COMPLAINTS AND COMPLIANCE COMMITTEE[1]

Dates: October and 18,20 November 2010 Case number: 41/ 2010

TELKOM SA LTD APPLICANT

vs

CELL C (PTY) LTD RESPONDENT

Committee

JCW van Rooyen SC (Acting Chairperson)
N Batyi[2]
Z Ntukwana
J Tlokana

For the Applicant : A Rafik Bhana SC (with him JJ Meiring) instructed by Maluleke Msimang & Associates, Johannesburg
For the Respondent : Deneys Reitz Inc

JUDGMENT

[1] Telkom SA Ltd (the fixed line incumbent) has created a self standing unit within the company to enter the mobile market, Telkom Mobile("TM"). For ease of reference, I shall refer to TM as the applicant, although it is not a legal persona. TM notified the Independent Communications Authority of South Africa ("ICASA") in terms of section 37(4) of the Electronic Communications Act 36 of 2005 ("ECA") that Cell C Pty Ltd ("Cell C"), a mobile operator in South Africa, was unwilling to agree to a wholesale termination flat rate of 93c per minute payable to

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1 Established in terms of s 17A of the ICASA Act 13 of 2000 as amended
2 Member appointed by Council in terms of section 17A(1) of the ICASA Act 13 of 2000

TM, inter alia since the rate was too high and, the rates were, in any case contingent upon the completion of the ICASA process which was underway in terms of section 67(4) *et seq*. of the ECA. TM requires that the said termination rate be applicable during all hours of the day and that it also be applicable to calls from Community Service Telephones ("CST's"). The position taken by Cell C is that the current industry agreed rate of 89c per minute and the lesser 76c off-peak rate should also be the rate charged by TM. Cell C also requires that TM only charges 6c per minute termination rate as to the CST's. Cell C, Vodacom and MTN were required by their original licenses to roll out a certain number of these telephones in delineated areas, generally described as underprivileged areas. For purposes of this judgment we will accept that the 6c rate was agreed upon between the three incumbents. ICASA states in its Explanatory Note for the Draft Call Termination Regulations[3] that the rates for CST termination are dealt with through separate regulatory processes.TM argued that since it is under no obligation to roll out such phones, it would be unreasonable to require it to terminate at the agreed rate of 6c. Also in this case, it required the ordinary termination rate of 93c. Cell C also disputes TM's attempt to include a clause in the agreement which will allow both parties to apply interconnection bypass.

[2] Counsel addressed the CCC as to what the task of the CCC is in a case such as the present. Was it adjudicating a complaint or an allegation of non-compliance, as would be the case in terms of section 17B(a)(ii) and (iii) of the ICASA Act (where it adjudicates the matter on the merits and if a finding is made against a licensee recommends a sanction to Council in terms of section 17D(3)) or was it called upon to finally resolve the matter without any participation by the ICASA Council. The CCC is of the view that the present matter falls squarely within the jurisdiction of the CCC to *resolve*. This is not a complaints procedure in terms of section 17C of the ICASA Act. See section 40(3) of the ECA.

[3] Section 37(4)(c) provides that the Authority may refer a dispute in the negotiation of an interconnection agreement to the CCC for resolution in accordance with the procedures prescribed in terms of section 38 of the ECA. No

[3] *Government Gazette* No 33698, 29 October p. 25.

such procedures have, however, been included in the Interconnection Regulations of 9 April 2010.[4] The CCC is of the view that the absence of such a procedure does not amount to a bar against the resolution which the CCC is called upon to make in terms of section 37(4)(c).[5] What is more, section 33 of the Constitution guarantees that everyone has the right to administrative action that is lawful, reasonable and procedurally fair. This rule was, of course, applied: the CCC laid down that the matter would be inquired into on affidavits and, if applied for, by oral evidence. Affidavits from both sides were filed on a founding, answering and replying basis and expert reports were also filed. All expert reports were admitted. The CCC requested TM, at the hearing, to provide it with a copy of the interconnection agreement between TM and Telkom(fixed) so as to establish what rates were being charged in this case by TM. This document was provided on the 10th January 2011 and copied to Cell C's attorneys. Cell C's attorneys informed the CCC that it was studying the document and questioned the fact that the document that it had received had not been signed. In the light of the conclusion which the CCC has reached as to termination rates, it is not necessary to deal with this document.

[4] A further preliminary matter had to do with whether Cell C had not delayed the conclusion of the interconnection agreement so as to, in effect, keep TM out as a competitor as long as possible. It will serve no purpose to spend time on this debate, since the order which TM seeks is a retrospective order as from the date that the parties had in fact commenced with interconnection activities, which would seem to have been in September 2010. There was no attempt to convince the CCC that it should consider taking the matter back to an earlier date as a result of the alleged conduct of Cell C.

[5] A further question was whether it was permissible in law for the CCC to determine a termination rate. Was this not a matter solely for the ICASA Council in terms of section 41 and 67(4) *et seq*. of the ECA? It was common cause during the hearing that ICASA had undertaken an inquiry on the matter in terms of

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[4] Published under Government Notice R282 in *Government Gazette* 33101 of 9 April 2010.

[5] *Compare the principle as discussed in Verstappen v Port Edward TB 1994 (3) SA 569 (D.)*

section 67(4) *et seq* and that it was about to publish the final Regulations. It was also argued that even if the CCC had this power, it should decide not to impose a rate in the light of the pending Regulations. Had ICASA already published the Regulations when interconnection activities between TM and Cell commenced, the CCC would, no doubt, have been acting *ultra vires* by ordering a rate in the resolution of this dispute. However, it is clear both from section 41 and 67(4) *et seq*. that there is no obligation on ICASA to have made the Regulations. It might very well have decided that Regulations were not necessary. In the absence of Regulations section 37 would indeed be necessary where a dispute arises between mobile operators, also in so far as rates are concerned. Before the Termination Regulations became effective,[6] the rates were unregulated and therefore section 37 also applies to disputes as to rates in this period.

[6] The question before the CCC is then, in terms of section 37 ECA, whether the rate requested by TM is unreasonable.[7] Section 37(3) provides as follows:

> For the purposes of subsection (1) a request is reasonable where the Authority determines that the requested interconnection—
> *(a)* is technically and financially feasible; and
> *(b)* will promote the efficient use of electronic communications networks and services.

[7] Mr *Bhana*, for TM, argued that since TM is the interconnection seeker and Cell C the interconnection provider, Cell C is called upon to show why the rate is unreasonable. In its answering affidavit Cell C stated that in so far as the 93c rate was concerned, *Cell C* was the interconnection seeker and therefore TM, as interconnection provider, would have to show that the rate of 93c is not unreasonable. In so far as the 89c is concerned, there was no dispute and, in that case, Cell C was the internet provider. Cell C would thus not have to show that the 89c peak and 76 off peak rates are not unreasonable. Mr *Bhana* argued that this argument was unacceptable, since per definition TM was the

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[6] See the Call Termination Regulations as published in the *Government Gazette* no 33698 of 29 October 2010.

[7] Both sections 37(1) and 37(4) refer to terms and conditions and even if 37(4) is read on its own, reasonableness would, read within the context, be applicable as criterion. The matter was, in any case, argued in this Cell C matter on the basis of reasonableness by Counsel from both sides. I have now read the judgment of my colleague, Vas Soni SC in Telkom v MTN (case 39/2010). We would, no doubt, have reached the same conclusion here as was reached in that judgment, had we applied that approach. Ultimately the decision of the CCC must be rationally related to the facts. That link was not supplied to us by TM.

interconnection seeker and, as a price taker, it was entitled to charge what it deemed reasonable to cover its costs. The CCC is of the view that in a case such as the present, it is not in the interest of justice to work with a strict set of rules as to onus. The question is, ultimately, whether the CCC is satisfied that the rate charged by TM is not unreasonable. In this regard it will, of course, also take heed of section 37(3) as quoted above. The CCC does not know on what grounds the 89c and 76c rates of Cell C are based. Even Cell C concedes in its answering affidavit that it "has not yet been able to determine its costs with sufficient accuracy to impose a cost-oriented remedy."

[8] From the expert reports placed before the CCC it has emerged that the efficient use of the electronic communications networks and services will not be promoted if costs for the ordinary running of the service were to be taken as the criterion. Such an approach might serve to protect poor management. The accent, accordingly, should be placed on the unavoidable costs (also called exogenous costs) of entering the mobile market. These costs are then delineated as costs relating to the efficiency of spectrum and economies of scale and scope, which are not available to a new entrant in comparison to the incumbents. We shall now deal with expert opinions presented to the CCC on affidavit by the parties.

[9] Dr Theron, an expert presented by Cell C, argues that while it is true that asymmetric termination rates are effective in ensuring increased competition, especially for late entrants, the question that needs to be answered is why this should be applied to TM if Cell C, as a late entrant in 2001, never received any benefits from the side of Government before 2006 or the ICASA after 2006. TM also does not face the same regulatory requirements which served to challenge and delay the entry of Cell C in 2001. The CCC is, however, of the view that when the proposed rate by TM is found to be not unreasonable, that concludes the matter, whatever the history of Cell C was. The question is what is reasonable within the present circumstances. If mistakes were made by the authorities in the past, they should, in any case, not be repeated.

[10] Dr Theron, with the aid of graphs, illustrates that claims which TM makes as to substantial benefits which Cell C will have from off-net calls from TM customers to its customers are not as substantial as TM claims. The CCC is of the view that TM's

argument as to what amounts Cell C will make in off-net calls from TM to Cell C is speculative and should not carry any weight in determining what is reasonable.

[11] Dr Theron also rejects the price taker principle espoused by TM. It is true that the price taker principle is best suited for a perfectly balanced competitive market and TM has argued that the principle should, in this matter, be seen within the context of the local mobile industry. The concept, as used by TM, probably rather means that within an unregulated mobile termination rate market, the seller has the right to charge the price which it believes to be justified in the circumstances. Section 37 of the ECA, however, clearly limits the "price taker" principle by reasonableness. Of course, it should also be borne in mind that the rates which apply amongst the three incumbents are based on an agreement or an arrangement between them.TM has no duty to abide by whatever this arrangement is. In that sense, it should be free to set its own rate and, as long as it is reasonable, it need not be identical with the rates charged by the incumbents. In fact, the concepts of asymmetry and symmetry would seem to be more appropriate within a regulated system, where asymmetric rates may be prescribed by the *Regulator* as an interim or even as a permanent mechanism to act as a pro-competitive measure.

[12] Dr Theron further argues that TM will benefit substantially from its relationship with Telkom SA Ltd. She refers to capital investment by Telkom into TM, the launch on the back of a very well entrenched brand and the established distribution network of Telkom which will be available to distribute the new offering. Telkom also has unused spectrum which could, according to her, easily be utilised by TM. These factors all combine, according to Dr Theron, to create an easier environment for TM upon entry. We agree with expert Simon Baker[8] that pure source of funds arguments rarely give credence in competition assessments of mergers or dominant firm conduct, because capital markets are generally assumed to be efficient. Thus, if capital markets will not finance a project for fear that it will not be profitable, then it would not normally make sense to use internal funds to finance it either. We agree that a more plausible argument relates to synergies with Telkom fixed line business that will lower the incremental cost of operation. Ultimately, however, this kind of argument tends to be speculative. Fact is, TM is a new entrant into a market which is also new to Telkom, in spite of its having had a 50% interest in Vodacom. Whatever the value as to economies of scale and scope this interest could have had, Telkom

[8] Presented by TM.

SA Ltd is presently no longer a shareholder of Vodacom. In the light of the conclusion which the CCC reaches in this matter, it is, however, not necessary to dwell on this aspect. The CCC accepts, for purposes of this judgment, that TM will to a substantial extent be a new entrant and, though to a much lesser extent than other new entrants, be subject to a higher unit cost than Cell C.

[13] Returning to the matter of spectrum. In so far as spectrum is concerned Cell C has access to spectrum in the 900MHz, 1800MHz and 2100MHz bands, while TM has access to 1800MHz and 21000MHz. According to Brett Nash, expert presented by TM, the economic implication of spectrum allocation for an operator is based on the fact that different spectrum provides different degrees of coverage. With GSM 900MHz spectrum fewer sites are needed to provide similar levels of coverage when compared to GSM 1800MHz spectrum. Nash then illustrates this by way of the application of a formula, the application of which leads to the result that twice the number of sites are generally required to give continuous coverage at the same level on 1800MHz compared to 900MHz for a given area. Thus, for every 100 sites that an operator with 900MHz builds, TM would need to build 200 sites to provide the same level of coverage. Working on approximately 4000 sites over the next five years, the total CAPEX for TM over the next five years will, according to Nash, be R6 billion. In the light of the formula referred to, this results in an overall CAPEX disadvantage of R3 billion. Considering the scenario whereby 4000 sites are deployed gradually over a five year period, the total operational costs (site maintenance etc) will, according to Nash, amount to approximately R2,5 billion. Had only the half of the sites been necessary the OPEX disadvantage would, according to Nash, have been approximately R1,3 billion. The total cost advantage is, accordingly, in the range of R4 billion over the next five years, according to Nash.

[14] According to expert Simon Baker, presented by TM, 900MHz is less affected by signal loss than is 1800MHz. The implication is that 900MHz spectrum can be used to cover a wider area for a given number of base stations than can 1800MHz spectrum. He points out that ICASA in its Draft Regulations also recognises that spectrum disadvantages may provide for an appropriate basis for asymmetric termination rates.[9]

[9] Of course, the 29 October 2010 Regulations also recognise this principle in Appendix B 1.3. However, at the time of argument of this matter, the Regulations had not yet been published. It would, accordingly, not be fair to refer to the final Regulations in his part of the judgment, which deals with the period before 29 October.

[15] The CCC accepts, for present purposes, the above quoted evidence of the TM experts as to unavoidable costs as to spectrum. The problem which the CCC, however, faces is how the amounts stated or broadly indicated, can rationally be supported by the 93c per minute wholesale termination rate. In essence this point was also raised by Cell C. In paragraphs [75] and [76] of its answering affidavit the following is said: "Telkom offers absolutely no justification for this rate. Telkom makes no more than the bald allegation...that the rate of R0.93 'is appropriate' and reflects 'what it would cost Telkom (averaged over 5 years) to run its network on a commercially feasible basis'. Telkom does not put up a single fact to support this assertion....it is astonishing that Telkom should come to the CCC to seek a final and binding order on such an important matter without providing the CCC with any of the necessary facts to evaluate its assertion." It is then suggested in paragraph [77] that it is not believed that TM is able to do so. In fact, Cell C concedes in paragraph [78] that it "has not been able to determine its costs with sufficient accuracy to impose a cost oriented remedy". Ultimately, in paragraph [82], that since TM has not demonstrated that the rate of 93c and not 89c, is the financially feasible rate "its demand...(is)...based purely on its theoretical arguments around asymmetry.." TM, in its reply by the Chief Managing Officer of TM, Mr Maharaj, once again refers to the price taker principle, that it is a new entrant and accentuates the matter of spectrum inadequacy, which he states will lead to its requiring a third more base stations and that this would result in a cost disadvantage of approximately R1 billion.[10] This reply demonstrates that the two parties are approaching the matter from two totally different angles. The approach of Mr Maharaj might be more appropriate in terms of the Call Termination Regulations,[11] where asymmetry in Appendix B is based on two criteria, the second of which, it would appear, could be shown to exist by merely providing the total percentage (less than 25%) of terminated minutes within the relevant market. Since the CCC might be involved in hearing complaints in terms of section 17C of the ICASA Act as to

[10] We have noted the difference between this amount and the amount mentioned by Mr Nash. However, the amount remains substantial. Mr Maharaj, Chief Managing Officer of TM, signed his affidavit on 13 October 2010 and Mr Nash his affidavit on 15 October 2010. That would probably explain the difference. In the light of the decision we have reached, it is not necessary to deal with this aspect further.

[11] Published on 29 October 2010 in GG 33698, Notice 1015 of 2010, after this matter was heard.

what a fair and reasonable rate is in the light of the two criteria mentioned, it would be inopportune to deal with the Appendix criteria further.[12]

[16] In determining whether a rate is reasonable[13] in terms of section 37 of the ECA, the CCC must be provided with facts as to how the 93c will address the unavoidable costs referred two in paragraphs [12]-[15] of this judgment if not in both then, at least, in the area of spectrum where R4 billion was put forward by expert Nash. Essentially, the CCC is confronted with an unsubstantiated estimate by TM, based on the price taker principle, as to the 93c and the relation thereof to the rates agreed to by the industry. To simply take the current trade fee of 89c and 76c as a basis, would not assist. Although those amounts are not in dispute between the parties, the CCC cannot simply accept that the said rates are cost based or orientated. In fact, Cell C has stated in its answering affidavit that it has, up to now, not been successful in determining "its costs with sufficient accuracy to impose a cost orientated remedy." One realises that it may be problematic to make such a forecast, but expert evidence should have been made available to the CCC as to how the 93c would relate to one or both of the categories of unavoidable costs. The R4 billion does assist, but is in itself of little value when the 93c itself must be evaluated in relation to it. As pointed out above, Cell C questioned the 93c on substantially the same ground in its answering affidavit and TM's reply, unconvincingly, remained within the parameters which it had put forward in its founding affidavit. Also Dr Theron's evidence did not provide this missing link. It was, accordingly, not as if TM was not challenged to substantiate the 93c. Cell C did so, but with no convincing answer by TM.

[17] As to CST's it was argued by Mr *Bhana* that since Telkom(fixed line) had already, in terms of its licence, complied with its obligations and is not subject to implementing community service telephones in underserviced areas, there is no reason why TM should only charge 6c per minute for the termination of calls from such phones. Once again, the CCC has not been provided with an expert forecast as to why TM could not absorb this lower rate which is intended to assist in bringing telephony to underserviced areas in the Republic and is in the public interest. Given

[12] See Appendix B read with regulations 7(2)(c) and 9(1).
[13] See note 7 above.

the lack of the said expert evidence, the rate of 93c per minute cannot be regarded as financially feasible or rationally connected to the R4 billion and is, in the CCC's view, unreasonable. The rate of 6c must, accordingly, also apply. Once again, the CCC will let this order cease as from 29 October 2010 when the new regulations will apply.
The Authority has stated in the Government Gazette no 33698 of 29 October page 25: "The Authority determines the following: a. Universal Service Obligations are not to form part of a determination on termination rates for commercial services. These matters are dealt with through separate regulatory processes." Since the final regulations had not been published when this matter was heard, it would not be fair to extend the 6c order beyond the scope of the period before 29 October 2010, since we had not heard full argument on this aspect. However, this conclusion does not imply that the said rate would not still be applicable to TM after 28 October 2010 – whatever the legal source thereof. That is a matter to be argued on another day, if it does come before the CCC.

[18] Although the CCC has no expert evidence on 89c and 76c, the amounts are not in dispute. There is, accordingly, no reason why they may not be charged by Cell C.

[19] In the draft interconnection agreement, TM proposed a clause 3.7 which deals with interconnection bypass. It reads as follows:
" The Parties agree that either Party may send calls destined for the ECN of the other Party to such other Party, regardless of the point of origination of such calls, and may furthermore send any such calls to each other either directly in terms of this agreement or via the ECN of any third party."

[20] TM argued in its founding affidavit that this clause promotes the efficient use of electronic communication networks and services. Cell C, however, states in its answering affidavit that interconnection bypass is not a matter which may be regulated by ICASA or, for that matter, the CCC. The Interconnection Regulations of 9 April 2010 do not, according to Cell C, address interconnection bypass and, accordingly, the matter should be left to commercial negotiation between the parties. Later on in the affidavit, it is stated that the matter should be dealt with by way of a public process in terms of section 4 of the ICASA Act; if it is appropriate to regulate this commercial matter at all. Still later on, in paragraph [91], it is stated that such a clause would not promote the efficient use of the Cell C network. The reason behind the refusal by Cell C is, according to paragraph [93] of the answering affidavit, that

interconnection bypass makes it impossible for Cell C to properly plan capacity and provision links – for example, Cell C might assume one traffic volume from a particular network and end up with much bigger volumes if another operator suddenly decides to send its traffic through another network. Interconnection bypass disrupts the efficient operation of its network. This refusal by Cell C has, according to Cell C, not been demonstrated to be unreasonable by TM.

[21] Given the above seemingly contradictory positions taken by Cell C, Cell C would seem to be vacillating between two, if not three, opinions in one affidavit. If the matter is left to commercial negotiation, the result of such negotiation would have to be part of the interconnection agreement. It is pointed out by Cell C that the Interconnection Regulations of April 2010 do not address interconnection bypass. The CCC could not find any rule against interconnection bypass. It is, however, clear that if such bypass leads to poor quality of service, the licensee which causes such poor quality of service would be in contravention of regulation 7 of the Interconnection Regulations 2010.[14] Regulation 7 lays down standards, the contravention of which could lead to sanctions in terms of section 17E(2) of the ICASA Act, including a maximum fine of R50 000 per contravention. Also see Regulation 8, which provides for contractual remedies, which must be included in the interconnection agreement. Furthermore, Regulation 21(2) permits the agreement to provide for suspension (on limited grounds) where this is necessary to address quality of service degradation of electronic communications networks or services or other material threat to the maintenance of the interconnection. Cell C is, accordingly, not without a remedy in so far as quality of service is concerned.

[22] It would, accordingly, not be unreasonable to include a clause in the agreement which permits interconnection bypass for both TM and Cell C. Of course, Cell C might, nevertheless, not wish to secure such a right for itself. It will then be free to do so. Proposed Clause 3.7 is, accordingly, not unreasonable in our view: the ECA and Regulations do not prohibit bypass and where quality of service is affected, there are sufficient remedies. The matter of unpredictability of volume, even if this argument is accepted, does not, in the CCC's view, carry sufficient weight to deny TM the right to interconnection bypass.

It would be fair to include this right as from 1 March 2011, so that the necessary preparation may be made by both parties.

[14] Published under Government Notice R282 in Government Gazette 33101 of 9 April 2010.

ORDER

1 That TM and Cell C be ordered to charge a wholesale termination rate of 89c (peak) and 76c(off-peak) per minute and TM must charge 6c per minute for CST calls which terminate on its system from Cell C.

2. The afore going order applies from the date that interconnection activities commenced between Cell C and TM and must form part of the interconnection agreement.

3. Clauses 1 and 2 cease to operate at midnight 28 October 2010 when the Termination Rate Regulations 2010 became operational on the 29th October 2010; such Regulations governing the matter as from that date. (No decision is reached as to whether the same rates would not, in any case, apply as from 29 October to 1 March 2011or for CST's in terms of other regulatory processes after that).

4. The agreement between Cell C and TM may include interconnection bypass as proposed by TM. TM is entitled to include this right for itself as of 1 March 2011 in the interconnection agreement with Cell C. If Cell C does not wish to apply such bypass, it may exclude itself from the said clause on or before 1 March 2011. Cell C must confirm with TM's attorneys and the CCC through its co-ordinator if it does not wish to include the right to interconnection bypass, on or before 12:00 Friday 28 February 2011. If no such notice is received, it will be accepted that the clause as presently put forward by TM will apply between the parties. It is taken for granted that the interconnection agreement contains all the obligatory clauses as provided for in the Interconnection Regulations of 9 April 2010. If not, they must be included.

JCW van Rooyen SC

Acting Chairman

31 January 2011

Members Batyi, Tlokana and Ntukwana concurred with the judgment of the Acting Chairman