

**Before the
Federal Communications Commission
Washington, D.C. 20554**

In the Matter of)	
)	
Sprint Communications)	
Company, L.P.)	ISP-97-M-708
)	
Request for Modification of)	
the International Settlements Policy)	
to Change the Accounting Rate)	
for Switched Voice Service with)	
Mexico)	

MEMORANDUM OPINION AND ORDER

Adopted: November 24, 1998

Released: November 24, 1998

By the Chief, International Bureau:

I. Introduction

1. We have before us a request filed by Sprint Communications Company L.P. (Sprint) for a modification of the Commission's International Settlements Policy (ISP)¹ to change the settlement rate for switched voice service with Mexico. We approve the \$0.19 rate which is to become effective on January 1, 2000. For the reasons discussed below, however, we deny Sprint's request for interim rates of \$0.375 effective January 1, 1998 and \$0.345 effective January 1, 1999.

II. Background

2. Sprint filed a request for modification of the Commission's International Settlements Policy (ISP) for switched voice service that would change its settlement rate with Teléfonos de Mexico, S.A. de C.V.

¹ The ISP requires uniform accounting rates, uniform terms for the sharing of tolls, and uniform settlement rates among U.S. carriers providing the same service to the same foreign point. The ISP also requires that U.S. carriers accept only their proportionate share of return traffic. *See Implementation of Uniform Settlements Policy for Parallel International Communications Routes*, 51 Fed. Reg. 4736 (1986) (1986 ISP Order); *Reconsideration*, 2 FCC Rcd 1118 (1987); *Further Reconsideration*, 3 FCC Rcd 1614 (1988). In 1991, the Commission reformed the ISP to encourage and facilitate accounting rate reductions by U.S. carriers. *See Regulation of International Accounting Rates*, CC Docket No. 90-337, Phase I, *Report and Order*, 6 FCC Rcd 3552 (1991); *Reconsideration*, 7 FCC Rcd 8049 (1992); *see also Regulation of International Accounting Rates*, CC Docket No. 90-337, Phase II, *Second Report & Order and Second Further Notice of Proposed Rulemaking*, 7 FCC Rcd 8040 (1992). In 1996, the Commission codified the proportionate return policy. *See Fourth Report and Order on Regulation of International Accounting Rates*, CC Docket No. 90-337, Phase II, *Report and Order*, 11 FCC Rcd 20063 (1997) (*Flexibility Order*).

(Telmex), a supplier of international telephone service in Mexico (*Sprint Modification Request*).² Sprint and Telmex are joint venture partners in Telmex/Sprint Communications (TSC). Sprint's previous agreement with Telmex, which included an average settlement rate of \$0.395 per minute for 1997 ("the 1997 settlement rate"), expired on December 31, 1997. Sprint seeks approval for average settlement rates of \$0.375 effective as of January 1, 1998; \$0.345 to become effective on January 1, 1999; and \$0.19 to become effective on January 1, 2000.³

3. AT&T, MCI, and WorldCom oppose the *Sprint Modification Request*. MCI and AT&T argue that Sprint's proposed rates for 1998 and 1999: (1) are inconsistent with the Commission's accounting rate policy because they reflect minimal reductions from the 1997 settlement rate and do not move far enough towards cost-based rates; (2) are a "whipsaw" that would preclude other U.S. carriers from negotiating lower rates; (3) are not in the public interest because they resulted from a "sweetheart" arrangement between Sprint and Telmex, its joint venture partner in TSC; and (4) are not in the public interest because Telmex has not made a firm commitment to honor the \$0.19 rate beginning on January 1, 2000.⁴

4. Sprint responds that the *Sprint Modification Request* is not a "garden variety" accounting rate modification request because it is based on an alleged compromise reached by Telmex with the U.S. and Mexican governments.⁵ Thus, Sprint disputes AT&T's and MCI's claim that its proposed rates reflect a "sweetheart" deal. Sprint acknowledges that its proposed rates neither achieve nor approximate annual proportionate reductions, but states that this is "irrelevant" because the Commission previously found that the reductions were in the public interest.⁶

² International Settlements Policy Modification for Change in Accounting Rates with Mexico, ISP-97-M-708 (filed October 28, 1997; amended November 12, 1997).

³ Settlement arrangements between U.S. carriers and Telmex are based on settlement rates that vary by rate band in each country, time of day, and service classification. Individual settlement rates are established for each of these categories. The individual rates filed by Sprint are set to produce the average settlement rates of 37.5¢ in 1998, 34.5¢ in 1999, and 19¢ in 2000.

⁴ AT&T Opposition to Sprint Waiver, ISP-97-708 (filed December 3, 1997) (AT&T Opposition), at 2-11; MCI Opposition to Sprint Waiver, ISP-97-708 (filed December 3, 1997) (MCI Opposition) at 1-6. *See also* WorldCom Opposition to Sprint Waiver, ISP-97-708 (filed December 3, 1997) at 2-3 (the rates are not in the public interest because they do not achieve annual proportionate reductions). AT&T and MCI state that Sprint does not have a firm commitment to the \$0.19 rate for 2000 because Telmex reserved the right to reconsider its commitment if the Commission requires it to comply with rates other than the rates in Sprint's modification request or if U.S. carriers make settlement payments at other rates. AT&T Opposition at 8; MCI Opposition at 5-6.

⁵ Sprint Opposition to Petitions of AT&T, MCI, and WorldCom, ISP-97-708 (filed December 16, 1997) (Sprint Opposition), at 1-5. Sprint describes a series of negotiations between U.S. and Mexican officials and carriers but does not describe the terms of the alleged compromise.

⁶ Sprint Opposition at 1-5.

III. Discussion

5. We consider here whether the *Sprint Modification Request* is in the public interest. For more than sixty years, the Commission has exercised regulatory oversight of international settlement arrangements.⁷ During this time, the Commission has developed policies to ensure that such arrangements are in the public interest. The cornerstone of these policies is the Commission's ISP. The traditional focus of the ISP was largely to prevent "whipsawing," which can occur when a dominant foreign carrier exercises its market power to play competing U.S. carriers off one another in order to force U.S. carriers to accept accounting rate agreements with unfavorable terms and conditions.⁸ The Commission has consistently found whipsawing to be contrary to the public interest because it prevents U.S. carriers from negotiating lower accounting rates, to the ultimate detriment of U.S. consumers. While the traditional focus of the Commission's regulation has been to prevent whipsawing, the Commission's policies have evolved over time to focus also on the "adverse effect of above-cost levels of international accounting rates on U.S. carriers and U.S. consumers."⁹ The Commission has found that above-cost accounting rates are contrary to the public interest because (a) they contribute to artificially high international calling prices and (b) they represent a subsidy from U.S. consumers to foreign carriers.¹⁰

6. Over the past several years, the Commission has increased its efforts to ensure that accounting rate arrangements are in the public interest. The Bureau has strictly enforced the Commission's regulations against whipsawing¹¹ and the Commission has modified its regulatory policies "in order to promote low, more

⁷ See, e.g., *Mackay Radio and Telegraph Company, Inc.*, 2 FCC 592 (1936); *aff'd by the Commission en banc*, 4 FCC 150 (1937); *aff'd sub nom. Mackay Radio and Telegraph Co. v. F.C.C.*, 97 F.2d 641 (D.C. Cir. 1938); *Regulation of International Accounting Rates*, CC No. Docket 90-337, *Report and Order*, 6 FCC Rcd 3552 (1991) (*1991 ISP Order*); *Regulation of International Accounting Rates*, CC Docket No. 90-337, Phase II, *Second Report and Order and Second Further Notice of Proposed Rulemaking*, 7 FCC Rcd 8040 (1992).

⁸ See, e.g., *1986 ISP Order*, 51 Fed. Reg. at 4741 ("The most frequent concession sought is a modification of the accounting rate in such a manner as to decrease the revenues paid by the PTT to the U.S. carrier for effectuating delivery in the United States or to increase the revenues paid by U.S. carriers to the PTT to effectuate delivery in the foreign country.").

⁹ *1991 ISP Order*, 6 FCC Rcd at 3552.

¹⁰ See, e.g., *1991 ISP Order*, 6 FCC Rcd at 3552 ("the existing above-cost international accounting rate structure appears to be the primary reason that U.S. international calling prices are significantly higher than U.S. domestic calling prices"); *International Settlement Rates*, IB Docket 96-261, *Report and Order*, 12 FCC Rcd 19806 (1997) (*Benchmarks Order*), *recon. pending, appeal filed, Cable & Wireless, P.L.C. v. FCC*, No. 97-1612 (D.C. Cir. filed Sept. 26, 1997) (*Benchmarks Order*) at ¶ 13 ("[c]onservative estimates put at least seventy percent of [the] total [1996 settlement payment] as an above-cost subsidy from U.S. consumers to foreign carriers"). See generally, *Policy Statement on International Accounting Rate Reform*, 11 FCC Rcd 3146 (1996).

¹¹ See, e.g., *AT&T Corp.: Proposed Extension of Accounting Rate Agreement for Switched Voice Service with Argentina, Order*, 11 FCC Rcd 18014 (International Bureau, rel. March 18, 1996); *AT&T Corp., MCI Telecommunications Corp., Sprint, LDDS WorldCom: Petitions for Waiver of the International Settlements Policy to Change the Accounting Rate for Switched Voice Service with Peru, Order and Authorization*, 11 FCC Rcd 12107 (International Bureau, rel. May 7, 1996).

cost-based, international accounting rates and calling prices."¹² As part of this effort, the Commission reformed its ISP in order to promote more cost-based accounting rates and directed U.S. carriers to "negotiate with their foreign correspondents accounting rates that are consistent with relevant cost trends."¹³ The Commission also adopted its *Benchmarks Order*, which establishes a set of benchmark rates and transition periods within which U.S. carriers are to negotiate settlement rates with their foreign correspondents that comply with these benchmarks.¹⁴ The Commission recognized in the *Benchmarks Order* that the benchmark rates are still above-cost, and reiterated that its goal remains "settlement rates that reflect incremental costs."¹⁵

7. Applying these Commission policies, we find that the interim rates for 1998 and 1999 contained in the *Sprint Modification Request* are not in the public interest. First, we find that the interim rates are contrary to the public interest because they do not make adequate progress toward achieving cost-based settlement rates. Second, we find that denial of the interim rates is necessary to prevent whipsawing. We discuss these findings further below.

8. Although the *Sprint Modification Request* proposes a \$0.19 settlement rate with Mexican carriers by January 1, 2000, as required by the *Benchmarks Order*, we find that the interim reductions remain so far above cost that they do not represent adequate progress in 1998 and 1999 toward cost-based rates.¹⁶ The Commission estimated that cost-based settlement rates are likely no higher than \$0.06-\$0.09.¹⁷ The interim settlement rates proposed by Sprint are well in excess of cost-based settlement rates. In the *Benchmarks Order*, the Commission stated that it "expected[ed] carriers to negotiate proportionate annual reductions in settlement rates."¹⁸ We note that Sprint's proposed reductions fall far short of the reductions that would be achieved under annual proportionate reductions. Sprint's proposed reduction of \$0.02 in 1998 from the 1997 settlement rate and an additional \$0.03 in 1999 unduly delay settlement rate reductions on the U.S.-Mexico route. Under the rates proposed in the *Sprint Modification Request*, 75 percent (15.5¢) of the aggregate reductions required in order to achieve the benchmark rate of \$0.19 would be delayed until January 1, 2000. This means that the aggregate U.S. settlement outpayments that would be due if the rates in the *Sprint Modification Request* were to be approved would be at least \$200 million greater than the aggregate outpayments that would be due if annual proportionate reductions were proposed, according to AT&T's calculations.¹⁹ Accordingly, we find that the interim rates for 1998 and 1999 in the *Sprint Modification*

¹² *Regulation of International Accounting Rates*, CC Docket No. 90-337, *Notice of Proposed Rulemaking*, 5 FCC Rcd 4948, 4949 (1990).

¹³ *1991 ISP Order*, 6 FCC Rcd at 3556. *See also Flexibility Order* (permitting U.S. carriers to negotiate alternative settlement arrangements that do not comply with the ISP in certain circumstances).

¹⁴ Pursuant to the *Benchmarks Order*, U.S. carriers are required to negotiate settlement rates of \$0.19 with their foreign correspondents in Mexico beginning on January 1, 2000.

¹⁵ *Benchmarks Order* at ¶ 44.

¹⁶ Although annual proportionate reductions are not mandated by the *Benchmarks Order*, the pace of interim reductions is relevant to our public interest analysis.

¹⁷ *Benchmarks Order* at ¶ 122.

¹⁸ *Benchmarks Order* at ¶ 172.

¹⁹ *See AT&T Opposition* at 5; *see also, MCI Opposition* at 3.

Request do not make adequate progress toward achieving cost-based settlement rates and are thus not in the public interest.

9. We also note that Telmex has shown no willingness to negotiate lower interim rates with other U.S. carriers.²⁰ For that reason, we find that denying, in part, the *Sprint Modification Request* is necessary to safeguard against whipsawing, which can occur when a foreign carrier uses its dominant market position to play U.S. carriers off one another to impose terms and conditions in accounting rate agreements that are unduly favorable to the dominant provider. Frequently, whipsawing takes the form of the foreign carrier isolating a U.S. carrier in an effort to negotiate a favorable accounting rate agreement. Once an agreement is reached with the foreign carrier, other U.S. carriers are under substantial pressure to accept the same agreement or risk retaliation by the foreign carrier. The retaliation could take several forms, some more subtle than others.²¹ The risk of whipsawing is particularly acute in cases where such an accounting rate agreement is reached between affiliates, as in this case. Whipsawing results in higher accounting rates than would otherwise exist if the foreign carrier were not able to play U.S. carriers off one another, to the detriment of U.S. consumers.

10. We find AT&T's and MCI's arguments regarding whipsawing to be persuasive. As the pleadings filed in opposition to the *Sprint Modification Request* indicate, other U.S. carriers have attempted to negotiate lower settlement rates with Telmex than Sprint has filed. Those efforts have not been successful because Telmex has exerted substantial pressure on other U.S. carriers to accept the same concessions as agreed to by Sprint.²² Moreover, as AT&T and MCI point out, the fact that Telmex and Sprint are joint venture partners in TSC could have affected Sprint's willingness to agree to terms and conditions that are not as favorable as AT&T and MCI seek.²³ If we approve the *Sprint Modification Request*, Telmex could be expected to exert more pressure on other U.S. carriers to accept the same inflated settlement rates to which its joint venture partner Sprint has agreed.²⁴ Indeed, Telmex has refused to negotiate lower rates with other U.S. carriers in part because it has argued that the Bureau already approved the interim rates in the *Sprint Modification Request* in the TSC Order.²⁵ We thus deny, in part, the *Sprint Modification Request* to prevent

²⁰ See AT&T Reply to Sprint Opposition, ISP-97-708 (filed January 13, 1988) (AT&T Reply), at 2. We note that Telmex currently has settlement rates with carriers in other countries that are substantially lower than the interim rates in the Sprint Modification Request. See *Ex parte* letter to Magalie Roman Salas, Secretary, Federal Communications Commission, from Judy Simonson, Government Affairs, Vice President, AT&T, October 30, 1998, at 1 (citing information provided by Telmex to the International Telecommunication Union showing that Telmex's lowest settlement rate is 25¢ per minute).

²¹ For example, a foreign carrier could retaliate simply by refusing to negotiate with other U.S. carriers. More aggressive forms of retaliation include diverting a disproportionate share of traffic to the U.S. carrier that agreed to the foreign carrier's demands or cutting off circuits of U.S. carriers that refuse to agree to the foreign carrier's terms.

²² See, e.g., AT&T Reply at 2-3.

²³ AT&T Opposition at 6-8; MCI Opposition at 3-4.

²⁴ See, e.g., *Petition for Waiver of the International Settlements Policy to Change the Accounting Rates for Switched Voice Service with India*, ISP-98-M-135, *Order*, DA 98-1060 (International Bureau, June 4, 1998).

²⁵ AT&T Reply at 2-3 (citing Telmex letter stating that the settlement rates in the Sprint Modification Request "are not negotiable" because the Bureau "found Telmex's commitment to reduce its settlement rates to these

whipsawing.

11. In finding that the interim rates are not in the public interest, we note that the U.S.-Mexico route is of unusual importance because of the high level of traffic and the extent to which traffic is unbalanced. The traffic levels on the U.S.-Mexico route are so high that U.S. settlement payments to Mexican carriers greatly exceed settlement payments to carriers in any other country.²⁶ Mexican carriers have received almost \$6 billion in settlement payments from U.S. carriers since 1990.²⁷ Under these circumstances, a relatively small difference in the settlement rate on the U.S.-Mexico route can have a substantial impact on settlement payments, and, ultimately, on U.S. calling prices. For example, based on the U.S. carriers' net traffic outflow to Mexico in 1997 of 1.8 billion minutes, a one cent decrease in the settlement rate would result in a reduction of almost \$20 million in outpayments to Mexican carriers. As the Commission noted in its *Benchmarks Order*, a substantial portion of U.S. settlement payments exceed the cost to terminate calls in other countries. The high outpayments to Mexican carriers are fueled by above-cost accounting rates and rapid growth in U.S. carriers' net traffic outflow to Mexico.²⁸ The portion of U.S. carrier settlement outpayments to Mexican carriers that are above-cost represents a subsidy from U.S. consumers to foreign carriers. The subsidy from U.S. consumers to Mexican carriers is particularly large because of the tremendous volume of traffic, the traffic imbalance, and the extent to which accounting rates on the route are above-cost. These particular circumstances provide additional support for our finding that the interim reductions for 1998 and 1999 contained in the *Sprint Modification Request* are not in the public interest.

12. Sprint argues that the Commission should approve the *Sprint Modification Request* under the standard adopted in the *Benchmarks Order* for "grandfathered" settlement rate agreements, even though the interim reductions are nominal.²⁹ We disagree for the following reasons. Sprint's argument refers to the Commission's statement in the *Benchmarks Order* that a settlement rate agreement reached prior to January 1, 1998³⁰ could be found to be in the public interest -- and thereby "grandfathered" -- even if it does not comply strictly with the requirements of the *Benchmarks Order*. The Commission stated that such "grandfathered" agreements could be found to be in the public interest, provided they achieved the goals the Commission set forth in the *Benchmarks Order* and achieved settlement rates at or below the relevant benchmarks within a

levels to be a significant public interest factor weighing in favor of grant of TSC's [Section 214] application"). In fact, the Bureau made no finding regarding interim rates in the *TSC Order* or elsewhere. See *infra*, para. 13.

²⁶ Data on U.S. carrier outpayments is contained in annual reports compiled by the Common Carrier Bureau of the information U.S. carriers file pursuant to Section 43.61 of the Commission's rules. See 47 U.S.C. § 43.61. The most recent report is entitled "1996 Section 43.61 International Telecommunications Data," January 1998, Industry Analysis Division, Common Carrier Bureau.

²⁷ Although settlement payments to Mexican carriers declined in 1997, they still exceeded \$700 million in that year, almost 13 percent of total U.S. payments worldwide. The next highest outpayment country after Mexico in 1997 was China, which received \$267.7 million in settlement payments from U.S. carriers.

²⁸ The traffic imbalance on the U.S.-Mexico route grew at a compound annual rate of approximately 26% in the years 1993 through 1997.

²⁹ Sprint Opposition at 6-7.

³⁰ January 1, 1998 was the effective date of the *Benchmarks Order*.

reasonable time.³¹ We find that the interim rates in the *Sprint Modification Request* are not consistent with the goals of the *Benchmarks Order* because, as discussed above, they delay unduly settlement rate reductions on the U.S.-Mexico route and do not represent adequate progress in 1998 and 1999 toward cost-based rates. We thus disagree with Sprint's argument that the rates are in the public interest and should be approved under the standard for grandfathered agreements contained in the *Benchmarks Order*.

13. Sprint further argues that the Bureau already found in its October 1997 *TSC Order*³² the interim rates for 1998 and 1999 to be in the public interest.³³ Sprint's assertion is incorrect. In fact, the Bureau made no finding whatsoever in the *TSC Order* regarding the interim rates. The Bureau found only that Telmex's agreement to reduce its rates to the \$0.19 benchmark by January 1, 2000 was in the public interest, and we reiterate that finding here in approving that part of the *Sprint Modification Request* proposing a \$0.19 rate from January 1, 2000.³⁴ We note that even this \$0.19 rate remains far above cost and encourage carriers to negotiate lower rates.

IV. Conclusion

14. For the above-stated reasons, we grant Sprint's request for the \$0.19 rate effective January 1, 2000 and deny Sprint's request for the interim rates of \$0.375 effective January 1, 1998 and \$0.345 effective January 1, 1999. We direct U.S. carriers to negotiate lower interim rates that demonstrate reasonable progress toward achieving cost-based settlement rates.

V. Ordering Clauses

15. Accordingly, IT IS ORDERED that Sprint's request to establish a settlement rate with Telmex of \$0.375 per minute effective January 1, 1998, and \$0.345 per minute effective January 1, 1999 is DENIED.

16. IT IS FURTHER ORDERED that Sprint's request to establish an accounting rate with Telmex of \$0.19 per minute effective January 1, 2000 is GRANTED.

17. IT IS FURTHER ORDERED that Sprint and other U.S. carriers shall continue their best efforts to achieve interim settlement rate reductions for 1998 and 1999 that comply with the Commission's ISP.

18. This order is effective upon adoption. Petitions for reconsideration under Section 1.106 of

³¹ *Benchmarks Order* at ¶ 190.

³² *Application for Authority under Section 214 of the Communications Act for Global Authority to Operate as an International Switched Resale Carrier Between the United States and International Points, Including Mexico*, ITC-97-127, *Order, Authorization and Certificate*, DA 97-2289 (October 30, 1997) (*TSC Order*), application for review pending.

³³ Sprint Opposition at 6-7.

³⁴ Specifically, the Commission found in the *TSC Order* that "Telmex's commitment to reduce its settlement rate to the applicable benchmark in a timely manner" was in the public interest. *TSC Order* at ¶ 59 (emphasis added). See Letter from Regina M. Keeney, Chief, International Bureau, FCC, to Luis López Rojo, Chief Executive Officer, Telmex/Sprint Corporation, dated June 2, 1998 (noting that the Bureau did not, contrary to the claim in a TSC press release, find that Telmex's commitments on interim rates for 1998 and 1999 were a public interest factor in favor of granting TSC a Section 214 authorization).

the Commission's rules may be filed within 30 days of the public notice of this order (*see* Section 1.4(b)(2) of the Commission's rules).

FEDERAL COMMUNICATIONS COMMISSION

Regina M. Keeney
Chief, International Bureau