MEXICO – MEASURES AFFECTING TELECOMMUNICATIONS SERVICES

(WT/DS204)

ORAL STATEMENT OF THE UNITED STATES
AT THE SECOND MEETING OF THE PANEL

March 12, 2003

1. Thank you, Mr. Chairman and Members of the Panel. We are pleased to be here again to present the views of the United States in this dispute and respond to the arguments recently made by Mexico in its Second Written Submission and Answers to the Panel's Questions.

2. Most of Mexico's arguments have not changed from the First Meeting of the Panel and its First Written Submission. Indeed, Mexico's Second Written Submission and Answers to Questions are more significant for what they do not argue. Although Mexico repeatedly attempts to make it appear as though the Mexican market is competitive, no effort is made to dispute the Mexican government's own findings of Telmex's market power or the fact that its ILD rules explicitly *prevent* competition in the termination of international calls.

3. Likewise, no effort is made to introduce evidence of the costs of providing international interconnection in Mexico; instead, Mexico cites the FCC and ITU benchmarks, which do not purport to represent cost-oriented rates, and continues to argue for an interpretation of *basadas en costos* that is so broad it would end up meaning nothing. Mexico seems to believe that its status as a developing country justifies any interconnection rate charged by its major supplier. Mexico repeatedly asserts that its need for infrastructure development and its goal of promoting universal access vindicate Telmex's rates. However, even if those were appropriate considerations (which they are not) in determining whether an interconnection rate is consistent with the obligations in Section 2 of the Reference Paper, Mexico has offered no evidence (just unsubstantiated assertions), of any connection or correlation between telecommunications infrastructure development in Mexico and the specific level of Telmex's international interconnection rates.

4. Finally, although not strictly relevant to the claims in this dispute, Mexico continues to misrepresent the U.S. international telecommunications regulatory system and the authority given to U.S. carriers such as WorldCom.

5. Before turning to these arguments, I want to start with Mexico's primary defense. In fact, almost all of Mexico's arguments in response to the United States' claims in this dispute hinge on a single question - that is, whether Mexico has undertaken a commitment to allow the

supply of basic telecommunications services on a cross-border and commercial presence basis. According to Mexico's Second Written Submission, not only has it not undertaken a commitment to allow the supply of such services, but the nature of basic telecommunications services actually precludes them from being offered on a cross-border basis. Both of these arguments are flawed and should be rejected by the Panel.

Mexico's Scheduled Commitments

6. I will begin with mode 1 or cross-border. The extent of Mexico's commitment is clear and unambiguous from the language of its commitment. Mexico chose "None," signaling a "full commitment." Mexico then inscribed a single qualification – that international traffic "route[] through the facilities of an enterprise that has a concession . . ." This is precisely how U.S. suppliers complete (and completed, before Mexico's WTO obligations entered into force) calls into Mexico – by "rout[ing] through the facilities of an enterprise that has a concession . . ."

7. Mexico argues that the routing requirement should be interpreted as a requirement that a supplier hold a concession from the SCT to supply basic telecommunications services into Mexico on a cross-border basis, and that this concession requirement is a "zero quota," and therefore covered by Article XVI:2(a), or that it is a limitation on the form of legal entity under Article XVI:2(e).[1]

8. The United States is doubtful that a "concession" requirement constitutes a market access limitation under Articles XVI:2(a) or (e). However, the Panel does not need to answer this question, for one very simple reason – the mode 1 market access column of Mexico's Schedule <u>does not include such a "concession requirement</u>." Mexico's Schedule simply does not require foreign suppliers sending international traffic into Mexico to themselves have a concession. Rather, it only requires that they route that traffic through the facilities of an entity that has a concession.

[1] Mexico Responses to Questions from the Panel, para. 37.

9. This interpretation of Mexico's routing requirement is reinforced by the contrast between Mexico's mode 1 and mode 3 market access limitations. To enjoy market access as a facilities-based operator in mode 3, Mexico's Schedule states that "[a] concession from the SCT is required." This wording shows that Mexico knew how to describe a concession requirement, where it so intended.

10. Not only does Mexico attempt to bootstrap a "concession" requirement into its mode 1 commitment, but it also attempts to further bootstrap this "concession" requirement into a commercial presence requirement. A review of Mexico's responses to the Panel's questions (specifically, questions 2, 5 and 6) reveals that Mexico's only support for this conclusion is the fact that the word "concession" is used in the limitations under both modes 1 and 3. At paragraph 69 of its responses, Mexico states that "[t]he point that the Mode 1 limitation must be read together with the Mode 3 limitation is relevant insofar as the identical word 'concession' is used in both limitations." Conveniently, Mexico ignores *how* the word is used in the two modes.

11. For this same reason, Mexico's assertion that it has done "exactly" what other Members have done in scheduling a commercial presence requirement as a limitation on cross-border market access in sectors outside of telecommunications is wholly inaccurate.[2] I urge the Panel to examine closely each of the examples cited by Mexico in paragraph 60 of its Second Written Submission. In each of those examples, the Member conditioned mode 1 market access on commercial presence by expressly inscribing the term "commercial presence." This is exactly what Portugal did, which is the specific example Mexico used. In stark contrast, the requirement in Mexico's Schedule to route international traffic through the facilities of a concessionaire does not use the term "commercial presence."

12. In another attempt to undermine the ordinary meaning of the terms included in its Schedule, Mexico suggests that the requirement to use the "facilities" of a concessionaire is equivalent to a requirement to route all traffic through international switched "ports" that can be

[2] Mexico Second Written Submission, paras. 60-61; Mexico Responses to Questions from the Panel, para. 36 and footnote 11.

operated only by Mexican concessionaires. At paragraph 102 of its Second Written Submission, Mexico inaccurately quotes the United States as "acknowledg[ing] that it will comply with the requirement to route through the international port of a concessionaire."

13. The United States made no such acknowledgment. Mexico's Schedule says that international traffic must be routed through "*the facilities of*" a concessionaire. As explained in our submissions, "facilities" is a much broader term than "ports," and embraces a variety of means that might be used to terminate cross-border traffic, including private leased circuits.

14. Finally, Mexico argues that even if the limitation included in its Schedule is only a routing requirement and does not require a foreign supplier to be commercially present in Mexico to provide basic telecommunications services on a cross-border basis, U.S. service suppliers cannot benefit from Mexico's market access commitment, since the "service" at issue in this dispute does not actually cross a border. Instead, Mexico asserts that cross-border supply "only occurs when *the same service supplier* transports a call from one country, across the border, and into the territory of another country."[3]

15. The cross-border supply of a service does not require that the service supplier operate on both sides of the border. Article I:2(a) of the GATS defines the cross-border supply of a service as the supply of a service from the territory of one Member into the territory of any other Member. The presence of service suppliers on the other side of the border, in another Member's territory, is explicitly addressed by modes 3 and 4, and not mode 1. Accepting Mexico's argument would mean that the provision of basic telecommunications services on a cross-border basis would only be possible if a service supplier also operated on a commercial presence basis. The result would render meaningless Mexico's and other Members' mode 1 commitments in the basic telecommunications sector.

[3] Mexico Responses to Questions from the Panel, para. 56 (emphasis added).

16. According to Mexico, the service at issue in this dispute and to which it committed to market access for foreign suppliers is not a "telephone call" or a "signal," but is instead "the service of transmission or transport of customer-supplied information."[4] According to Mexico, because U.S. suppliers do not "transmit or transport" customer-supplied information on both the U.S. and the Mexican side of the U.S.-Mexico border, they do not supply the services at issue in this dispute on a cross-border basis, within the meaning of Article I:2(a) of the GATS. Therefore, even if the limitation included in Mexico's Schedule is only a routing requirement, and does not require a foreign supplier to be commercially present in Mexico to provide basic telecommunications services on a cross-border basis, Mexico argues that U.S. service suppliers cannot benefit from Mexico's market access commitment, since the "service" at issue – "transmission or transport of customer-supplied information" – cannot and does not actually cross a border.

17. Mr. Chairman, the Panel should reject this rather bizarre argument, in which Mexico ignores the text of the CPC codes it has inscribed and from which it selectively quotes in its responses to your questions. In reviewing the CPC codes, you will note that the services subject to Mexico's market access commitments are not simply the "transmission or transport of customer-supplied information," as Mexico asserts. Contrary to Mexico's argument, the nature of the service and its cross-border character is not affected by the fact that the Mexican concessionaire assumes responsibility for the traffic at the border. This "hand off" is expressly contemplated in CPC 75212, which provides that the customer has access to both "the suppliers' and *connecting carriers'* entire telephone network." Thus, the CPC code specifically contemplates the "joint provision" of voice services.[5]

18. The CPC codes make clear that the services covered by Mexico's market access commitments include, under CPC 75212, "switching and transmission services necessary to establish and maintain *communications* between local calling areas."[6] Establishing and

[4] *Id.*, paras. 48, 51.
[5] *Id.,*, para. 53.
[6] Emphasis added.

maintaining communications require active coordination between a supplier on each side of the border, and are not two discrete services provided by different companies. For example, in order to complete a call, AT&T's switch must communicate with Telmex's switch, which is located within Mexico, not on the border.

19. Similarly, CPC 75212 states that the scheduled service "provides the *customers* with access to the suppliers' and connecting carrier's entire telephone network."[7] What a "customer" purchases from a U.S. supplier is a "communication" – a telephone call – from its point of origin in the United States to its point of termination in Mexico. In other words, the service includes the entirety of a telephone call.

20. Moreover, CPC 75212 covers "services necessary to establish and maintain communications *between* local calling areas."[8] This includes communications between a local calling area in the United States and a local calling area in Mexico.

21. I would also point out that Mexico's argument regarding the nature of the service is contradicted by Mexico's definition of commercial agencies in its schedule. By Mexico's definition, commercial agencies are agencies that do not own transmission means. Thus, based on Mexico's argument that the service at issue is the transport and termination of customer supplied information, a commercial agency or reseller can supply services on neither a Mode 1 nor Mode 3 basis, because a commercial agency by definition is not itself transmitting the call. If that is the case, Mexico's inscription under Mode 1 and Mode 3 for commercial agencies means nothing. Likewise, it would mean that the inscription for Mode 1 for facilities-based operators is completely superfulous since there is no need to schedule a "standstill" commitment if it is impossible to provide basic telecommunications services on a cross-border basis, as Mexico argues.

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[7] Emphasis added.

[8] Emphasis added. We note that Section 3 of the Annex defines "public telecommunications transport service" to include transmission "between two or more points," which includes between a point in the United States and a point in Mexico. *Cf.* Mexico Responses to Questions from the Panel, para. 43.

22. Mr. Chairman, for all of these reasons, Mexico's argument that it has not made a commitment to accord market access to foreign suppliers operating on a cross-border basis, and its argument that the basic telecommunications service sector and sub-sectors in which it has scheduled commitments cannot and are not provided on a cross-border basis, should be rejected. The obligations included in Mexico's Reference Paper and the Annex therefore apply.

23. Mexico also asserts that its Schedule does not obligate it to issue permits for the establishment and operation of mode 3 commercial agencies.[9] This is quite a different picture than was presented to the U.S. FCC by Telmex's U.S. subsidiary, which in 1997 stated that Mexico's WTO commitments required Mexico "promptly" to adopt the relevant regulations and issue reseller permits.[10]

24. In any event, the issuance of regulations is not a market access limitation listed in Article XVI:2 of the GATS. A Secretariat Explanatory Note states that any limitations to scheduled commitments stemming from laws or regulations should be set out explicitly.[11] With respect to Mexico's Schedule, the general reference to "relevant regulations" is without any legal effect.

25. Mexico states that had it intended to "ma[k]e commitments to take certain actions in the future, those commitments would have been inscribed" as "additional commitments."[12] Mexico asserts that a Secretariat Note "confirms" that commitments to take certain actions in the future are included in the "additional commitments" column.[13] The Secretariat Note says no such thing. Paragraphs 6-8 of the Note describe the types of commitments scheduled by Members in the "additional commitments" column. Nothing in this Note "confirms" Mexico's assertion that commitments to take certain actions in the future had to be, or were only, inscribed in the "additional commitments" column.

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[9] Mexico Responses to Questions from the Panel, paras. 108-110.
[10] U.S. Responses to Questions from the Panel, paras. 32-34.
[11] MTN.GNS/W/164/Add.1, para. 8.
[12] Mexico Responses to Questions from the Panel, para. 109.
[13] S/CSC/W/34 (July 16, 2002).

Section 2 of the Reference Paper

26. I would like to turn now to Mexico's arguments in response to the United States' claim under Section 2.

27. Mexico continues to assert that its Reference Paper applies only to matters relating to domestic regulation, and does not apply to interconnection between a Mexican major supplier and U.S. suppliers of basic telecommunications services on a cross-border basis. Yet, as Mexico acknowledges, Section 2.1 defines "interconnection" broadly to include all "linking" of suppliers for the purpose of enabling users to communicate – whether the suppliers are operating on a cross-border basis or are commercially present. Section 2.1 begins with the phrase "This section applies," indicating that the definition determines the scope of Section 2.

28. Mexico asserts that because Sections 2.1 and 2.2 refer only to "suppliers" rather than "service suppliers of any other Member," Section 2 only applies to suppliers that are providing public telecommunications transport networks and services "in Mexico."[14] Mr. Chairman, if Mexico had meant to limit the applicability of Section 2 to interconnection of "some" suppliers with a major supplier, it would have adopted language to that effect. In the absence of any such limitation, Section 2 applies to interconnection of "all" suppliers with a major supplier. For context, we refer to the definition in Article XXVIII(g) of the GATS, which states that "'service supplier' means any person that supplies a service." There is no limitation on whether the service supplier is domestic or foreign.

29. Second, Mexico argues that the Reference Paper only applies to situations "where a dominant supplier can exert control <u>over its competitors</u>."[15] However, major suppliers do in fact compete with cross-border suppliers in some situations. A major supplier also has an incentive

[14] Mexico Responses to Questions from the Panel,., paras. 131-134. *See also* Mexico Second Written Submission, para. 27.

[15] Mexico Second Written Submission, para. 30 (emphasis in original). *See also* Mexico responses to questions from the Panel, paras. 139-140.

to impose a competitive disadvantage on a foreign cross-border supplier if an affiliate of the major supplier competes with the cross-border supplier.

30. Third, Mexico repeats its argument that Section 2 cannot apply to interconnection between cross-border suppliers and a major supplier, because some of its provisions only apply to interconnection between commercially-present suppliers.[16] We have already observed that although some of the provisions of Section 2 might only apply to interconnection between commercially-present suppliers, other of its provisions apply to interconnection between cross-border suppliers and a major supplier. For example, although Mexico claims that accounting or interconnection rates between cross-border suppliers and a major supplier are "*per se* discriminatory" and thus cannot meet the non-discrimination requirement of Section 2.2(a), the United States has already explained that accounting rates, even if "differential," are not *per se* discriminatory.[17] Additionally, the provisions in Section 2 regarding unbundling and cost-orientation are equally relevant to the interconnection of international traffic as they are to the interconnection of domestic traffic.

31. Contrary to Mexico's assertion, under the United States' interpretation, <u>all</u> provisions of Section 2 are given meaning – none is rendered meaningless. Some provisions apply to interconnection between commercially-present suppliers, some provisions apply to interconnection between cross-border suppliers and a major supplier, and some provisions apply to both. It is Mexico's interpretation that is inconsistent with the rules of interpretation reflected in the *Vienna Convention*, since it ignores the definition of the term "interconnection" included in Section 2.1 of the Reference Paper.

32. Mr. Chairman, we have demonstrated that Section 2 of the Reference Paper applies to interconnection between U.S. cross-border suppliers and Telmex, which is a "major supplier."[18] The obligations in Section 2.2 therefore apply to rates associated with that interconnection.

[16] Mexico Responses to Questions from the Panel, paras. 137-138.
[17] U.S. Response to Question 16(b) from the Panel.
[18] Mexico has provided no evidence whatsoever to rebut the United States showing, in paragraphs 68-99 of its First Written Submission, that Telmex is a major supplier.

33. Although neither Sections 2.1 nor 2.2 contain language restricting themselves to certain kinds of interconnection rates, Mexico maintains that the obligations in Section 2.2 do not apply to "settlement" or "accounting" rates.

34. First, Mexico asserts that continued maintenance of the accounting rate system by Members that scheduled a commitment to observe Section 2.2(b) confirms that the Reference Paper does not apply to the accounting rate regime.[19] However, "accounting rates" are merely a type of interconnection rate. Members that have scheduled the Reference Paper may continue to allow their carriers to charge "accounting rates" to terminate traffic. Those Members must simply ensure that those "accounting rates," when used by major suppliers, are consistent with the requirements of Section 2.2(b). Neither Mexico nor any other Member violates the Reference Paper by continuing to use "accounting rates," or violates the ITU's International Telecommunications Regulation by subjecting "accounting rates" to the obligations in the Reference Paper.

35. Second, Mexico argues that if national carriers in the 55 Members that signed on to the Reference Paper were required to maintain cost-based termination rates, while national carriers in other countries were not required to do so, the result would be "net outflows of payments" that would force carriers subject to the cost-based standard "to choose between bankruptcy and refusing to pay."[20]

36. Mexico's "doomsday" scenario is an invention. Mexico's assertion that Telmex would be forced into bankruptcy if it is forced to observe the "strict 'cost-oriented' standard posed by the United States"[21] is not accurate. The United States has shown that Telmex's current rates substantially exceed the *prices* charged for the very same elements of interconnection furnished domestically. Cutting Telmex's rates for the interconnection of international traffic to the level of prices charged for interconnection furnished domestically would not lead to the "doomsday"

[19] Mexico Responses to Questions from the Panel, paras. 142-145.
[20] *Id.*, paras. 148-152. *See also* Mexico Second Written Submission, para. 34.
[21] Mexico Responses to Questions from the Panel, para. 151.

scenario posed in Mexico's submissions, since under Mexican law these rates already cover costs, including a reasonable rate of return.[22]

37. Moreover, approximately 80 percent of Mexico's international traffic is exchanged with the United States. FCC statistics for the year 2001 show that U.S. carriers made net outflow payments to Mexican carriers of almost $500 million.[23] If Telmex were to charge cost-based interconnection rates to terminate this traffic, given the large imbalance in traffic flows between the U.S. and Mexico, the result will not even approach a situation in which Telmex makes "net outflows of payments."

38. Additionally, Mexico contends that national carriers in countries not subject to the Reference Paper will lower their interconnection rates to cost-based levels in response to "financial pressures" from cost-based rates charged by carriers in the 55 WTO Members who did commit to the Reference Paper.[24] If this is the case, then Mexico need not worry that Telmex will be faced with "net outflows of payments." In fact, the accounting rate regime has already been superceded in large part by ISR or other types of interconnection arrangements among most of the 55 countries Mexico lists.[25]

39. Nonetheless, Mexico asserts that if countries not subject to the Reference Paper are "effectively . . . compelled to bring [themselves] closer into compliance with" the cost-based standard included in Section 2.2(b), "the overall balance of concessions that formed the basis for the agreement" will be upset.[26] Mexico calls this result "absurd." The United States calls it "competition." Price reductions made by private parties in response to competitive pressure are not "compelled."

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[22] *See* United States Responses to Questions from the Panel, para. 77.
[23] FCC 2001 International Telecommunications Data, Table A-1, January 2003.
[24] Mexico Second Written Submission, para. 35.
[25] *See* ITU, Trends in Telecommunications Reform 2000-2001, Section 8.2 (Exhibit MEX-59).
[26] Mexico Responses to Questions from the Panel, para 35.

40. Third, Mexico mistakenly claims support from Australia for its contention that the Reference Paper does not apply to international interconnection.[27] Australia's statement to the Panel in this dispute should be dispositive as to Australia's position on this issue. Australia stated to the Panel that "*the Reference Paper obligations relating to interconnection apply to international interconnection*."[28]

41. Mexico is in any event wrong in speculating that if the Reference Paper applied to accounting rates, Australia "would not have made" the statement in its April 1996 draft offer concerning "the deletion of the principle on accounting rates from the regulatory principles," and that "Australia looks to further negotiations to provide liberalization in this area."[29] The deleted provision on accounting rates to which Australia was referring would have required "*any supplier* of public telecommunications transport networks" to provide for "public review" of its accounting rates with foreign correspondents -- not just the *major suppliers* that are subject to the interconnection requirements of Section 2 of the Reference Paper.[30] Additionally, this separate provision would still have applied to those Members that deleted the requirement of cost-oriented rates and reasonable terms from the versions of the Reference Paper inscribed in their Schedules.

42. Mexico also fails to recognize that Australia sought during the negotiations on basic telecommunications to obtain WTO commitments on accounting rates from many more countries than the limited number that agreed to the Reference Paper. Australia sought the scheduling of termination services by all countries, and tariffication of termination charges by "developing countries in particular," to encourage the adoption of WTO commitments to reduce high accounting rates.[31] Australia's concerns were not fully addressed by the interconnection commitments made under the Reference Paper. Many developing countries with high

[27] Mexico Responses to Questions from the Panel, paras. 154, 155, footnote 60.
[28] Third Party Submission of Australia, para. 8 (emphasis added).
[29] Mexico Responses to Questions from the Panel, paras. 154-155.
[30] Australia made this proposal in 1995. *See* S/NGBT/W/4/Add.1 (April 21, 1995), para. 43 ("operators should be required to publicise termination rates.").
[31] Communication from Australia, *Termination Services and Developing Country Issues*, S/NGBT/W/13 (September 28, 1995), pg. 4.

accounting rates either made no Reference Paper commitments, or committed to modified forms of the Reference Paper that did not include the provision of interconnection at cost-oriented rates and on reasonable terms. Therefore, Australia has continued to press for a broader application of GATS disciplines to accounting rates.

43. Fourth, Mexico asserts that if its interconnection obligations applied to accounting rates, there would be no need for the Understanding included in the Chairman's Note, because there would be no discrimination that would be actionable under Article II of the GATS.[32] As we explained in our previous submissions,[33] most WTO Members made no Reference Paper commitments, and others did not include the "cost-oriented" provision. The Chairman's Note gave those Members some degree of reassurance that at least until January 1, 2000, "the application of such [differential] accounting rates would not give rise to action by Members under dispute settlement under the WTO."[34]

44. Fifth, Mexico argues that its ILD rules in effect at the time of the negotiations distinguish between "settlement rates" and "interconnection," and that those rules should dictate the exclusion of "settlement rates" from the reach of the Reference Paper.[35]

45. Mexico cites to *EC – LAN* as support.[36] While it is true that in *EC – LAN*, the Appellate Body found that a Member's legislation at the time of negotiations can be used as a *supplementary* means of interpretation, Mexico considers that its ILD rules should *override* the definition of "interconnection" used in Section 2.1.

46. Mexico ignores the Appellate Body's cautionary note that "[t]he purpose of treaty interpretation is to establish the *common* intention of the parties to the treaty. To establish this

[32] Mexico Responses to Questions from the Panel, para. 249.
[33] United States Responses to Questions from the Panel, paras. 83-85; Second Written Submission of the United States, para. 51.
[34] Report on the Group on Basic Telecommunications ("Chairman's Note"), S/GBT/4, paragraph 7.
[35] Mexico Responses to Questions from the Panel,, paras. 156-159.
[36] *European Communities – Customs Classification of Certain Computer Equipment*, WT/DS62/AB/R, WT/DS67/AB/R, WT/DS68/AB/R (adopted 22 June 1998).

intention, the prior practice of only *one* of the parties may be relevant, but it is clearly of more limited value than the practice of all parties."[37] According to the Appellate Body, if the prior practice of a party is not consistent, it is not relevant at all as a supplementary means of interpretation.[38] While Mexico focuses on one particular provision of Mexican law which it contends distinguishes between "interconnection" and "settlement rates," the United States has demonstrated that elsewhere in Mexican law, the linking of foreign service suppliers to Mexican international port operators is referred to as "interconnection," and that throughout its laws and regulations, Mexico uses the term "interconnection agreement" to describe agreements with foreign operators.

47. Mexico compares the terms of a so-called "accounting rate agreement" between Telmex and SBC, a U.S. carrier, with the terms of a "standard domestic interconnection agreement" between U.S. local exchange carriers.[39] However, the term "accounting rate" is not used in any of the agreements cited by Mexico, including the Telmex-SBC agreement. Instead, page 1 of the Telmex-SBC agreement says "INTERCONNECTION AGREEMENT."

48. Mexico notes differences between the Telmex-SBC agreement and a U.S. local exchange carrier agreement. As we explained in our response to Question 8, these differences are not surprising in light of the different services provided and the different regulatory processes applicable to the two types of agreements. As long as the agreement deals with "linking with suppliers" to "allow the users of one supplier to communicate with users of another supplier," it deals with "interconnection."

49. Let me turn now to Mexico's response to the United States' demonstration that Telmex's international interconnection rates are inconsistent with Section 2 of Mexico's Reference Paper.

[37] *EC – LAN*, para. 93.
[38] Id., para. 95.
[39] Second Written Submission of Mexico, paras. 166-168.

50. I repeat that we are <u>not</u> asking the Panel to determine what rate would be *basadas en costos*. We are instead asking the Panel to determine that the rates currently charged by Telmex are not *basadas en costos*, in part because they substantially exceed the prices charged for the same elements domestically. Those prices were set out by the United States at paragraphs 121-140 of our First Written Submission and under Mexican law must recover at least the total cost of all network elements.[40] Since Mexico has made no attempt to show that there are additional costs associated with international interconnection, rates for cross-border suppliers that exceed prices for the same elements provided to commercially-present suppliers are therefore not based in cost.

51. Mexico does not contest the factual evidence we have presented to the Panel to demonstrate that the rates Telmex charges for mode 1 interconnection substantially exceed prices charged within Mexico for the same network elements. Instead, Mexico asserts that under the U.S. interpretation of "*basadas en costos*," "the carrier supplying the service would be prohibited from making any profit . . . ."[41] This is not correct. Under Mexican law, interconnection rates for commercially-present suppliers must recover at least the total cost of all network elements. The term used for "total cost" in Mexican law is "long run average incremental cost."[42] As we demonstrated in paragraph 77 of our responses to the Panel's questions, the term "long run" refers to a period long enough so that all costs become variable. As a result, when Mexican law requires that carriers recover "at least the long run average incremental cost," it already builds in the cost of capital, which includes a *reasonable rate of return*, or in other words a profit.

52. Mexico proposes two alternative benchmarks to show that its rates are "sufficiently cost-based" to satisfy its Reference Paper obligations – one from the ITU and another from the FCC.[43] However, neither benchmark is appropriate, because both the ITU and the FCC state that their benchmarks are not cost-oriented.

[40] 1995 Federal Telecommunications Law, Article 62 (Exhibit US-16).
[41] Mexico Responses to Questions from the Panel, para. 185.
[42] 1995 Federal Telecommunications Law, Article 62 (Exhibit US-16).
[43] *See* Mexico Responses to Questions from the Panel, paras. 195-196.

53. ITU Recommendation D.140 states that its target rates are "to be used . . . during the *transition* to cost-orientation," and should not be "taken as cost-oriented levels."[44] After ITU Members have attained these target rates they "should continue to take positive steps to reduce their accounting rates to cost-oriented levels."[45]

54. Likewise, the benchmark rates established by the FCC in 1997 were not cost-oriented when issued, and are even less so in 2003. In adopting those rates, the FCC stated that its benchmarks ". . . still exceed foreign carriers' costs to terminate international traffic because they are based primarily on foreign carriers tariffed rates" in effect in 1996, and "include costs associated with providing retail communications services to consumers which would not be included in cost-based settlement rates."[46] The FCC therefore emphasized that its benchmarks "continue to exceed, usually substantially, any reasonable estimate of the level of foreign carriers' relevant costs of providing international termination services."[47]

55. Finally, by stating that "accounting rate revenues remain an important source of potential revenue for infrastructure development,"[48] Mexico effectively concedes that its international interconnection rates recover more than the cost of the "network components or facilities . . . require[d] for service to be provided" to U.S. suppliers.

56. Mexico also argues that its "success in introducing competition in the domestic market for long distance services has satisfied its obligations to ensure that settlement rates are cost-based within the meaning of the Reference Paper."[49] Mexico's argument that competition in a *different* market, for the supply of long distance service in Mexico, ensures cost-oriented rates in the separate market for the provision of interconnection to U.S. suppliers operating in the cross-border mode, is not logical.

[44] *See* Second Written Submission of the United States, para. 66; United States Responses to Questions from the Panel, para. 67. *See also* ITU Recommendation D.140, paras. E.1, E.2, footnote 7 (Exhibit MEX-11).
[45] *Id.*
[46] FCC Benchmarks Order, paras. 44, 70
[47] *Id.*, para. 19.
[48] Second Written Submission of Mexico, para. 95.
[49] Mexico Responses to Questions from the Panel, para 198.

57. Mexico asserts that "in a market where there is competition, market dynamics will ensure that the rates are cost-oriented." While competitive market dynamics could reasonably be expected to ensure cost-oriented rates in most countries, the market dynamics that would normally lead to cost-oriented rates are not allowed in Mexico.

58. Mexico imposes a naked prohibition on competition on all international routes between firms that would otherwise be competitors.[50] Mexico's ILD rules require a horizontal price-fixing cartel among Mexican suppliers. Those rules prevent all price competition between Mexican suppliers providing interconnection to U.S. cross-border suppliers. Even if other WTO Members do not have explicit requirements for settlement rates to be cost-based, they also do not have restrictions on competition like Mexico, and therefore can reasonably rely on competitive market dynamics to yield cost-based rates.

59. Finally, Mexico argues that the term "economic feasibility" provides "wide latitude to allow rates that would allow continued development of needed infrastructure and the achievement of universal service." Mexico purports to base its argument on the dictionary meaning of "economically." However, nothing in this definition supports consideration of the public policy factors cited by Mexico.

60. Mexico's definition of "economically feasible" as requiring consideration of the "efficient" use of income and wealth in fact *prohibits* consideration of the non-cost-oriented factors Mexico seeks to include through this language. The efficient use of resources requires cost-oriented pricing and not subsidization. Indeed, the ITU has said that "[t]he goal of economic efficiency is generally achieved by establishing charges that are as close to cost (ideally LRIC [Long Run Incremental Cost]) as possible, and that are specifically based on cost causation."[51] Therefore, the efficient use of income and wealth must preclude the open-ended subsidization of "policy goals" such as infrastructure development and universal service. The

[50] Second Written Submission of the United States, paras. 5, 85.
[51] ITU, *Trends in Telecommunications Reform 2000-2001* (Exhibit MEX-14), pg. 45.

terms "*basadas en costos*" and "cost-oriented" require a relationship between interconnection rates and the costs incurred in providing *interconnection*.

61. The last phrase of Section 2.2(b) provides context, requiring rates that are "sufficiently unbundled *so that the supplier need not pay for network components and facilities that it does not require for the service to be provided*."[52] This language makes clear that interconnection charges are limited to the specific network components and facilities required for the interconnection service provided. Lastly, Mexico's argument is also refuted by Section 3 of the Reference Paper, which provides for separate universal service obligations to finance universal service and infrastructure development. The recovery of universal service subsidies hidden in interconnection charges would be contrary to the Section 3 requirement for transparent administration of universal service obligations.

62. Mexico also argues that "under U.S. law the concept of 'economic feasibility' is a complete exception to the requirement to offer cost-based interconnection rates,"[53] based on provisions concerning rural telephone companies. However, this requirement of U.S. law is fully consistent with the United States' Reference Paper obligations. The United States expressly *limited* Section 2.2 of its Reference Paper to permit this exemption for rural carriers. Mexico made no such limitation on its Reference Paper, with respect to rural or any other carrier.

63. Mexico also wrongly claims that a U.S. statement during the 1990 negotiations on the Annex supports Mexico's assertion that the term "cost-based" allows flexibility to take into account social policy goals.[54] It is clear from this statement, however, that the United States was drawing a distinction between a cost-based rate and a price that includes a universal service component. As Mexico notes, this statement was made in the context of the Annex negotiations, which did not lead to the adoption of any "cost-based" or "cost-orientation" rate requirement. In

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[52] Emphasis added.
[53] Mexico Responses to Questions from the Panel, para. 234..
[54] Second written submission of Mexico, para. 188.

contrast, the Reference Paper separates the disciplines on interconnection rates in Section 2 from the disciplines on universal service in Section 3.

64. Finally, Mexico wrongly contends that the anti-competitive effect of the ILD rules falls only on Mexican concessionaires other than Telmex, and therefore cannot be "unreasonable" with regard to Telmex.[55] This argument misses the point. By conferring monopoly power on Telmex that allows it to negotiate artificially high interconnection rates, the ILD rules suppress demand, which is not "reasonable," and violates Section 2.2(b) of the Reference Paper.

Annex on Telecommunications

65. In response to the United States' showing under Section 5 of the Annex on Telecommunications, Mexico argues in its Second Written Submission, that "it did not inscribe any market access for ISR in its Schedule" and that therefore it does not have to permit the supply of public telecommunications services over private leased circuits.

66. This is remarkable given that in paragraph 106 of its Answers to the Panel's Questions Mexico admits that its "commercial agencies" commitment is a commitment for resale. In that paragraph, Mexico states "[t]hese commercial agencies are 're-sellers' and, to the extent of this inscription, Mexico has made a commitment respecting telecommunications services supplied by resale." Mexico then goes on to argue that this commitment is limited under mode 1 by the routing requirement and under mode 3 by the notation regarding the issuance of the relevant regulations.

67. Thus, again Mexico's defense in this case comes back to its reliance on the argument that the term "facilities" should be interpreted as something more than its ordinary meaning and that the notation in its Schedule regarding regulations gives Mexico complete discretion to deny market access indefinitely.

[55] Second Written Submission of Mexico, para. 103.

68. We have already addressed both of these arguments today and at length in our submissions so I will not repeat those points. In addition to those points, however, I would like to note that the definition of commercial agencies in Mexico's Schedule contradicts Mexico's argument that the routing requirement under mode 1 means that the supplier itself must hold a concession. This definition reads:

> Agencies which, without owning transmission means, provide third parties with telecommunications services by using capacity leased from a public network concessionaire.

69. That the reseller (*i.e.,* the commercial agency) will NOT be the party holding the concession is explicitly anticipated by this definition. Rather, the definition states that it is the lessor of the private leased circuits that will have the concession. Mexico's definition of "commercial agencies" is consistent with the U.S. interpretation of the routing requirement. That is, that the requirement that international traffic be routed through the facilities of a concessionaire does not mean that the supplier has to hold the concession itself, just that the facilities through which the services are routed must be owned by a concessionaire.

70. Thus, because Mexico undertook a commitment for resale of telecommunications services under both mode 1 and mode 3, it is obligated under Section 5(b) of the Annex to ensure that United States service suppliers have access to and use of private leased circuits for the provision of those services.

71. I would also like to comment upon Mexico's citation of sub-sector (g), entitled "private leased circuit services." Mexico cites to sub-sector (g), but then concludes that sub-sector (g) "does not encompass ISR."[56] The United States agrees. Sub-sector (g) does not address the use of private leased circuits for the purposes of resale. Rather, this sub-sector involves the operation of private networks, which is confirmed by a review of the CPC codes inscribed, 75221 and 75222, and the definition of "private leased circuit services" in the Chairman's Scheduling Note.

56 Mexico Response to Panel Question 6(b), para. 101.

72. The Scheduling Note states that "[s]ub-sector (g) – private leased circuit services – involves the ability of service suppliers to sell or lease any type of network capacity for the supply of services listed in any other basic telecom service subsector unless noted in the sector column. This would include capacity via cable, satellite and wireless network." It is clear from this definition that private leased circuit services covers service suppliers who are in the business of being the seller or the lessor (not the lessee) of private leased circuits. Thus, this sub-sector and the limitations inscribed under it in Mexico's Schedule are not relevant to the question of whether Mexico limited the provision of telecommunications services by resale.

73. Finally, Mexico's statements that private leased circuits are not offered to the public generally in Mexico and that Mexico has not authorized the use of private lines to carry public telephone traffic are simply false. In point of fact, private leased circuits are tariffed in Mexico and are routinely used by competitors in Mexico for the provision of public telecommunications services.

74. In light of these facts, Mexico's argument that it " . . . was careful to ensure that there would be no ambiguity suggesting that Mexico had agreed to allow private lines to be used to carry public switched telephone traffic,"[57] must be rejected.

75. Mexico also argues that the nature of the service included in its commitments makes the Annex inapplicable. As I have already explained, this is incorrect, since the "service" as defined in Mexico's Schedule covers the entirety of an end-to-end telephone call as provided to customers, from its original point of origin to its final point of termination.

76. On a different point, Mexico argues that the U.S. claim under the Annex should be rejected because Sections 5(a) and (b) do not operate to ensure interconnection at reasonable rates.[58] According to Mexico, to interpret the term "reasonable" in Sections 5(a) and (b) of the Annex as ensuring interconnection at reasonable rates would make Section 2.2(b) of the

[57] Mexico Responses to Questions from the Panel, para. 103.
[58] Mexico Responses to Question 6(b) from the Panel, para 101.

Reference Paper redundant.

77. We note that in paragraphs 314-317 of its responses to the Panel's questions, Mexico acknowledges that the context of a provision also informs its meaning. We agree, and consider that the context in which the term "reasonable" is used in Sections 5(a) and (b) of the Annex and Section 2.2(b) of the Reference Paper means that they can both require interconnection at reasonable rates, *just in different contexts*.

78. As we discussed in paragraph 106 of our responses to the Panel's questions, unlike Section 5 of the Annex, Section 2 of the Reference Paper imposes disciplines to prevent *major suppliers* from using interconnection to restrict other suppliers from offering a scheduled service. This qualification is important in markets like Mexico, where foreign service suppliers are barred from owning facilities and must rely on the major supplier to interconnect with end users. Among other things, Section 2.2(b) of the Reference Paper requires that Mexico ensure that its major supplier not abuse its market power to extract above-cost prices for interconnection that will reduce demand for and restrict the supply of basic telecommunications services.

Section 1 of the Reference Paper

79. Finally, let me turn briefly to Section 1 of Mexico's Reference Paper. Mexico's recent submissions present mostly the same arguments as its earlier submissions. Accordingly, I do not intend to wholly repeat our responses to those arguments today.[59]

80. Mexico argues that its ILD rules are "appropriate ... to prevent anticompetitive practices" because those rules in some fashion allowed Mexico to open international traffic to alternate suppliers in 1996.[60] This is not sufficient since those same rules have prevented essential price competition over the ensuing seven years and nullified the operation of competitive market

[59] *See* paragraphs 78-96 of the U.S. Second Written Submission, and the U.S. Responses to Questions 17-19 from the Panel.
[60] Mexico Responses to Questions from Panel, paras. 261-263.

conditions.

81. As previously explained, Mexico's competition law, the 1992 Federal Law of Economic Competition, prohibits price-fixing. However, Mexico's ILD rules fundamentally contradict the FLEC by requiring what Mexico's "antitrust" law would otherwise prevent. The resultant price-fixing cartel has precluded competition for the termination of cross-border traffic and the normal dynamic toward cost-based pricing, not facilitated it. It is not necessary to define exactly what measures may be "appropriate... to prevent anticompetitive practices" in order to confront measures that are obviously inappropriate.

82. In a desperate attempt to defend its ILD rules, Mexico admits today that its rules have anti-competitive effects (which it tries to justify by repeatedly misstating the U.S. International Settlements Policy ("ISP") rules) and then takes the astounding position that the government can effectively adopt measures to compel anti-competitive practices, if that is in fact the policy of the government. Mexico's argument renders Section 1 of the the Reference Paper completely and utterly meaningless.

83. Although we have already rebutted Mexico's previous assertions that its rules "mirror" those of the U.S. ISP, Mexico continues to misdescribe U.S. ISP regulations in a number of statements that are just flatly wrong.

84. Specifically, Mexico wrongly claims in paragraph 268 of its responses that the FCC will merely "consider waiving" the ISP for arrangements with carriers that do not possess market power. The FCC stated in a May 6, 1999 Report and Order on this subject that it "*will remove the ISP for arrangements with foreign carriers that lack market power in all foreign markets*."[61]

85. Second, Mexico fails to recognize that U.S. carrier arrangements with carriers with market power in countries authorized for ISR are also exempt from the requirements of the ISP

[61] FCC 99-73, FCC Report and Order on Reconsideration (released May 6, 1999), para. 36, available at http://www.fcc.gov/Bureaus/International/News_Releases/1999/nrin9016.html

for nondiscriminatory rates, proportionate return of traffic and the equal division of rates between the U.S. and the foreign carrier.[62] These ISR arrangements have been authorized in 84 countries.[63] FCC rules also allow ISR arrangements with all nondominant carriers in all countries.[64]

86. Mexico also mischaracterizes another critical difference between the International Settlements Policy and its ILD rules. Mexico incorrectly states that the United States requires "uniform settlement rates" like Mexico,[65] and that other U.S. carriers "lack discretion to deviate from the negotiating position" of WorldCom.[66] Unlike Mexico, the United States does not require uniform rates. Instead, the United States simply requires *nondiscriminatory* treatment of U.S. carriers: "all U.S. carrier must be *offered* the same effective accounting rate. . . ." All U.S. carriers negotiate rates independently, and any U.S. carrier may always seek to negotiate a more favorable rate. Indeed, AT&T complained to the FCC in 2001 that it had attempted to negotiate lower rates with Telmex than WorldCom had negotiated, but that Telmex had refused to negotiate with AT&T.[67]

87. It is pro-competitive rather than anti-competitive to apply a proportionate return system and the other requirements of the International Settlements Policy narrowly to prevent dominant suppliers with high rates from using their market power to receive increased above-cost subsidies. Mexico does not apply its ILD rules in this pro-competitive manner. Instead, Mexico applies its rules broadly, to all suppliers, to prevent price competition and to maintain the payment of above-cost subsidies resulting from the abuse of market power by Telmex.

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[62] FCC, Consolidated Accounting Rates of the United States (January 6, 2003), Note 11, available at http://www.fcc.gov/ib/pd/pf/account.html ("ISR allows U.S. carriers to enter agreements with foreign carriers that can differ from traditional settlement arrangements prescribed by the Commission's International Settlements Policy (ISP).") .

[63] *See* http://www.fcc.gov/ib/pd/pf/isr.html (listing 84 countries authorized for ISR arrangements with foreign dominant carriers).

[64] 47 CFR § 63.22(e)(2), 63.23(d)(2).

[65] Mexico Responses to Questions from the Panel, para. 174.

[66] *Id.*, para. 296.

[67] *See AT&T and Concert Objection to International settlements Policy Modification request for a Change in the Accounting Rate for International Message Telephone Service with Mexico*, FCC File Number ARC-MOD-20010530-00123.

88. Mr. Chairman, and Members of the Panel, this concludes my oral statement. For the reasons stated today and in our prior submissions, the United States urges the Panel to find that Mexico has not complied with its obligations under Sections 1 and 2 of its Reference Paper and Section 5 of the Annex on Telecommunications. I want to thank the Panel for its attention and note that we would be happy to answer any questions that the Panel may have.