spectrum fees, international coordination of the satellite to be utilized, and changes needed to Costa Rica's table of frequency allocation. While it may take some time to work through these technical issues, Costa Rica has said that it is considering implementing a transitory framework that will allow the company to obtain a license and begin operations pending the finalization of the technical details.

Given that the commenter's license application has been pending for more than two years, USTR believes Costa Rica must act expeditiously to grant authorization (including, if necessary, a temporary authorization) to the company while SUTEL and the telecommunications ministry (MINAET) seek to resolve any outstanding issues regarding Internet services provided via satellite.

Costa Rica – Auctioning of Mobile Spectrum
In last year's Review, USTR urged Costa Rica to resolve the microwave frequency issue that was causing a delay in the mobile telephony frequency auction, in order to fulfill its CAFTA-DR commitment to introduce much needed competition into the mobile telephony market. In September of 2010, Costa Rica finally moved forward with its auction, and announced that two companies (Mexico's America Mobile and Spain's Telefónica) had won spectrum to begin to compete with incumbent operator ICE. The government's ability to move forward was related to the implementation of a regime to ensure that operators could share certain microwave links that are needed to connect base stations to towers throughout the country. Although this regime was implemented in a manner that allowed the spectrum auctions to move forward, USTR understands that legal challenges have been lodged against the microwave ruling but expects that Costa Rica will ensure that its CAFTA-DR commitment to liberalize its mobile telephony market is realized.

China and India – Requirement to Sell Satellite Capacity Through Government-owned Intermediaries

As in previous years, commenters in this year's Review note problems regarding U.S. operators' ability to offer satellite capacity to customers in China and India. Commenters continue to point to a lack of transparency in the rules governing the provision of satellite capacity in these countries and note that the requirement to sell capacity only through government-owned satellite operators is problematic.

In the case of China, only one company – China DBSAT – holds the license necessary to sell domestic satellite services and foreign satellite operators must therefore sell capacity to end users through that company. Two companies in Hong Kong are allowed to sell capacity directly to end-users in China, but both companies are partially owned by Chinese government entities.

In the case of India, foreign operators are precluded from participating directly in the provision of satellite capacity for the lucrative direct-to-home (DTH) market. Foreign operators are required to first sell the DTH capacity to India's domestic satellite operator, the Indian Space Research Organization (ISRO), which resells the capacity to the DTH customers and maintains ownership of the customer.

USTR will continue to raise the commenters' concerns regarding the barriers to supplying satellite services in China and India and will encourage these countries to consider changes to their respective frameworks.

VOIP Issues

This year, a trade association representing suppliers of Voice over Internet Protocol services (VoIP) has submitted comments that point to a range of barriers faced around the world in the provision of this service. The barriers cited include regulatory regimes that impose the same requirements on VoIP providers as on traditional fixed or mobile voice providers; allowing incumbent operators to block the ability of companies to provide VoIP services over the incumbent's broadband network; and the inability to provide VoIP services that connect to the public switched network (PSTN).

VoIP offers an important competitive option to traditional phone service, to the benefit of consumers. USTR will continue to evaluate the barriers listed in this year's comments and – as appropriate – will engage with countries to ensure that any measures taken regarding the service are consistent with each country's telecommunications trade commitments.

ISSUES AFFECTING THE TELECOMMUNICATIONS EQUIPMENT TRADE

China - Multi-Level Protection Scheme

In 2010, the United States raised its concerns with China about framework regulations for information security in critical infrastructure known as the Multi-Level Protection Scheme (MLPS), which were first issued in June 2007 by the Ministry of Public Security (MPS) and the Ministry of Industry and Information Technology (MIIT). The MLPS regulation put in place guidelines to categorize information systems according to the extent of damage a breach in the system could pose to social order, public interest and national security. The MLPS regulations also appear to require, by reference, purchasers' compliance with certain information security technical regulations and encryption regulations that are referenced within the MLPS regulations. If implementing rules for the MLPS regulations are issued and applied broadly to commercial sector networks and IT infrastructure, they could have a significant impact on sales by U.S. information security technology providers in China. The United States has therefore urged China to notify any MLPS implementing rules laying down equipment-related requirements in accordance with China's obligations under the Technical Barriers to Trade (TBT) Agreement. In addition, going forward, the United States will continue to urge China to refrain from adopting any measures that mandate information security testing and certification for commercial products.

India – Restrictions on Encryption

India is currently exploring how it will implement the 2008 Amendments to the Information Act of 2000. U.S. companies are concerned that, in trying to meet its national security concerns, India will develop policies to implement the 2008 Amendments that will impose stringent and burdensome encryption requirements, including for equipment sold for solely for commercial use, or even ban the use of certain encryption technologies. Given that India's national security concerns may be shared by many other countries, the United States has encouraged India to actively seek to address those concerns through policies that do not deviate from commonly-accepted or best practices. To date, the United States and U.S. industry have engaged in a constructive dialogue with India focused on best practices for managing security concerns while not unduly restricting industries' ability to utilize encryption technology. USTR will continue to engage India to seek ways to ensure U.S. telecommunication companies can effectively protect information, while also respecting security concerns of the Indian government.

India – License Amendments Affecting Importation of Telecommunications Equipment

India issued a series of new requirements for telecommunications service providers (TSP) and equipment vendors in December 2009, February 2010, March 2010, and July 2010 which were designed to maintain the security of India's commercial networks. The guidelines apply to the purchase of imported products and do not apply to products manufactured in India by Indian-owned or Indian-controlled manufacturers. Issued in the form of amendments to telecommunications service licenses, the new regulations sought to impose an inflexible and unworkable security approval process, which mandated the forced "transfer of technology" to Indian companies, the escrowing of source code and other high-level and detailed designs, and assurances against malware and spyware during the entire use of the equipment.

The United States has emphasized to the GOI that these measures effectively halted billions of dollars worth of trade in telecommunications equipment and were unlikely to advance India's security objectives. Recognizing these concerns, the GOI suspended implementation of several of these conditions while it works to revise the policies in consultation with relevant stakeholders. To date, the United States and U.S. industry have engaged in a constructive dialogue with India focused on best practices for managing security concerns while not unduly restricting trade. The United States has also strongly encouraged the GOI to conduct a broad public consultation, including with respect to draft regulations, to ensure that all relevant issues and concerns are taken into account and that any measures potentially affecting trade be notified through the established processes at the WTO.

USTR will continue to engage India to seek ways to ensure U.S. telecommunication companies can participate in the Indian market, while also respecting security concerns of the Indian government.

General Concerns with Conformity Assessment Requirements

U.S. industry continues to identify conformity assessment procedures relating to information and communications technology (ICT) equipment as a significant barrier to trade, focusing in particular on certain electromagnetic compatibility (EMC) testing and certification requirements. Mandatory certification requirements maintained by China, Costa Rica, India, Mexico, and Brazil (especially for EMC), as well as requirements maintained by China that equipment be tested domestically, are areas of concern. Requirements that telecommunications and information technology equipment be tested domestically can lead to redundant testing, particularly where a product is required to undergo testing to the same standard in both the exporting and importing country (e.g., for EMC).

In the case of China, U.S. industry identifies several specific redundant testing requirements that China imposes with respect to mobile phones, as well as a lack of transparency with respect to the testing and certification procedures China maintains for mobile phones. China's three main approval processes for mobile phones—the Network Access License (NAL), the Radio Type Approval (RTA), and the China Compulsory Certification (CCC) mark—often overlap. For example, the NAL and RTA processes both require electromagnetic interference tests. The NAL and the CCC both require EMC testing and product safety tests. In addition to redundancy, China does not consistently or comprehensively publish its requirements for mobile phones. For example, the requirement that mobile phones be WAPI-enabled, described elsewhere in this report, represents a clear example of an unpublished requirement. Those requirements that are published are often unclear and subject to change without written notification and adequate time for companies to adjust. In some cases, testing requirements for products can change on an almost monthly basis. The United States and China discussed these issues bilaterally in 2010, including working group meetings held under the auspices of the U.S.–China Joint Commission on Commerce and Trade (JCCT). At the JCCT Plenary, China announced it will set up a "one-stop-shopping" mechanism to establish one application for two certification processes for mobile devices. China agreed to initiate exchanges regarding bilateral APECTEL Mutual Recognition Agreement (MRA) negotiations. As of early 2011, China has not yet followed through on those commitments. The United States will continue to pursue these discussions in 2011.

Israel, Chile, and China have indicated a willingness to consider MRAs for ICT and other telecommunications equipment. MRAs could help address restrictions these countries maintain on equipment testing outside their territories, and eventually could lead to these countries permitting equipment sold in their markets to be certified in the United States. USTR will continue to seek timely implementation of such agreements. The United States and Mexico have had extensive discussions regarding implementation of a bilateral MRA. Towards that goal they have set a deadline of May 1, 2011 to finalize the text of an agreement.

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