Independent Communications Authority of South Africa

Council Decisions 18 February 2022

NO.	AGENDA ITEM	COUNCIL DECISION
1.	**Outcome of Pre-Qualification Assessment – IMT Licensing** 1.1. The purpose of this submission was to recommend to Council that: 1.1.1 The pre-qualification report on the applications received in relation to the Invitation to Apply relating to the licensing process for International Mobile Telecommunications ("IMT") in respect of the provision of mobile broadband wireless access services for urban and rural areas using the complementary bands, IMT700, IMT800, IMT2600 and IMT3500 ("2021 ITA"), be approved. 1.1.2 The above-mentioned notice will be published in the Government Gazette, communicating the outcome of the pre-qualification stage. 1.1.3 The letters to the qualifying bidders, communicating the decisions of the Authority in relation to the pre-qualification assessment made. 1.2. On 10 December 2021, the Authority published an Invitation to Apply on the licensing process for IMT in respect of the provision of the mobile broadband wireless access services for urban and rural areas, using complementary bands IMT700, IMT800, IMT2600 and IMT3500, published in Government Gazette No. 45628.	**The recommendation was approved by Council.**

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	1.3. On 31 January 2022, the Authority received six (6) applications responding to the 2021 ITA from: Cell C, MTN, Vodacom, Telkom, Rain Networks and Liquid Telecoms. 1.4. According to section 18.3 of the 2021 ITA: 1.4.1 The Authority will announce the qualified bidders on 21 February 2022. 1.4.2 The Committee will attend auction training from 21 to 25 February 2022. 1.4.3 The bidder seminar will be on 28 February 2021. 1.4.4 Following that, the individual mock auctions will resume from 01 to 03 March 2022. 1.4.5 The Opt-in round auction will be on 08 March 2022. 1.4.6 Following that, the main auction will start from 10 March 2022. 1.5. The Licensing of IMT Spectrum Council Committee ("the Committee") with the assistance of the Service Provider, has assessed the six (6) applications received in order to determine applicants that will be eligible to participate in the auction stage. The assessment of applications was done in accordance with section 16.3.8 of the 2021 ITA. 1.6. A score of 80 out of 100 in points is required for an applicant to be qualified as a bidder. The scoring approach is all or nothing on each factor. Each of the critical efficiency factors has a score of more than twenty (20). Applicants have to meet all three (3) to qualify as bidders. 1.7. The Committee noted that Vodacom indicated that it applied in November 2021 to return 1 x 5 MHz TDD portion of its assigned spectrum on 2100 MHz band, the application of which has not	

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	yet been finalised. Vodacom submitted that the 1 x 5 MHz surrendered should be incorporated in determining its overall cap.	
	1.8. Liquid Telecoms argued that its assignment on the IMT850 should not be considered in calculating its IMT spectrum holdings. The Committee resolved that the assignment of the IMT850 must be included, since the band is identified for IMT.	
	1.9. Similarly, Rain Networks submitted that its 1x10MHz on the IMT1800 should not be considered in calculating the IMT spectrum holdings. However, the Committee resolved that the assignment of the IMT1800 must be included since the band is identified for IMT.	
	1.10. Council should note that Cell C did not mention the 80% explicitly in its submissions in relation to the functional criteria. However, it confirms that coverage and speed obligations will be met, and that it will use contractual mechanisms with one or more managed network service providers to ensure this.	
	1.11. Cell C further added that it can continue to ensure, through these agreements, that its customers enjoy the same extensive geographical and population coverage as the host network(s).	
	1.12. On 14 February 2022 the Committee wrote to Liquid to confirm its commitment and plans on the 700 MHz and 800 MHz bands, and to demonstrate how the rollout obligation will be achieved. Liquid has subsequently responded that, as per its business plan, the Coverage Roll-out Plan provided includes 3 phases over a total of 5 years.	
	1.13. Liquid made the assumption based on its intention to deploy its networks, which are based on IMT2020 System, where deployments can be made in the low, mid and high bands. The coverage obligations, therefore, are to be met with the low bands, that is with spectrum either	

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	in the 700 MHz or 800 MHz band. Liquid made assumptions, based on the fact that they do not have any precedents to benchmark against, and extrapolated the deployment in phases over the period set out in the ITA in order to achieve the required 80% population coverage. 1.14. The Committee confirmed that the obligations will form part of the licence condition, and that the deployment of infrastructure in the various phases will have to be monitored and reported to the Authority in accordance with the phased approach, leading to the compliance with the 80%, and the period within which this has to be complied with. <u>Recommendation to Council</u> 1.15. It was recommended that Council approve: 1.15.1 The prequalification report on the applications received against the ITA; 1.15.2 The notice to be published in the Government Gazette communicating the outcome of the pre-qualification stage of the licensing process; and 1.15.3 The letters communicating the decisions of the Authority in relation to the prequalification assessment made and outlining the upcoming auction process.	

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2.	**SAPO RFS Evaluation** 2.1. The purpose of this submission was to make a recommendation to Council to approve the evaluation of SAPO's Regulatory Financial Statements ("RFS") for the 2020/21 Financial Year ("FY") (i.e. 1 April 2020 to 31 March 2021). 2.2. The Authority, in terms of section 8 and section 30 of the Postal Services Act No. 124 of 1998 ("the Act"), published the Accounting Separation Regulations for Reserved Postal Services ("the Accounting Separation Regulations"). 2.3. The purpose of the Accounting Separation Regulations is to prescribe a structured accounting and regulatory reporting framework for SAPO's reserved postal services to achieve uniformity, and consistent reporting of elements required to determine fees and charges for reserved postal services before the said fees and charges are implemented. 2.4. During the Authority's evaluation of SAPO's RFS and OPM, it noted that the cost of equity (KE) borne by SAPO decreased from 67.37% in the previous year to 46.57% in the 2020/21 FY. 2.5. The decrease in KE is desirable to SAPO, as it lowers the burden on SAPO's operations to generate long-term value for shareholders. This in turn improves the risk profile of SAPO's ability to generate future cashflows. However, SAPO is currently grappling with a negative balance on shareholders' equity, arising from its liabilities exceeding its assets. 2.6. The Capital Asset Pricing Model (CAPM), which was used in calculating the KE, establishes the relationship between the risk and expected return for assets.	**The recommendation was approved by Council.**

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	2.7. Although the Price Cap Regulations allow SAPO to increase the price charged for reserved postal services, these price increases are limited by the Authority through a general price control formula, which effectively sets a price ceiling or price cap on reserved postal services. 2.8. The evaluation of the RFS is intended, amongst other things, to assist the Authority in monitoring SAPO in pursuit of the following objectives: 2.8.1 Ensuring that SAPO does not exploit its market power in terms of the provision of reserved postal services. 2.8.2 Ensuring that SAPO does not engage in anti-competitive cross subsidisation i.e., SAPO does not use profits from reserved services to cross-subsidise unreserved services (it may, however, use profits from unreserved services to finance reserved services); 2.8.3 Ensuring that SAPO does not price on an unduly discriminatory basis; 2.8.4 Ensuring that tariffs are cost-orientated and sufficiently unbundled; 2.8.5 Monitoring SAPO's financial situation; and 2.8.6Evaluating the effectiveness of the price control regime. 2.9. The AGSA is the statutory auditor for SAPO. However, since the inception of the Accounting Separation Regulations in 2011, no regulatory audit scope has been set out as Agreed Upon Procedures ("AUP") for the audit of SAPO's RFS.	

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	2.10. The PRA division requested that it be allowed to engage SAPO and the AGSA to begin the process to rectify this in the 2018/19 FY, so that SAPO may be able to present audited RFS to the Authority from 2019/20 FY onwards. 2.11. The Authority requested the AGSA to perform an AUP engagement, which included a proposed AUP scope, as far back as 2019. A meeting was held between the Authority and the AGSA on 26 June 2019, to discuss the AUP engagement request. 2.12. The AGSA indicated that it was not able to conduct an AUP engagement on the 2019/20 FY and 2020/21 FY RFS given the advent of the Corona virus epidemic in 2020. Additionally, the AGSA was unable to incorporate the AUP alongside its Statutory Audit of SAPO, due to internal process limitations and SAPO's financial constraints. Further, the Statutory Audit process itself was still not concluded at the time of the RFS submission by SAPO. 2.13. In its RFS submission for the 2020/21 FY, SAPO has indicated that, given the separation of Postbank from SAPO, the RFS will be as per the annual financial statements. As such, no reconciliation of figures is required and the need for the RFS to be audited by the AGSA is not necessary. 2.14. The Authority's evaluation covered three (3) areas: 2.14.1 Administrative procedures compliance as per the Act, licence conditions, and Accounting Separation Regulations; 2.14.2 Accounting records preparation as per the Accounting Separation Regulations; and 2.14.3 Financial ratio analysis.	

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	2.15. SAPO's revenue dropped by 27.45% in the 2020/21 FY. This reflects further deterioration in the ability to generate revenue from reserved services (which could have been amplified by the adverse effects of the Covid 19 pandemic). A decrease of 24.28% was previously recorded in the 2019/20 FY. 2.16. As a result, operating losses increased by 33.04% and 46.90%, in the 2019/20 FY and the 2020/21 FY respectively. This is an indication of SAPO's inability to generate sufficient sales from its operations to cover its operating expenses, further questioning the sustainability of the company. 2.17. While a slight increase in both operating profit margin and ROA was achieved in the 2018/19 FY, the ratios have steadily declined in the 2019/20 FY and the 2020/21 FY. Of particular concern is the 85.50% deterioration of operating profit margin experienced in the last reported financial year due, in part, to the considerable increase in losses (i.e., negative EBIT). 2.18. Whilst operating costs (such as employee costs, transport costs and other operating costs) decreased during the 2020/21 FY, this was not enough to mitigate the negative impact of SAPO's sustained losses. 2.19. A similar worsening trend of ROA to -31.64% was experienced in the 2020/21 FY due to negative earnings. The deteriorating ROA trend shows that SAPO's assets are not being efficiently employed in generating adequate returns. 2.20. In the 2018/19 FY SAPO registered a significant liquidity improvement, which was short lived, as it regressed in the subsequent 2019/20 FY and 2020/21 FY.	

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	2.21. During the 2020/21 FY, current assets increased by 13.20%. However, the accompanying increase of 35.60% in current liabilities is the primary reason for the decrease in liquidity. 2.22. During the 2020/21 FY the total equity position worsened from -R40.57 million to -R2.576 billion, which decreased the equity multiplier to -3.04%. 2.23. The following findings were noted: Financial Ratio Analysis: 2.23.1 **Revenue, OPEX and Operating Profit/Loss**: The drop in revenue and increase in operating losses is an indication of SAPO's inability to generate sufficient sales from its operations to cover its operating expenses. 2.23.2 **Profitability and operating efficiency**: The deteriorating Return On Assets trend shows that SAPO's assets are not being efficiently employed in generating adequate returns. 2.23.3 **Liquidity**: Both the current and quick ratios decreased to 0.44%, which reveals the ongoing deterioration in SAPO's ability in meeting its short-term obligations. 2.23.4 **Financial Leverage** - Equity Multiplier and Debt to Equity Ratio: During the 2020/21 financial year, the total equity position worsened from -R40.57 million to -R2.576 billion, which decreased the equity multiplier to -3.04%. 2.23.5 **Conclusion on SAPO's Financial Performance**: From the performance and ratio analysis included in the evaluation report, SAPO is clearly still battling in providing a sustainable postal service.	

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	2.23.6 Given SAPO's continued inability to submit audited RFS to the Authority, the Authority places heavy reliance on SAPO's statutory Audited Financial Statements ("AFS") and public signalling. After consideration of the above, there is reason for the Authority to be concerned about the RFS. <u>Recommendation</u> 2.24. It was recommended that Council approve the evaluation of SAPO's 2020/2021 FY Regulatory Financial Statements (RFS) (i.e. 01 April 2020 to 31 March 2021).	

Per: ICASA Secretariat Unit

Nicholous Mabilane
Corporate Secretary