Vodacom's written submission in response to the Authority's invitation for comments on the Draft Call Termination Regulations

[General Notice 1018, Government Gazette 36919 of 11 October 2013]

INTRODUCTION

Vodacom (Pty) Ltd ("Vodacom") welcomes the opportunity to comment on the Draft Call Termination Regulations ("Draft Regulations") as published by the Independent Communications Authority of South Africa ("the Authority") in Government Gazette No. 36919, General Notice No. 1018 of 11 October 2013.

We further confirm our willingness to participate in any public hearing or further consultative process which the Authority may undertake in this regard.

Our submission is comprised of three parts:

- Part A: General
- Part B: Vodacom's principal comments on the Draft Regulations
- Part C: Vodacom's specific comments on the Draft Regulations
- Part D: Just Administrative Action

Annexure A: Lessons learnt from Europe
Annexure B: Vodacom's Analysis on Disproportionate Impact of Too Low Mobile Termination Rates
Annexure C: The ERG Common Position on the Symmetry of Fixed Termination Rates and the Symmetry of Mobile Termination Rates

PART A: GENERAL

Vodacom supports the Authority's process to further regulate voice call termination rates and supports reductions in voice call termination rates down to the cost of an efficient operator derived from a cost model suitable for an emerging economy like South Africa.

One of the Authority's roles is to regulate the market to *"ensure that access [to communication services] is extended to all the citizens of South Africa"*. The Authority has declared that it adopts the principles of (i) necessity, (ii) effectiveness and (iii) proportionality in the consideration of regulatory policy.[1] These principles suggest that any new regulatory policy should not only be shown to be necessary and effective, but should seek to correct proven market failure through remedies that are proportionate to the ills sought to be cured.

The Government, like the Authority, also recognises that broadband has the potential of creating opportunities and opening new markets that allow businesses to grow. Given the strategic importance of this enabling [broadband] infrastructure, *"the Department of Communications, together with the ICT industry, have committed to delivering 100% broadband penetration and delivering a million jobs by 2020."*[2]

Incentivising investment that accelerates broadband access are therefore defining characteristics of both the Authority and government's objectives.

Evidence suggests that the current regulatory pricing regime (from 2010 to 2013) has, during a time when the number of fixed lines have fallen from 4.4m at the end of 2009 to 3.9m at the end of 2012,[3] delivered a gradual decline in MTRs whilst also providing an environment which has encouraged investment, with mobile operators providing significant network expansion and consequently driving economic growth and employment. For example:

- Vodacom invested R9.5 billion in its network in the financial year ending March 2013, adding 1,752 3G cell sites and investing to attain 601 operational LTE sites in the year.[4]

[1] ICASA website : https://www.icasa.org.za/AboutUs/VisionMission
[2] South African government website - http://www.info.gov.za/aboutsa/communications.htm
[3] The Mobile World : telecoms database
[4] Vodacom Preliminary Results, March 2013

- MTN announced in late 2012 that its EDGE and 3G sites cover 92% and close to 65% of South Africa respectively. MTN invested a total of R2 billion in its network in 2011, resulting in 598 additional 3G sites. A further deployment of 1087 3G sites took place in 2012.[5] [6]
- In 2009, during the current charge control period, Cell C announced that it would be investing R5 billion in a HSPA+ network offering speeds of up to 21 Mbps. Its HSPA+ network already covers close to 92% of the population.[7]
- When Telkom launched its mobile network 8ta (since rebranded as Telkom Mobile) in 2010, Telkom had already constructed 800 base stations across the country. Since then, Telkom has expanded its network to 2067 base stations and its services have been built on an end-to-end all-IP 2G and 3G network, which is upgradable to LTE (4G)[8]. It has re-iterated its focus on its NGN rollout programme in 2013.[9]

However, whilst there has been significant investment in mobile networks – for example, Vodacom's 2G footprint now covers around 99% of the population, and increased rapidly from 43% population coverage in 1995 to 95% by 2005 – further investment is required for next generation infrastructure for data services. It is in this context that the appropriate approach to MTR regulation should recognise the need to set a solid foundation for investment and growth in order to meet its strategic objective of ensuring that *"broadband service providers have sufficient incentive to develop and offer broadband services*".

Vodacom will continue to invest in its network, concentrating on the capacity and quality of its network to carry more traffic as well as the extension of coverage. Vodacom has also made significant progress in simplifying and transforming its tariffs with the explicit purpose of reducing the cost of communicating.

However, investment decisions reflect economic incentives and specifically the investment process exists to ensure that the expected returns from individual projects are not less than

[5] MTN investment presentation, 8th Oct 2012, http://www.mtn.com/Investors/Notices/Presentations/UBS%20SA%20Telecom's%20infrastructure%20day%2017%20October%202012.pdf
[6] MTN Integrated Report, 2012
[7] http://www.cellc.co.za/cellc-news-room/cell-c-is-going-next-generation
[8] **Group Interim Results** for the six months ended 30 September 2012
[9] Telkom SA SOC Limited Group Annual Results, 2013

the (risk-reflective) cost of invested capital. Vodacom notes that significant reductions in MTRs will result in lower revenues and this will have a negative impact on investment decisions.

To the extent that the voice call termination rate reductions are effected, Vodacom appeals that it be done in a manner that does not adversely affect investment and the goal of broadband for all by 2020. Lower wholesale prices may benefit consumers in the short term (to the extent that reductions in wholesale prices translate into lower retail prices). However, if such prices are reduced too fast, it may reduce incentives for operators to invest in new technology and infrastructure and detrimentally affect consumer welfare in the medium to long run. Experience from Europe where there has been a highly interventionist regulatory regime shows a significant deterioration in industry investment and the Authority must learn from these regulatory failures and avoid a repeat of the same mistakes in South Africa.

[Please refer to **Annexure A**: Lessons learnt from Europe]

On reflection, the 2010 MTR reductions were significant and triggered considerable cost containment initiatives within Vodacom in an attempt to minimise the overall impact on its financial performance. Because of the gradual glide path that was allowed, these initiatives could be planned and managed in a manner that did not result in job losses or significant change in Vodacom's investment plans.

Vodacom had anticipated further reductions in MTRs and Fixed Termination Rates (FTRs), but not on the scales proposed in the 2013 Draft Regulations. The main areas of concern are:

- the levels of MTR declines;
- asymmetry;
- the proposed target MTR;
- the absence and lack of consultation on the Bottom-up Long Run Incremental Cost ("BULRIC") model;
- the steepness and duration of the proposed glide path; and
- unchanged FTRs and the proposed MTR/FTR differential.

The proposed MTR reductions do not provide Vodacom with the same (2010) opportunity to gradually align its business with the proposed MTR/FTR regime. The short term impact of what is proposed is so significant that it will necessitate more drastic action and it will put pressure on Vodacom's pricing transformation, capital investment plans as well as cost containment programmes. The proposed Draft Regulations will hamper industry investment and innovation, especially in delivering mobile broadband nationally, with huge consequences to the gap in the provision of communications services to urban and rural communities,

In a market characterised by:

- low population density, standing at 154th in the world with 42 people per square km;
- a high proportion of its population living in rural areas, for example, 38% of its population lives in rural areas compared with 17% in Kenya and 26% across the EU;
- a significantly skewed distribution of wealth, with the highest degree of income inequality globally; and
- household fixed line penetration in South Africa of 14.5% compared with, for example, 71% in the EU;.

marginal projects, in respect of next generation infrastructure investment to meet broadband objectives, may be disproportionately impacted in poorer and more rural areas as these become financially unviable for the operators.

To explore these issues, Vodacom has undertaken analysis to understand the potential sensitivity of investment incentives with respect to MTRs. Specifically, the following was considered:

1. The relationship between fixed line penetration in rural areas, and income levels.

2. Analysis at a cell site level of the contribution of mobile termination to total revenues, and how this may vary in different parts of the country.

3. The importance of MTRs as part of the revenue generated by low users groups.

[An extract out of the aforementioned analysis is attached hereto as **Annexure B**.]

In conclusion, Vodacom recommends that an MTR/FTR regulatory regime should:

- encourage infrastructure investment and sector development to the benefit of the wider community;
- set cost based target rates after consultation on a bottom-up long run incremental cost (BULRIC) plus model;
- allow reasonable time for licensees and customers to adjust to new target rates through a gradual glide path; and
- set symmetrical termination rates within the same sector (i.e. mobile sector and fixed sector respectively). However if asymmetry is allowed within a sector, it must be reasonable, objectively justified and limited to the short term and should not increase dependency and prolonged inefficiencies.

PART B: PRINCIPAL COMMENTS

As indicated under Part A above, Vodacom has identified five main areas of concern on the Draft Regulations. Vodacom will set out its principal comments in respect of each of these concerns in detail below.

1. Asymmetry

The 2010 Regulations[10] determined that asymmetry for a transitory period will benefit total social welfare and that it must be limited and reduced to ensure that investments by new entrants are efficient. These determinations were in line with international best practice where the overwhelming evidence is that asymmetry is phased out over time and the level reducing towards the MTR target rate.

Figure 1: Country count by asymmetry *versus* symmetry MTR regimes[11]

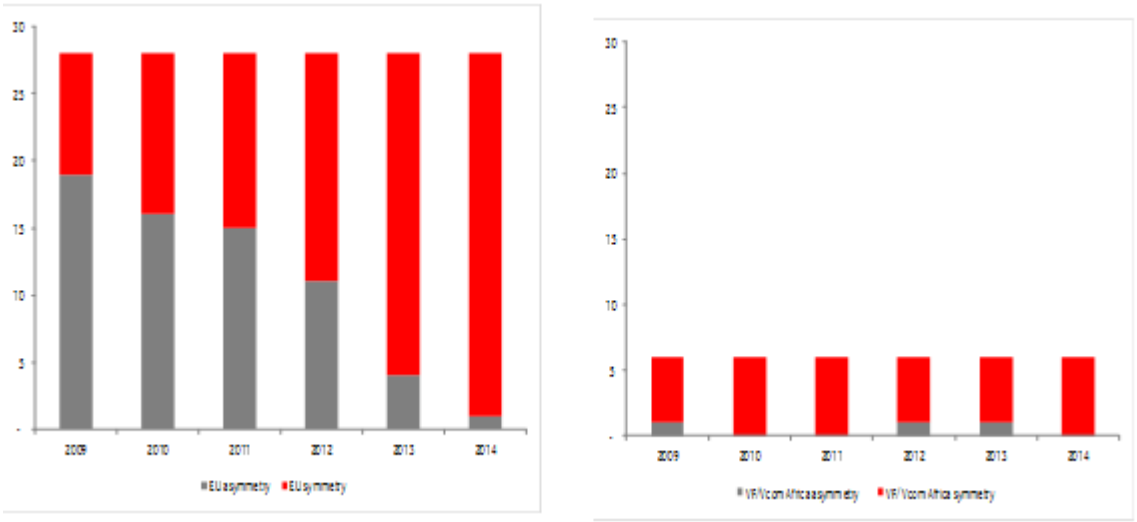


Figure 1 above indicates that asymmetry is being phased out in Europe and in the Vodafone/Vodacom African markets asymmetry was phased out in Mozambique. It is only in Ghana where asymmetric rates were recently introduced under very narrow circumstances,

[10] Call Termination Regulations and Explanatory Notes on the Call Termination Regulations, General Notice 1015, Government Gazette 398 of 29 October 2010.
[11] Vodafone data, GSMA, Cullen International

i.e. it only applies to new entrants as well as operators with less than 5% subscriber market share, for a maximum period of 24 months or when market share exceeds 5% whichever comes first and at a maximum level of 20% and 10% for the 1st and 2nd year respectively.

Figure 2: EU asymmetry levels[12]

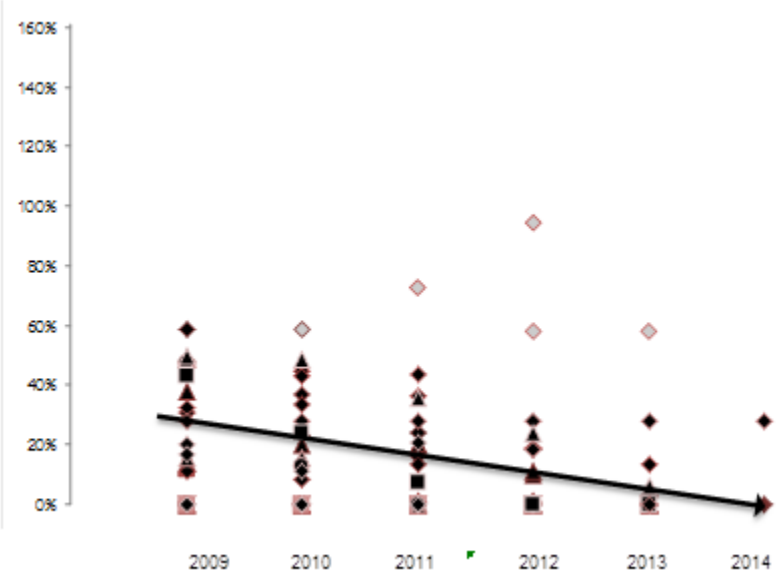


Figure 2 demonstrates that not only is asymmetry being phased out; the level of asymmetry is also reducing with the exception of certain outliers. In terms of figures 2 and 3, the EU member states with asymmetric MTR regimes amount to a count of 19, 16, 15, 11, 4 and 1 from 2009 to 2014 respectively.

[12] Vodafone data, GSMA, Cullen International

Figure 3: Average asymmetry levels towards end point[13]

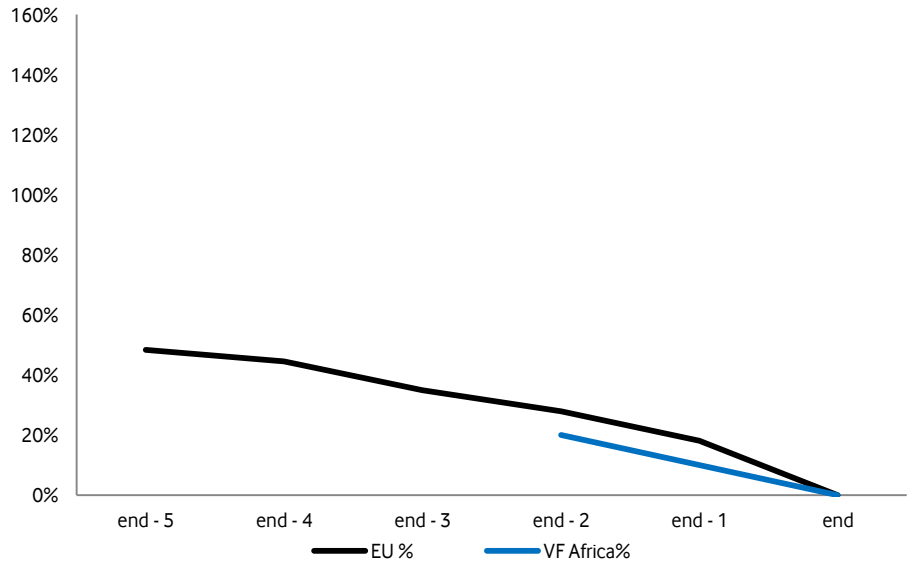


Figure 3 demonstrates that as asymmetry approaches the end-point, the level is reduced in an attempt to gradually move towards symmetry. Vodacom is of the view that the Draft Regulations deviate from the aforementioned 2010 principles and go against international best practice that raises a number of concerns, namely:

1.1. Asymmetry to supplement termination rate reductions

Paragraph 5.8 of the Explanatory Notes to the Draft Call Termination Regulations ("Explanatory Notes") frames asymmetry as a necessary supplement to voice call termination rate reductions to better address alleged continued market failure. It is not clear which market is being referred to in relation to market failure and how the Authority arrived at this conclusion.

Ignoring these ambiguities, Vodacom disagrees with the notion that termination rate reductions will not be sufficient to address the alleged continued market failure. Unjustified additional remedies risks dis-proportionate "over-regulation".

[13] Vodafone data, GSMA, Cullen International

Vodacom further notes that Cell C lodged a complaint with the Competition Commission regarding on-net/off-net price differentials, Vodacom therefore also cautions against parallel interventions by the Competition Commission in relation to on-net/off-net differentials, to the extent that the Authority does not itself intervene and affirm the acceptability of such differentials. Uncoordinated parallel interventions may further compound the effect of asymmetry and distort competition.

1.2. Reintroduction and significant (further six year period)/indefinite extension

A critical success factor for this form of entry encouragement[14] is commitment by the Authority to a fixed time period. It is critical because of the importance of the regulatory signal to late entrants that entry assistance will be limited and they will have to be become efficient and achieve scale during this limited period. It is also important for the regulatory signal to other licensees who need certainty around the duration of these subsidies that may distort competition in the retail market.

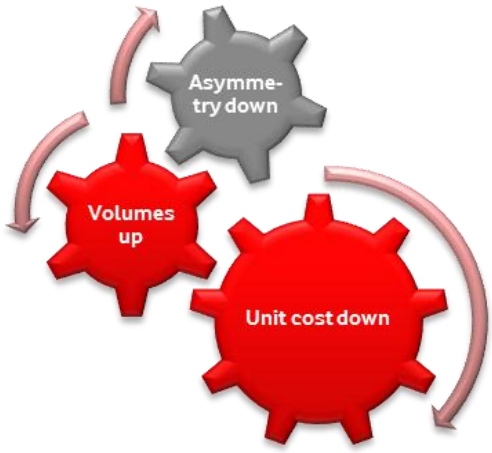
The 2010 regulatory signal was that 3 years would allow adequate time for smaller licensees to compete more strongly and any operator to bring down its cost to more efficient levels. The 2010 Regulations and Explanatory Notes acknowledged and captured this fundamental by confirming that asymmetry must be temporary and decreasing and if allowed for too long it could support inefficiency. The Draft Regulations propose a significant deviation from the 2010 position through the reintroduction and significant/indefinite extension that opens the door for the risks associated with a loosely managed intervention of this nature.

The risks that may materialise as a result of this deviation may not have been properly considered by the Authority and tested to be in consumers' interest.

[14] ERG Common Position on the Symmetry of Fixed Termination Rates and the Symmetry of Mobile Termination Rates

1.3. The significant increase in the level of asymmetry goes against the grain of the qualifying criteria and is exceptional in recent times

Figure 4: Relationship between; volumes, unit costs and asymmetry



Both the qualification criteria of spectrum and economies of scale, in the context of unit cost, should result in a reduction in unit cost of an efficient operator over time. The 2010 regime accurately aligned the level of asymmetry with this phenomenon through a decrease in the level of asymmetry over time and the intention to bring it to an end. The Draft Regulations, on the other hand, deviate from the 2010 position and principle through the proposed reintroduction and significant increase in the level of asymmetry.

Figure 5: Average asymmetry levels towards end point[15]

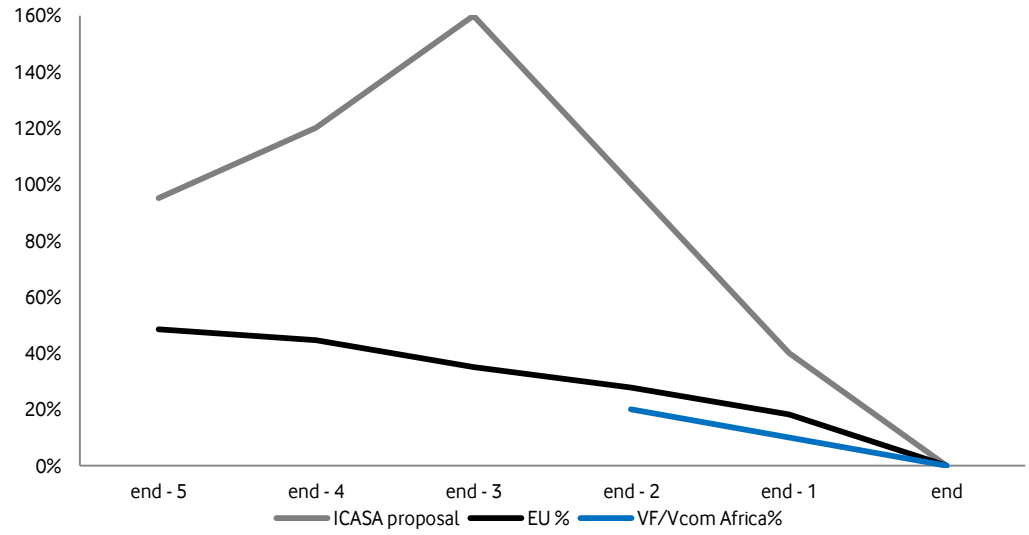


Figure 5 captures the levels of asymmetry per the Draft Regulations with the levels of asymmetry observed in those EU states and Vodafone/Vodacom African markets where asymmetry was phased out over the last 5 years.

The aforementioned deviation may be indicative of an unjustified high level of asymmetry that opens the door for the risks associated with a loosely managed intervention of this nature.

1.4. Actual cost disadvantage due to current spectrum allocation

Vodacom submits that MTN, Cell C and Vodacom all have access to an equal amount of spectrum in the 900MHz and 1800 MHz bands, therefore asymmetry for Cell C on this criterion is not justified. Vodacom contends that on the basis of spectrum assignments, only the case of Telkom Mobile's spectrum assignment warrants consideration for external cost differentials on a forward looking basis. It is however Vodacom's view that the perceived unit cost disadvantage in Telkom Mobile's case, due to a lack in low band spectrum, is largely negated due to the significant influence

[15] Vodafone data, GSMA, Cullen International

that matters such as unique network roll-out obligations, national roaming, network sharing, etc. may have on actual network topology and the associated lack in economies of scale. Network roll-out are likely to be focussed on traffic dense areas, where scale and scope disadvantages will be minimal, whilst national roaming serves the remaining areas that are less attractive from a network build perspective. It should also be noted that Telkom Mobile has access to significantly more high demand spectrum than the other mobile operators.

The level of asymmetry informed by perceived spectrum related cost differentials may not be justified when considering actual network cost differentials.

1.5. Actual cost disadvantage due to economies of scale and scope

Another critical success factor for this form of entry encouragement[16] is a guarantee by the Authority that the level of asymmetry is less than the cost differential. This is important to ensure that the subsidy is contained to the actual higher unit cost of late entrants in an attempt to promote efficiency. Anything more opens the door for the risks associated with a loosely managed intervention of this nature.

Unique network roll-out obligations, sharing, national roaming, modern equivalent assets, access to Telkom's fibre network and other network buildings and facilities by Telkom Mobile etc. may significantly reduce, if not eliminate, the perceived unit cost disadvantage due to a lack in scale. Based on Vodacom's calculation it is likely that the Authority may find that the opposite is true where late entrant's unit costs are below/the same as that of others for the reasons mentioned. It is therefore important that these factors be duly considered and incorporated in the Authority's assessment of the actual cost differential.

In the absence of a robust cost model, the level of asymmetry informed by economies of scale may not be representative of the actual unit cost disadvantage. This concern is

[16] ERG Common Position on the Symmetry of Fixed Termination Rates and the Symmetry of Mobile Termination Rates

amplified by the proposal to keep market shares static for a period of 5 years. As actual market shares move from the December 2012 level, cost differentials will gradually move from the level of asymmetry and asymmetry will become inefficient.

The significant/indefinite extension of asymmetry also contradicts economies of scale as qualifying criterion. To the extent that the period is informed by lack in economies of scale, the period should capture the time it takes an efficient operator to achieve scale, which should be temporary and around the time of entry. The proposed extension fails to accurately reflect on this requirement due to an over reliance on market share as a proxy for economies of scale. This disconnect between the period and qualifying criteria may indicate that the proposed period is unjustified.

Vodacom finds it difficult to establish a logical link between the level and period of asymmetry and the qualifying criterion of economies of scale. The absence of such a logical link raises questions regarding the real purpose behind the relevant interventions.

1.6. Proportionality and fairness of the substantial difference between asymmetry granted in Market 1 *versus* Market 2

The proposed outcome where the level of fixed asymmetry remains static over a significant period is questionable for the same reasons mentioned under paragraphs 1.1 to 1.6 above. Specifically the fact that economies of scale and scope is the only qualifying criterion and based on paragraph 1.6 above, static FTRs and levels of asymmetry go against the grain of economies of scale and scope where traffic (even if only data traffic) is increasing.

The substantial difference in the level of asymmetry between Mobile *versus* Fixed further highlights the excessiveness of the level of Mobile asymmetry

In the absence of a robust cost model, the significant difference in the levels of mobile and fixed asymmetry and the static fixed level applying for 5 years or even indefinite may not be justified based on the actual cost differentials.

1.7. No transparency on the objective basis of the proposed amended pro-competitive measure.

The Draft Regulations do not set out what changes in the competitive nature of the market warrant the significant modification of asymmetry in Market 1 to ensure proportionality. The reasonable grounds, facts and information that form the objective basis of this decision are further not transparent. In addition, the proportionality and fairness of the proposed determination on asymmetry in Market 1 is also questioned, based on unsupported and significant different treatment of the fixed and mobile voice call termination markets as well as the exceptional and substantial subsidisation required by the imposed levels and extended period of asymmetry that may promote inefficiencies.

1.8. Lack of a transparent and public process by which licensees will apply and be assessed for asymmetry

The Draft Regulations provide no detail on the process that will be followed by licensees to apply for and justify their compliance with the qualifying criteria.

The outcome of a process that lacks consultation and transparency may not be properly and objectively informed.

Vodacom recognises that entry encouragement assistance *via* asymmetry used to be common regulatory practise. Regulators have acknowledged the benefits of this form of intervention where properly justified and limited and have also acknowledged the significant downside where not properly managed. Vodacom is not convinced that all the important matters are properly managed by the Authority, more specifically the proposed deviation

from the 2010 sunset commitment and the lack of evidence that the proposed levels of asymmetry does not exceed the actual cost differential. Since late entrants managed to successfully grow market share during the 2010 regime there should be no need to drastically deviate from the 2010 position. If not carefully managed, asymmetry will be accompanied by the following risks:

- if not correctly applied, asymmetry could amount to regulatory support for inefficient operators, resulting in customers of one operator cross-subsidising customers of the new entrant;
- the advantage created may reduce the new entrant's incentive to innovate, as they may become increasingly reliant on higher MTRs to maintain profitability rather than trying to compete more effectively, which will likely lead to market distortions;
- where high asymmetrical termination rates are allowed, which makes-up a part of the cost of an off-net call, it may lead to higher off-net tariffs for calls to these operators. Examples of such tariffs are the current differentiated charges being levied by Telkom for calls to MTN and Vodacom as well as to Cell C and Telkom Mobile;
- prolonged asymmetry creates a safety blanket that would be difficult to unwrap and might act as a disincentive for efficiency gains and result in a distortion of competition. In this regard, the European Commission[17] expressed the view that: "*the fact that an MNO entered the market later and has therefore a smaller market share can only justify higher termination rates for a limited transitory period. The persistence of higher termination rates would not be justified after a period long enough for the operator to adapt to market conditions and become efficient and could even discourage smaller operators from seeking to expand their market share*"; and
- it can prevent industry from reaching its efficient structure by artificially supporting inefficient operators. Smaller operators are in a sense penalised if they become more efficient, invest in their respective networks and succeed in growing their market share, as they will lose the benefit of receiving substantial asymmetry; and
- it can distort competition in the retail markets.

[17] Reference: Google Case BE/2006/0433, Case FR/2006/0461

[Please refer to **Annexure C** for the European Regulators Group common position on the symmetry of termination rates.]

Vodacom recommends that the Authority adheres to the 2010 principles of phasing out asymmetry in favour of symmetric rates. If this proves inadequate, further wholesale interventions could be considered subsequently. However, should the Authority now be of the view that asymmetry should be extended; such extension can only be justified if it is used for the unwinding of the current level over the short term. In addition, an impact assessment should be conducted by the Authority in order to ensure an efficient outcome and the qualifying criteria for asymmetry need to be applied to all operators on a case by case basis by means of a transparent public and consultative process.

2. The target MTR and proposed levels of MTR decline

Vodacom is of the view that the publication and targeting of unsubstantiated values, which is subsequently to be informed by a diligent cost model, would have detrimental consequences. More specifically, Vodacom is concerned with the following aspects of the proposed target MTR, namely:

2.1. No transparency on the reasonable information that form the objective basis by which the R0.10 was calculated and what it represents

As there is no transparency on the facts and information that forms the objective basis of the determination, Vodacom cannot assess the basis on which the R0.10c was calculated and what it represents, i.e. is it the cost of an average efficient operator today? The robustness of this calculation and its outcome is consequently questioned.

2.2. The proposed target MTR is insufficiently informed with a risk of it being set at the wrong level

The appropriate manner for setting termination rates is by way of cost modelling. The 2010 Regulations and Explanatory Notes acknowledged the superiority of cost models and a cost model supplemented with accounting separation and cost accounting, plus

specific additional cost modelling on voice call termination was planned for the 2013 review. These actions would have facilitated more certainty on the cost of termination and reduced the risk of error that is currently being faced. Without a cost model there is a great risk of getting the target charge wrong.

2.3. The target MTR of R0.10c is too low for South Africa

The target MTR of R0.10c is too low for South Africa where extensive further investment on mobile networks is still required, especially to provide wireless broadband that is the most cost effective option. This may have an impact on millions of mobile customers benefiting from wide coverage and low cost of ownership and access.

MTRs that do not allow for sufficient recovery of costs may risk:[18]

- the exclusion of some low-usage and low-income customers;
- unfair benefit to fixed-line customers; and
- reducing the incentives for operators deploying mobile solutions to invest in new technologies and infrastructure to the detriment of consumers and the broader community in South Africa in the long run.

In addition, too low a rate will deepen the digital divide. [In this regard, please refer to **Annexure B**]

Vodacom submits that the appropriate manner of setting termination rates is informed by diligent cost modelling and an impact assessment. The target MTR should be based on a cost standard that considers consumer interests, particularly those depending on the provisioning of mobile Information Communication and Technology (ICT) services across the country (including underserviced areas), as well as innovation and infrastructure investment required for delivering of broadband to all.

[18] Ofcom Wholesale Mobile Voice Call Termination Market Review, page 201

As the proposed target MTRs and FTRs are not cost based, Vodacom recommends that the Authority should in the interim; impose 'reasonable' termination rates in order to ensure that operators are able to recover their efficiently incurred costs of termination and allow a reasonable return on investment. The World Bank Cost Model Guidelines[19] confirms this approach in the following extract:

"*It is therefore, crucial to ensure that, when a mistake is made, it is made in favour of overinvestment rather than underinvestment.*"

Vodacom further recommends that the Authority proceeds with the consultation on a (BULRIC) model and key pricing parameters and appeals that adequate time be allowed for the development thereof as the proposed target MTR is not cost based.

3. Absence and lack of consultation on the BULRIC model

Vodacom is concerned with the lack of consultation on all the associated complexities of the proposed BULRIC model, such as cost standard, period, operator, etc.

Vodacom recommends that the Authority proceeds with the consultation on a BULRIC model and the associated complexities and appeals that adequate time is allowed for the development thereof. It would therefore be premature for Vodacom to elaborate in detail on all the associated complexities since it falls outside the ambit of this consultation process.

With regards to the optimal cost standard for the South African mobile market, Vodacom is of the considered view that the Authority should adopt LRIC plus, as the appropriate cost standard for the following reasons:

- it allows for the recovery of efficiently incurred costs and therefore provides an investment incentive;
- it reflects economies of scale and scope and therefore exhibits strong cost orientation characteristics; and

[19] A Model for Calculating Interconnection Costs in Telecommunications, The World Bank, page 21.

- it provides appropriate forward looking market signals to new entrants.

Pure LRIC is not recommended based on the following:

- it does not allow for full cost recovery;
- it will increase the proportion of cell sites that are unprofitable;
- it may dampen profitability and reduce investment incentives to the detriment of consumers;
- next generation infrastructure investment required to meet broadband objectives may be disproportionately higher in poorer and particularly rural areas where there is a higher weighting of incoming calls in relation to outgoing traffic;
- it discourages infrastructure investment in rural areas with huge consequences to the gap in the provision of communications services to urban and rural communities; and
- it will affect lower income users who are over represented in rural areas.

It must be noted that the above reasoning is not complete and Vodacom will comment in detail during the relevant consultation.

4. Steepness and duration of the proposed glide path

Although the final rates may be uncertain, any changes to termination rates should be done based on a glide path that allow operators to adjust their respective business models and that of their respective distribution channels, which may be affected by adjustments in the market. Vodacom submits that the target rate should however be certain before it is possible to determine the impact or appropriateness of a glide path. Vodacom did not anticipate a reduction in termination rates as steep as the proposed 50% reduction in MTRs in the first step of the glide path or as inequitably as proposed in the Draft Regulations. Vodacom submits that an overall proposed reduction of 75% in 730 days is too aggressive. The extract of the study below, although developed for the country of New Zealand, supports this view.

Figure 3: Characteristics of glide paths employed by various Regulators[20]

Table 1 Summary of glide path characteristics.

Country	Total MTR % Change	Average % reduction per drop	Average days between drops	Total number of drops	Total duration (days)
Australia	60	17	274	5	1,095
Austria (1)	69	13	191	7	1,527
Austria (2)	55	15	143	5	716
Belgium (1)	48	15	173	4	690
Belgium (2)	88	39	229	4	916
Denmark	34	13	365	3	1,096
France	61	26	334	3	1,001
Hungary (1)	56	13	366	6	2,193
Hungary (2)	30	16	274	2	548
Netherlands (1)	38	15	343	3	686
Netherlands (2)	84	28	197	5	787
Norway (1)	48	9	249	7	1,746
Norway (2)	70	20	165	5	827
Sweden	47	14	273	4	1,090
UK	30	10	310	3	930
Median	**55**	**15**	**273**	**4**	**1,001**
Draft STD	**73**	**73**	**n/a**	**1**	**0**
Final Report*	**70**	**45**	**365**	**2**	**365**

* Average of upper and lower bound MTR benchmarking.

Glide paths are normally used by Regulators to allow operators time to adapt their business models, to adjust to new pricing levels as well as ensure that operators are not subject to price shocks that may disrupt pricing, profitability and consequently corporate decision making. Glide paths also assist regulators to strike a balance between the short term welfare gains of immediate price reductions against the protection of investment incentives.

Most regulators are mindful of the risks of an adverse effect on investments (which are typically planned and assessed with reference to forecast returns over a multi-year timeframe) as an outcome of sudden price shocks and the disruptive impact on operators that such shocks can bring.

Vodacom notes that the proposed glide path will have the following impact:

- business plans will be disrupted as it will be impossible to re-plan and adjust commitments;

[20] Mobile Termination Glide Path Benchmarking, Covec, 7 February 2011

- Vodacom will not be able to invest at the same level as intended due to the significant shortfall that will result and was referred to under Part A above;
- medium to long term commitments with suppliers and distribution channels will lead to unavoidable losses as they cannot be amended on such short notice; and
- there will not be sufficient time to appropriately consider the re-deployment of staff in order to achieve improved efficiencies and decrease the cost of service delivery.

Vodacom submits that the market conditions that justified the imposition of a glide path in the 2010 regulations still currently exist, namely to allow operators time to adapt their business models, to adjust to new pricing levels as well as to ensure that operators are not subject to price shocks. For this reason the Authority is commended for the decision to make provision for a glide path, however Vodacom appeals that the steepness of the reduction be adjusted to a more reasonable level with specific reference to the first step.

5. Unchanged Fixed Termination Rates and the proposed MTR/FTR differential

Vodacom is concerned with the following aspects of the proposed target FTR, namely:

5.1. No transparency on the cost of fixed termination

The cost of mobile termination was estimated (albeit in a manner that Vodacom disagrees with) at R0.10 whilst no such estimation/determination is made for fixed.

5.2. No transparency on the basis by which it was determined that there is no need to change the rates for fixed

As there is no transparency on the facts and information that forms the objective basis of the determination, Vodacom therefore cannot assess the basis on which the cost of FTR was calculated and what it represents. The Authority's determination that FTRs remain unchanged is surprising, because data traffic on fixed networks would have increased and the cost of network equipment has reduced post the 2010 intervention. The robustness of this calculation and its outcome is questioned.

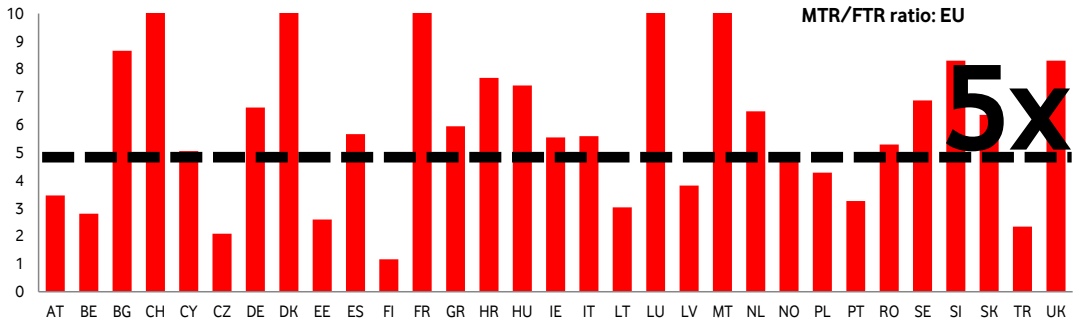
5.3. The proposed target FTR is insufficiently informed with a risk of it being set at the wrong level.

The target FTR is not based on the cost of an efficient operator given that it is not informed by a robust cost model. Further, the Authority found both markets for wholesale voice call termination to be ineffectively competitive and yet did not amend the pro-competitive terms and conditions for Market 2, when those for Market 1 have been amended.

Vodacom also observes with concern that the Authority intends to set the target MTR lower than the target FTR, which is not in line with the likely outcome of regulatory cost models for fixed and mobile respectively and international practice where MTRs are set well above FTRs.

The graph below captures the differential between MTRs and FTRs for EU states based on information published by Cullen International. FTRs represent a local average call where call-set up was considered based on a 3 minute call. Based on this analysis MTRs are significantly above FTRs, which is on average five times higher.

Figure 6: EU MTR/FTR differential



This ratio is unsurprising given the significant difference in cost structure between fixed and mobile networks. In both cases the majority of cost is in the 'access' network.

In the case of fixed this is the network of copper loops. In the case of mobile this is the network of base stations. Copper loops are dedicated to specific users and are not included in the cost of voice services. Base stations are infrastructure that is competed for by multiple users and are included in the cost of voice services. The appropriateness of this is best explained by way of an analogy. If all the customers of a fixed network double their number of calls/minutes there wouldn't be any additional investment in copper loops. This shows that the cost of copper loops is not causally related to the provision of voice services. If all the customers of to a mobile network would double their number of calls/minutes the number of base stations would increase significantly. This shows that the cost of base stations is causally related to the provision of voice services. This is the fundamental reason why termination rate regimes which are based on cost-orientation principles always result in FTRs that are significantly lower than MTRs.

Vodacom reiterates and recommends that the appropriate manner of setting termination rates is by way of diligent cost modelling.

PART C: SPECIFIC COMMENTS ON THE DRAFT REGULATIONS

Vodacom's representations under Part C below move away from general and principle comments into the substance of the regulations. Comments are provided in the same order and with the same numbering as set out in the draft regulations (Notice 1018 of 2013).

1. Definitions

Mobile voice call termination service:

Vodacom submits that although the proposed definition is identical to the definition included in the current Call Termination Regulation, it requires clarification and the Authority should consider the following definition:

'means a wholesale voice call termination service provided by an ECNS or ECS licensee to mobile subscriber equipment enabled by wireless technology that offers full call handover',

In addition, the following definition for 'full call handover' is proposed: 'means a service that allows a subscriber to initiate, receive and continue a voice call for the duration of that call, despite any change in location.'

The proposed amendment to the definition and introduction of the definition of 'Full call handover' is in line with paragraph 2.2 of the Authority's *Practice Note on the implementation of the asymmetry provisions of the Call Termination Regulations* dated 28 January 2011. Vodacom is of the view that to avoid ambiguity going forward it is more appropriate to include such clarification within the proposed definition.

Retail service:

Vodacom is of the view that the definition as per the ECA should apply.

2. Purpose of Regulations

Regulation 2(d)

Vodacom agrees with the stated purpose of imposing pro-competitive measures to remedy market failure. As this is a review of pro-competitive measures in terms of section 67(8) of the ECA, the purpose of this regulation should also be to assess whether the current pro-competitive measures are proportional and whether such measures should be modified to ensure proportionality and Vodacom therefore contend that the provision should be amended accordingly.

3. Market definition

The categorisation of markets into Market 1 and 2 is misleading because it may create the perception that there are only 2 markets, i.e. a mobile market and a fixed market. It is therefore proposed that the categorisation be eliminated and that the 4+ mobile markets and 20+ fixed markets be listed and appropriately named.

Regulation 3(a)

Vodacom submit that the reference to "mobile location" should be amended to be in line with our representations on the definition of mobile voice call termination service above.

Regulation 3(b)(i) and (ii)

Fixed geographic services

The introduction of "within 0N" and "between 0N" fixed termination rates in 2010 relied on the expectation that it will be financially and technically feasible for points of interconnection to take place at the 0N level and that a request for such a point of interconnection may not be refused in those geographical areas where it is possible. This expectation did not materialise in practise because most of the new entrants (VoIP operators) have not rolled-out points of interconnection (POIs) in the five different regions identified by ICASA, but have in most instances rolled out one POI, that being in Gauteng region.

This *status quo* causes operators to pay more for outgoing calls to these new entrants because of inefficient routing to "one" POI plus the higher "between" rates adopted by these licensees. Not only do the originating operators pay the higher termination rate, they also make use of their own transmission facilities to get the call to the single interconnection point.

ICASA should consider reviewing the termination rate regulations for fixed geographic services with respect to regional interconnection, as the theory behind the differentiation of within and between rates for geographic numbers does not apply in practice, due to points of interconnection not being rolled out in every region with every operator.

In addition, Vodacom contends that the fixed voice call termination market/market segments have not been appropriately defined because the between 0N area code segment incorrectly widens the call termination market through the inclusion of interregional transit. This erroneous inclusion is due to the fact that the interregional transit market is a competitive market (i.e. between 0N area code segment) whilst voice call termination market (i.e. within 0N area code) is a non-competitive market. Vodacom submit that the proposed market segmentation and the treatment of each segment need to be reconsidered. Vodacom is of the view that in respect of geographic fixed services the segmentation of between 0N area code and within 0N area code should be removed and provision should only be made for the regulation of the non-competitive within 0N area code segment.

Fixed non-geographic services

In the South African telecoms market, neither fixed non-geographic numbers nor mobile numbers are linked to a specific area code. However, unlike mobile numbers, termination rates to fixed non-geographic are not strictly regulated and licensees have the freedom to negotiate the termination rate within the range of Within and Between 0N area rates. Operators thus far have, unsurprisingly, generally chosen the maximum rate, i.e. the asymmetric between 0N rate that is currently R0.21.

This benefit of selecting a rate that is higher than the rate determined for geographic numbers incentivises operators to circumvent the use of geographic numbers for fixed geographic services.

Vodacom has tolerated this situation since 2011, but submits that a market review of the fixed market and its variety of services is required so that some normalisation and fairness is achieved in these markets. Therefore a market review and costing exercise is required to determine whether there are different markets, and whether there are any grounds for different rates albeit it may only be marginal differences.

In the absence of a review of the fixed voice call termination market and appropriate interventions, Vodacom recommend that the Authority provide for a single FTR set at the within 0N area level.

4. Methodology

Regulation 4

The draft regulations are not transparent on the methodology used to assess effectiveness of competition. Transparency on the methodology is necessary as a consistent approach is required to ensure that the competitive nature of the market during a review is assessed using the same methodology as during the initial review. It is likely that applying a different methodology during a review will lead to a substantially different outcome. Regulation 4 repeats the factors to be considered as provided for under section 67(4) of the Act; however this Regulation and the Explanatory Note do not provide transparency on how these factors were applied nor on the findings in respect thereof.

The current draft Regulation therefore does not assist in assessing whether a consistent approach in relation to the 2010 review was applied, which is required to inform the competition assessment and the need to modify pro-competitive conditions to ensure proportionality.

5. Effectiveness of competition

Regulation 5

Vodacom submits that the Authority has merely recited the provisions of sections 67(6) of the ECA. This does not in any measure or form sufficiently discharge the Authority from the burden of setting out how these tests were applied to reach the conclusion that competition is not effective owing to inefficient pricing. In addition, the criteria to consider when assessing the effectiveness of competition in the market is provided for in terms of section 67(6)(b) and must be considered and applied.

Vodacom recommends that the Authority should use a methodology prescribed in the ECA in order to address any market failures in markets that it finds to be ineffectively competitive. It is not clear on which legal basis the Authority relied with respect to the use of only inefficient pricing as the basis for a finding that the market is not competitive. It is further uncertain whether inefficient pricing refers to wholesale or retail pricing – it is assumed that the finding was made on the relevant wholesale market. As the current wholesale rate has been set by the regulator, it is not possible for operators to implement more efficient pricing without a review of the relevant market and before due process has being followed

Vodacom questions the Authority's measurement of the level of concentration in a market that has not been defined, i.e. the collective market for mobile voice call termination. Since all licensees hold 100% market share in the relevant market it is not clear what the rational is for measuring the level of concentration.

In addition, in terms of section 67(8) the Authority needs to assess the competitive nature of the market and must modify the applicable pro-competitive conditions to ensure proportionality due to changes in the competitive nature of the market. The Draft Regulations and Explanatory Notes do not provide reasonable grounds that inform the basis of the determination and further does not set out which changes in the competitive nature of the market warrant modification of pro-competitive remedies to ensure proportionality.

6. SMP determination

Regulation 6

Vodacom has no comment on this regulation.

7. Pro-competitive Terms and Conditions

Regulation 7(1)(a)

Vodacom's representations in respect of the finding of 'inefficient pricing' under Regulation 5 above refer.

Regulation 7(2)(a)

Vodacom hereby refers the Authority to Vodacom's comments relating to fair and reasonable pricing under paragraph 1.1 of Appendix A of the Draft Regulations.

Regulation 7(3)(a)

In 2010, the criterion relating to spectrum in respect of the imposition of additional pro-competitive conditions read as follows "*Licensees that have historically benefitted from the allocation of more efficient lower band spectrum*" whereas the Draft Regulations has now amended this provision to read "*Licensees that have historically benefitted from reciprocal treatment by the Authority in the allocation of spectrum*". Vodacom notes this inconsistency and confirm that it is not clear what reasonable grounds, facts and information inform the objective basis for this amendment. In addition, it is not clear what spectrum allocation ICASA is referring to in this provision.

It further is uncertain what "reciprocal treatment by the Authority" entails and why it would justify the imposition of additional pro-competitive conditions that are forward looking in nature. Vodacom is nevertheless of the view that it has not benefited from reciprocal treatment by the Authority in the allocation of spectrum and therefore does not have this characteristic and should be excluded from regulation 7(4)(a).

Vodacom recommends the insertion of the word "and" after the semi-colon to clarify that both factors apply cumulatively.

Regulation 7(3)(b)

Vodacom's comments under Parts B, paragraph 1.6 refer.

The basis for the decision on the differentiator of 20% market share is not clear and should be transparent. It remains unclear whether the basis for the decision was drawn from a review that proved that markets with less than 20% market share actually do not benefit from economies of scale.

Vodacom submits that there is no alignment between the share of total terminated minutes in the respective markets and the market definition. The market has been defined as termination on individual networks however the remedy proposed speaks to the entire termination market, which is a new market which the Authority has not defined through a market definition process as envisaged in section 67(4)(a) of the ECA. Further, Vodacom contend that all licensees have 100% share of the total terminated minutes in the relevant market and all licensees should therefore be included under 4(a) and (b).

In addition the equation term "*a share of total minutes terminated in the respective markets*" is not clear, as this could be construed as a share of total minutes terminated that arises only from operators active in the mobile market, or arising from all operators including fixed nationally or even international operators, or roaming traffic arising from the operator's own customers roaming internationally or nationally. The Authority needs to be more specific about its remedy and whether the 20% decision was based on only one of these call scenarios, as a different percentage is obtained depending on the call scenarios used.

Vodacom is of the opinion that the use of the date of '*December 2012'* is arbitrary and that "*economies of scale and scope*" is a vague term. Indeed it would be more prudent to review the share of the markets on a regular basis as operators may exceed the 20% market share

threshold especially over the lengthy period for which the remedies, for instance high asymmetry percentages, are proposed.

Vodacom recommends that at a minimum, the Authority needs to review the application of this remedy annually, and notify operators, where applicable, that the asymmetry remedy no longer applies to a particular operator so that voice call termination rates can be reconfigured by all operators within a certain time period.

Regulation 7(4)(a)

As stated above, Vodacom is of the view that it has not benefited from reciprocal treatment by the Authority in the allocation of spectrum and therefore does not have this characteristic and should be excluded from this regulation 7(4)(a).

Regulation 7(5)(a)

Vodacom's comments under Parts A and B refer.

In terms of section 67(8) of the ECA, the Authority is required to modify pro-competitive terms and conditions imposed to ensure continued proportionality.

Vodacom has identified three areas of concern under this Regulation, namely the target MTR, the glide path and the unchanged target FTR.

Further, the price control is imposed for a specific period, i.e. 1 March 2014 to 1 March 2016 and asymmetry is imposed for 1 March 2014 to 1 March 2019. Subject to its comments on the reintroduction and extended period of asymmetry, Vodacom seeks clarity on this inconsistent arrangement and what will happen to MTRs after March 2016.

Target MTR

Vodacom refers the Authority to our representations under Part B, paragraph 2 above.

Vodacom is of the considered view that a cost model should inform the charge control to be imposed.

In terms of regulation 7(5)(a) the target MTR is set at R0.10c. The Authority, in paragraph 5.3 of the Explanatory Note on the Draft Regulation, states that it "*determines that the cost of termination in Market 1 is now approximately R0.10 per minute based on, amongst others, the increase in traffic on licensees' networks*".[21] It is not evident from the reading of the Regulations, how the target MTR of R0.10c was determined as the Authority has not disclosed all the factors that were considered in determining the target MTR.

Vodacom submits that the information requested by the Authority to date is insufficient to inform cost-oriented rates based on detailed economic analysis and the development of a cost model. Regulation 7(5)(b) of the Draft Regulations mentions a BULRIC cost model that is still to be developed, which is a further indication that in arriving at the target rate, the Authority did not make use of such a model. The Draft Regulations allow the Authority to amend existing rates based on the outcomes of the model. Vodacom conducted a high level cost estimate which indicates that the target MTR of R0.10c is too low for South Africa.

[Please refer to **Annexure B** for a detailed analysis on the impact of reducing MTRs to an inappropriate level.]

Based on the aforementioned, Vodacom is of the considered view that the proposed MTRs are not informed by evidence based data i.e. a cost model and therefore likely to be incorrect. Vodacom recommends that in the absence of a cost model, the Authority exercise caution and impose reasonable interim rates while the Authority proceeds with thorough consultation on a BULRIC model.

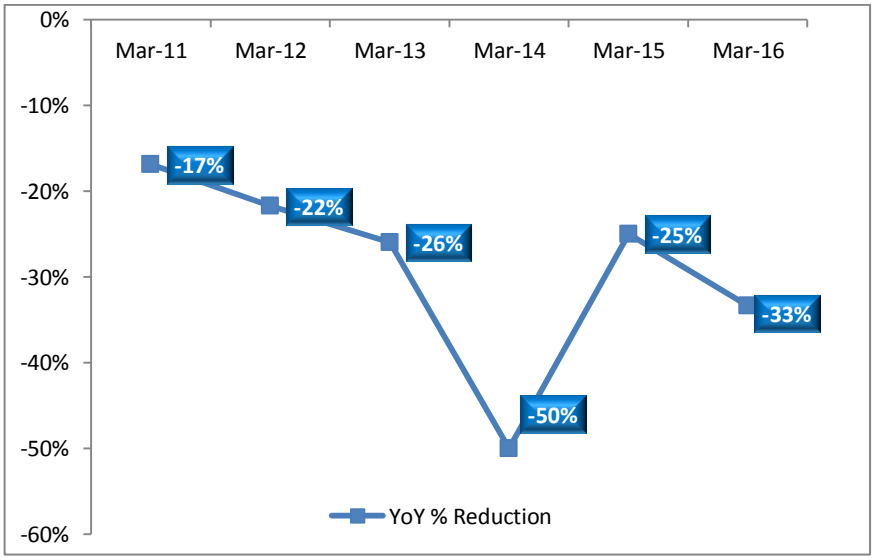
[21] Paragraph 5.3 of the Explanatory Note on the Draft Regulations, page 13.

Glide Path

Vodacom refers the Authority to our representations under Part B, paragraph 4 above.

The figure below demonstrates the more reasonable rate of reductions prescribed in 2010 compared to the proposed reductions.

Figure 2: Comparison of year on year MTR reductions from 2011 and as proposed



Vodacom submit that the market conditions that justified the imposition of a glide path in the 2010 regulations still currently exist, namely to allow operators time to adapt their business models, to adjust to new pricing levels as well as to ensure that operators are not subject to price shocks. For this reason the Authority is commended for the decision to make provision for a glide path, however Vodacom appeals that the steepness of the reduction be adjusted to a more reasonable level with specific reference to the first step.

The Unchanged FTR

Vodacom refers the Authority to our representations under Part B, paragraph 5 above.

The Authority has not provided transparency with regard to the reasonable grounds that form the objective basis of the determination that the target FTR should remain unchanged

and has also not provided any explanation with regard to the facts and information that informed this proposal.

Vodacom submits that setting MTRs below FTRs is artificial and sends the wrong pricing signal. Vodacom recommends that the target FTR should be determined on the basis of a robust cost model.

Regarding the distinction between Within 0N area code and Between 0N area code in Table 2, please refer to Vodacom's comments under Regulation 3(b)(i) and (ii) above.

Regulation 7(5)(b)

Vodacom refers the Authority to our representations under Part B, paragraph 3 above.

As stated above, Vodacom is of the considered view that proposed MTRs are not informed by evidence based data i.e. a robust cost model and likely incorrect. Vodacom submits that the publication of an unsupported number, which is still to be confirmed by a cost model, is premature and could have negative consequences. Only a cost model yields the appropriate level of evidence for such a key regulatory decision. Vodacom recommends that the Authority should proceed with the thorough consultation on the BULRIC model and key pricing parameters and that adequate time should be allowed for such a model to be properly developed and executed. Vodacom confirms its view that the appropriate cost standard for South Africa is LRIC plus.

In addition, Vodacom contend that it would not constitute a proportionate and justifiable remedy, to only do a BULRIC model for operators as listed in sub-regulation (7)(4). All operators found to have SMP in their respective markets should submit data so that an appropriate rate can be set. This will assist the Authority to ensure that the level of asymmetry is objectively justified.

8. Schedule for review or revision of markets

Regulation 8

Vodacom submits that it is important to provide for a minimum requirement to assess the market in order to ensure that remedies, such as the asymmetry proposed, do not remain in place for an indefinite period of time.

9. Contraventions and Penalties

Vodacom supports measures introduced by the Authority to facilitate compliance with regulations by imposing penalties for non-compliance. Vodacom is of the view that failure to comply with the Call Termination Regulations should fall under the category of offences contemplated under section 17H(3)(d) and (e) of the ICASA Act which provides that it is an offence for a licensee to:

> *"(d) fail to comply with any order made by the Authority in terms of the ICASA Act or the underlying statutes*
>
> *(e) act in disregard of any prohibition imposed by order of the Authority in terms of the ICASA Act or the underlying statutes".*

According to section 17H(3)(h) failure to comply with the provisions of section 17H(3)(d) and (e) is punishable by a fine not exceeding R250 000.

In light of the above, Vodacom recommends that the Authority revise the penalty provision having regard to section 17H of the ICASA Act.

10. Short title and commencement

Vodacom has no comments.

Appendix A: Application of the Fair and Reasonable Obligation

Paragraph 1.1

Vodacom agrees with the principle that "fair and reasonable" prices for voice call termination are rates that are equivalent to cost-orientated rates. Vodacom reiterates that the rates proposed under Regulation 7(5) are not cost-oriented in light of the fact that the rates are set when a robust cost model is yet to be developed. Please refer to Vodacom's comments under regulation 7(5) above.

Vodacom hereby draws the Authority's attention to the fact that its reference to "Regulation 7(4)" is incorrect and should read as "Regulation 7(5)".

Paragraph 2

Vodacom supports the principle of asymmetry to the extent that it is justified based on objective exogenous cost differences.[22] The criteria for asymmetry should therefore be objective, exogenous and aligned with internationally accepted principles.

Vodacom is of the view that the qualifying criteria for asymmetry need to be applied to all operators on a case by case basis by means of a transparent public and consultative process.

Vodacom refers the Authority to our representations under Part B, paragraph 1 above.

Paragraph 2.1

Vodacom refers the Authority to our representations under Part B, paragraph 1.5 above.

Paragraph 2.2

Vodacom refers the Authority to our representations under Part B, paragraph 1.6 above.

[22] The ERG Common Position on the Symmetry of Fixed Termination Rates and the Symmetry of Mobile Termination Rates.

Vodacom submits that market share in respect of a non-new entrant is not an appropriate factor to consider with regard to asymmetry as a lack of economies of scale cannot be attributable with absolute certainty to exogenous factors only.

Vodacom is of the view that Cell C has had adequate time to achieve scale and it can be argued that Cell C's lack of scale is due to its own inefficiencies and possible past strategic errors.

Vodacom reiterates that it would be prudent for the Authority, to review the share of the markets on a regular basis, at least annually, to assess the application of this remedy, and notify operators, where applicable, that the asymmetry remedy no longer applies to a particular operator so that voice call termination rates can be reconfigured by all operators within a certain time period.

Vodacom confirms that the relevant market for MTRs is defined as "the market for wholesale voice call termination services to a mobile location on the network of *each* ECS/ECNS licensee which offers such a service within the Republic". Vodacom therefore questions reference to "total terminated minutes in the relevant market" which seems to refer to a new total voice call termination market that has not been defined. In terms of the current market definition in the Draft Regulations all licensees have 100% of the share of terminated minutes in the relevant market and should therefore not qualify for asymmetry on this basis.

Paragraph 2.3

Vodacom refers the Authority to our representations under Part B, paragraph 1. above.

Vodacom reiterates that regulated wholesale products should not be used as a tool to facilitate cross-subsidisation between players operating in the same market. Asymmetry should not be turned into a "safety blanket" which might enable inefficiencies and may cause smaller operators to remain small and dependant. The proposed asymmetry can prevent industry from reaching its efficient structure through consolidation by artificially supporting inefficient operators.

When applied, the practice worldwide is that asymmetry is a short-term measure to assist new entrants in their market entry stage. In addition, the level of asymmetry should gradually converge to symmetry. For example, in Ghana,[23] a two year period of asymmetry is offered to new entrants with less than 5% subscriber market share. In addition, an operator which reaches a market share of 5% within the first two years would cease to enjoy asymmetry.

Vodacom contends that on-going asymmetry is not international best practice as it is exceptional, and therefore should not be sanctioned by the Authority.

Paragraph 2.4

Vodacom reiterates that it would be prudent for the Authority to review the share of the markets on a regular basis, at least annually, to assess the application of this remedy, and notify operators, where applicable, that the asymmetry remedy no longer applies to a particular operator so that voice call termination rates can be reconfigured by all operators within a certain time period.

Paragraph 2.6

Vodacom refers the Authority to our representations under Part B, paragraph 1. above.

Vodacom is concerned about the proposed level of asymmetry which, as demonstrated in Table 1 below, increases from the current 10% and peaks to 160% in March 2016.

Table 1: Levels of asymmetry granted since 2011

Period	Asymmetry (R)	Asymmetry (%)
01 March 2011	R0.15c	20%
01 March 2012	R0.08c	15%
01 March 2013	R0.04c	10%
01 March 2014	R0.19c	95%

[23] http://www.nca.org.gh/downloads/Interconnect_News.pdf

Period	Asymmetry (R)	Asymmetry (%)
01 March 2015	R0.18c	120%
01 March 2016	R0.16c	160%
01 March 2017	?	?
01 March 2018	?	?
01 March 2019	?	?

Vodacom reiterates that in terms of section 67(8) of the ECA, the Authority must modify applicable pro-competitive terms and conditions to ensure proportionality subject to changes in the competitive nature of the market. The Draft Regulations do not set out what changes in the competitive nature of the market warrant the significant modification of asymmetry in Market 1 to ensure proportionality. The Draft Regulations further are not transparent on the reasonable grounds, facts and information that form the objective basis of this decision. The proportionality and fairness of the proposed determination on asymmetry in Market 1 is also questioned, based on unsupported and significant different treatment of the fixed and mobile voice call termination markets as well as the exceptional and substantial subsidisation required by the imposed levels and extended period of asymmetry that may promote inefficiencies.

Based on the aforementioned, Vodacom is of the view that the proposed levels of asymmetry are not justified. Vodacom recommends that symmetrical rates be imposed on all licensees, or in the case where asymmetry is allowed to continue it should be done over the short term to gradually reduce the current level of asymmetry.

Paragraph 3.1

Vodacom submits that the difference in asymmetry imposed between Market 1 and Market 2 is significant although the Authority has stated that it found in both markets that competition is ineffective. The Authority has not provided transparency in respect of the reasonable grounds, facts and information that inform the aforementioned determination and deviation from the *status quo*.

In the 2010 Call Termination Regulations, the same levels of asymmetry were granted for Market 1 and Market 2. The Authority has now deviated from this by imposing only a 10% asymmetry on Market 2

Vodacom reiterates its position that termination rates should be based on cost and that the level of asymmetry provided should be to address quantifiable cost differences. Vodacom recommends that an impact assessment should be conducted as the proposed remedies may lead to a distortion of the market.

Paragraph 3.2

Vodacom's comments under regulation 2.3 refer.

Paragraph 3.3

Vodacom's comments under regulation 2.4 refer.

PART D: JUST ADMINISTRATIVE ACTION

Just administrative action and good regulatory practice promote evidence-based regulatory processes that include meaningful public participation. The Draft Regulations are in Vodacom's view not representative of just administrative action due to lack of:

- evidence-based regulation;
- (transparency on the) reasonable grounds, facts and information that form the objective basis of decisions such as the proposed modified pro-competitive measures;
- proportionality of the proposed modified pro-competitive measures;
- fairness, based on questionable and significant different treatment of the fixed and mobile voice call termination markets as well as the exceptional and substantial subsidisation required by the imposed levels and extended period of asymmetry that may promote inefficiencies;
- impact assessment, as current remedies may lead to distortion of the market and questionable outcomes;
- reasonable consultative processes, for example the Authority in June 2013 formally stated that a consultation process by means of a Discussion Document will precede and inform the Draft Call Termination Regulations. However, this consultation process did not take place; and
- consistency, when measured against the stated principles and approach of the 2010 Call Termination Regulations and its Explanatory Notes.

Just administrative action is a recognised right in the Bill of Rights of the Constitution (section 33): "Everyone has the right to administrative action that is lawful, reasonable and procedurally fair." The Promotion of Administrative Justice Act, 2002 ("PAJA") gives effect to this right.

The process of making determinations and imposing pro-competitive conditions is an exercise of quasi-judicial administrative powers by the Authority under Chapter 10 of the ECA.

Vodacom's above submission highlights missing elements and shortcomings in the exercise of such administrative powers; this follows, unfortunately, from the lack of/limited consultation, evidence based regulation, transparency and/or limited nature of the Draft Regulations and accompanying Explanatory Notes.

Vodacom submit that a lack of evidence based regulation, consistency, thorough consultation, transparency and sound regulatory decisions negatively impacts on investment decisions and business and leads to regulatory uncertainty, In addition, the South African government objectives and the broader consumer community will likely also be negatively impacted in the medium to long term.

ANNEXURE A: LESSONS LEARNT FROM EUROPE

In many regards the European Union has been at the forefront of the development of the mobile industry. The GSM standard originated in Europe and many of the regulatory approaches that have been enacted outside of Europe in recent years have been strongly influenced by European regulatory policy. One of the most notable pieces of European regulatory intervention in recent years has been the policy of pure incremental cost termination rates. Pure incremental cost is the lowest cost standard that has been advocated in the context of cost-orientation. The policy shift for termination rates has also coincided with a move into retail price regulation in relation to roaming services. Further, European policy makers have been trying to favour new entrants and small operators with lower wholesale access fees on fixed networks, favourable spectrum conditions for new entrants and small operators and the threat of mandated national roaming access and pricing.

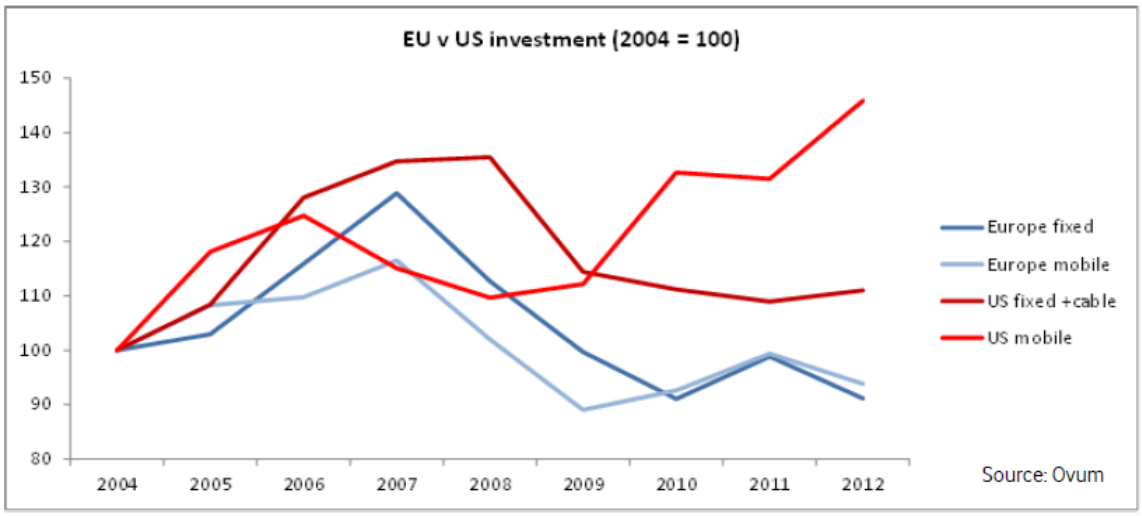
Having gone down a path of increased regulatory intervention – in relation to both mobile and fixed networks, and a policy approach to favour certain operators over others, Europe now finds itself with an investment crisis. It is the view of Vodafone Group that this crisis is largely due to the short-termism of the policy approach whereby only the short-term benefits of lower retail prices[24] were taken into consideration rather than the longer-term benefits of investment. The tables and graph below show how Europe has trailed the rest of the OECD and the US in relation to investment since the more interventionist approach was adopted.

[24] Refer to the analysis of the European Commission which shows the extent to which pricing has been driven down in Europe in contrast to other regions: http://ec.europa.eu/digital-agenda/sites/digital-agenda/files/DAE%20SCOREBOARD%202013%20-%201-THE%20eCOMM%20SECTOR.pdf

2009-2011	Telecoms investment per pop (USD)
Switzerland	291
Australia	287
Canada	241
New Zealand	239
United States	223
Japan	158
W Europe	135
Korea	118

2009-2011	Mobile investment per pop (USD)
United States	210
Korea	175
Canada	171
Switzerland	169
New Zealand	122
W Europe	121

Source: OECD



It is only now, many years later that the investment gap is understood. This is one of the major drivers of the new policy initiative from the European Commission – The Connected Continent.[25] This proposed policy seeks to act as a stimulus for the European telecoms industry to prevent further job losses and reinvigorate investment and innovation. Even if this policy gets enacted and is successful, the European telecoms industry will have taken a number of backwards steps, which could have been avoided.

The investment gap is now evident in the performance of networks, e.g. Ofcom complaining about the quality of 3G coverage in the UK.[26] The Italian government is also seeking to

[25] http://ec.europa.eu/digital-agenda/en/connected-continent-single-telecom-market-growth-jobs
[26] http://www.telegraph.co.uk/technology/10401571/Ofcom-to-launch-unprecedented-review-of-mobile-phone-speeds-as-shock-figures-reveal-3G-non-spots.html

address the investment gap by setting specific investment targets for Telecom Italia.[27] This is completely at odds with the deregulation and free market agenda that has been at the forefront of European policy for the last 20 years.

Having regard for the market situation in Europe, Vodacom calls on the Authority to avoid making the same mistakes that were made by European policy makers. The role of MTR regulation should be to ensure:

- pricing is at sustainable levels;
- competition is not compromised; and
- investment is incentivised.

It is Vodacom's views that cost-based MTRs based on the LRIC plus cost methodology will strike the right balance between these three objectives. This will allow market forces to work and enhance the symbiotic relationship between the telecoms industry and the wider economy. In the global marketplace the countries with the best infrastructure will be the winners. Vodacom is fully prepared to be the provider of such infrastructure and trusts that the appropriate regulatory regime will be enacted to support this.

[27] http://www.reuters.com/article/2013/11/18/italy-telecom-idUSL5N0J32DJ20131118

ANNEXURE B: VODACOM'S ANALYSIS ON DISPROPORTIONATE IMPACT OF TOO LOW MOBILE TERMINATION RATES

Investment decisions reflect economic incentives and specifically the investment process exists to ensure that the expected returns from individual projects are not less than the (risk-reflective) cost of invested capital. As discussed below, significant reductions in MTRs (for example, as a result of adoption of a pure LRIC cost standard) will result in lower revenues and hence, other things equal, lower returns and this will have an impact on investment decisions. Marginal projects in poorer and particularly rural areas, in respect of next generation infrastructure investment to meet broadband objectives, may be disproportionate from the investments in metropolitan areas as these projects may no longer be financially viable. In this regard, any policy that discourages investment in rural areas, risks widening the digital divide between urban and rural consumers and will negatively affect lower income users who are over-represented in rural areas.

To explore these issues, we have undertaken analysis to understand the potential sensitivity of investment incentives with respect to MTRs. Specifically, we have considered:

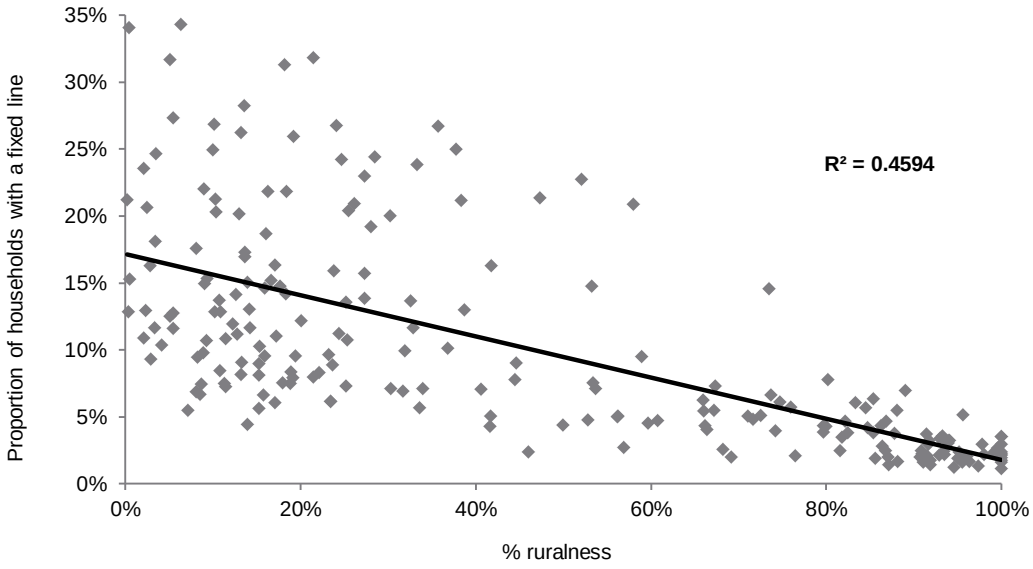
1. the relationship between fixed line penetration in rural areas, and income levels;
2. analysis at a cell site level of the contribution of mobile termination to total revenues, and how this may vary in different parts of the country; and
3. the importance of MTRs as part of the revenue generated by low users groups.

These issues are considered further in the following sections.

Fixed line penetration and income in rural areas

In this section we seek to illustrate the relationship between fixed line penetration, the proportion of a particular South African municipality that is defined as rural by the South African 2011 Census, and income levels. Figure 1 below demonstrates that there is a strong urban/rural dimension to fixed line presence, with fixed access concentrated in urban areas.

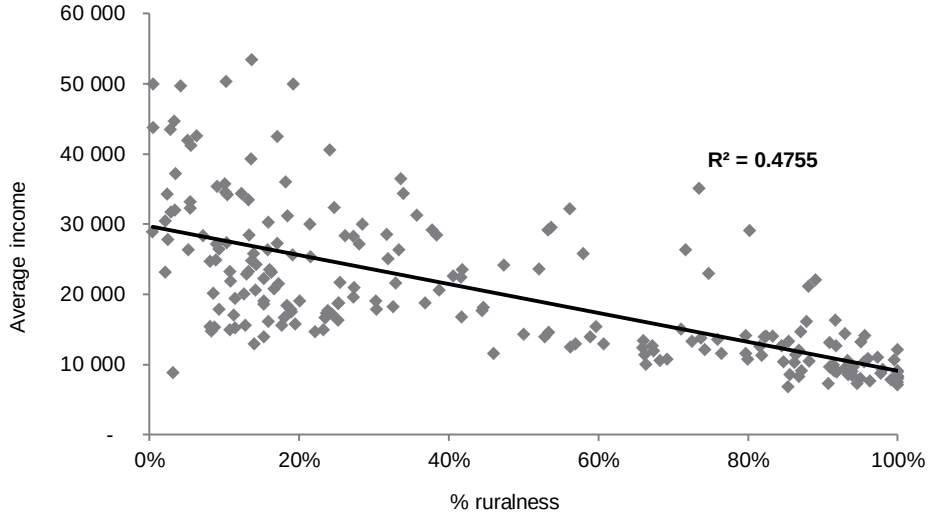
Figure 1: Proportion of households with a fixed line *versus* 'ruralness'[28] by municipality



Source: South Africa 2011 census, EY analysis

Figure 2 below suggests a strong relationship between average income and the degree of ruralness.

Figure 2: Average Income *versus* ruralness by municipality



Source: South Africa 2011 Census, Vodacom data

[28] Ruralness is defined as the proportion of households in a municipality who live in rural areas

Together, the two figures above suggest that rural areas exhibit lower fixed line penetration and are therefore likely to be primarily dependent on mobile networks to provide broadband access. Further, there is a relationship between low average income and ruralness, suggesting that such areas may, on average, benefit most from regulatory policies which encourage an extension of broadband services through employment, economic growth and the narrowing of a digital divide. Conversely, a regulatory policy that does not incentivise investment in rural areas will risk deepening a digital divide between rural areas and urban areas and will disproportionately affect lower income South Africans who are over represented in rural areas.

In the context of determining an appropriate cost standard for MTRs, based on our analysis, it is clear that a LRIC plus (or FAC) cost standard would provide more appropriate investment incentives than a pure LRIC standard, as it allows for full recovery of FCCs, and hence would be more closely aligned with the Authority's stated objectives in respect of broadband investment.

Cell site analysis

In this section, we seek to understand the link between MTRs and investment incentives, particularly in rural and/or low income areas. We therefore analysed to what extent different cell sites were reliant on revenue from MTRs, and how marginal investment decisions (for example in terms of technology upgrades to extend mobile broadband coverage) may be affected by material cuts in MTRs.

To do so, we obtained a sample of call records from 672 Vodacom cell sites, from a total population of 9 104 (as at March 2013). These sites were drawn from five municipal areas (as defined by the 2011 Census), which we considered provided a reasonably representative mix of income levels and rural/urban population splits. The dataset included details on usage by subscriber (voice, data and messaging), and associated subscriber ARPUs, and hence enabled us to undertake some in-depth analysis on revenue drivers by cell site. Figure 3 below shows

that the relative contribution of terminating revenue to total revenue[29] varies considerably by cell site.

Figure 3: Terminating revenue as a proportion of total revenue[30], by sampled cell site

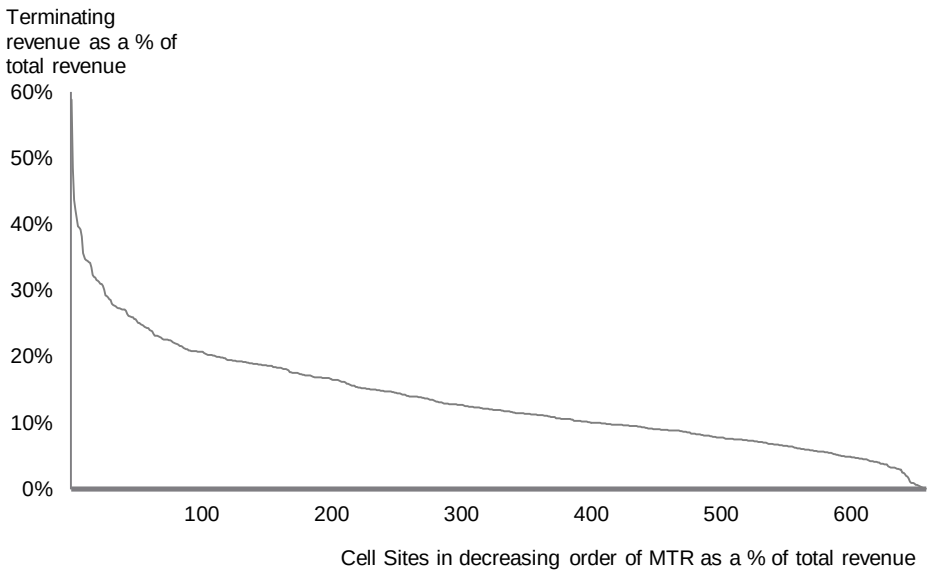


Figure 3 shows that there exists a significant number of cell sites for which mobile termination revenue is a significant component of total cell revenues (for example accounting for at least 20% of revenue for 17% of sampled sites) and therefore that a significant reduction in MTRs will result in a material decline in cell revenue and hence risk a material negative impact on the financial performance of such sites.

To illustrate numerically, Table 1 below shows cell sites where termination revenue contributes (i) over 10% and (ii) over 20% of total revenue.

[29] Total revenue is derived using monthly ARPU for call origination (based on an average of 3 months of data (February, March and April 2013)) plus the number of termination minutes (based on data for April 2013) multiplied by the MTR. This data is then annualised (multiplied by 12)

[30] Revenues per cell site are derived from customer ARPU information with customers being tagged to one cell site based on the most used cell site from which they made and received calls in the previous month

Table 1: MTR as a proportion of total cell site revenue by municipality

Proportion of cell sites in which MTR as a proportion of revenue exceeds	City of Cape Town	Lesedi Municipality	Okhahlamba Municipality	Ubuntu Municipality	Witzenberg Municipality	Total
10%	61%	7%	89%	31%	91%	60%
20%	15%	0%	43%	25%	64%	17%
Total sampled cell sites	603	14	28	16	11	672

Source: Vodacom data

In total, as mentioned above, in 17% of cell sites termination revenue accounts for greater than 20% of total revenue. However, we can also see that there is considerable variation across different municipalities. For example, in Witzenberg municipality, MTR revenue contributes over 20% of revenue in nearly two thirds of all cell sites whereas, in Cape Town, 15% of cell sites are dependent on termination revenue for over 20% of their total revenues. This indicates that the financial performance of cell sites in municipalities such as Witzenberg and Okhahlamba, which have a high proportion of the population living in rural areas, is more sensitive to changes in termination revenue than cell sites in urban areas. However, it also shows that, even in urban areas such as Cape Town, there exist cell sites for which termination revenue is an important contributor of their financial performance.

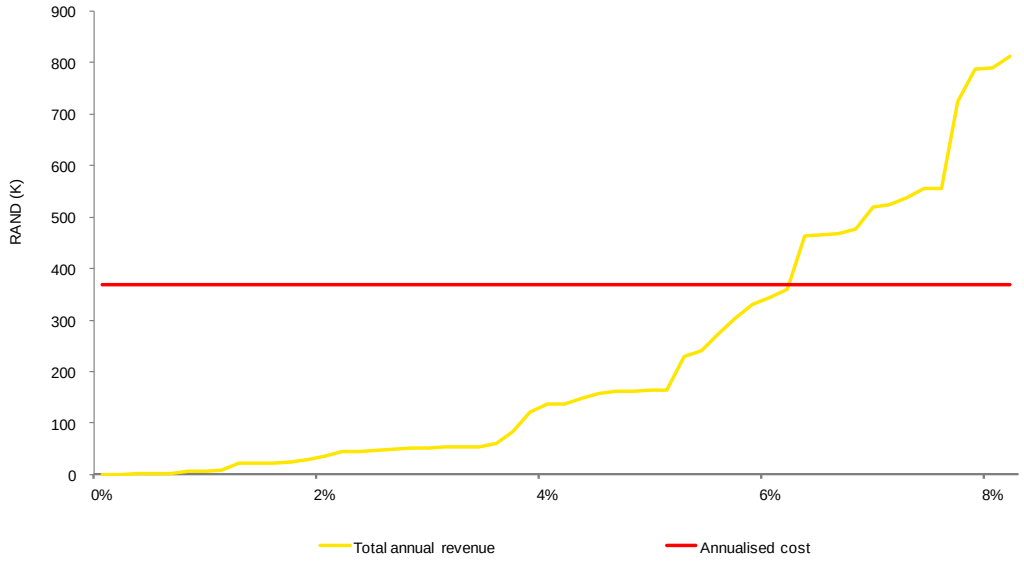
A material reduction in MTR revenue, for example, a reduction of the MTR from 40c to 10c, will result in a reduction in total revenue of at least 15% for one in six cell sites, risking both the financial viability of the site and, importantly, potentially undermining or at least dampening future investment cases consistent with broadband ubiquity objectives. Further,

this impact will not be limited to rural areas, and will also affect a proportion of cell sites in urban areas.

Material reductions in MTR revenue (by for example the adoption of a pure LRIC cost standard), risk dampening future investment in technology migration, and while disproportionately affecting rural areas, will also impact investment in urban areas.

To illustrate how this may take effect, Figure 4 below shows the bottom 8% of cell sites from our sample by revenue and an estimate of cell site costs.[31]

Figure 4: Revenue per cell site for the bottom 8% of cell sites by revenue



Source: Vodacom

This broadly illustrates that the lowest 6% of sites by revenue are loss-making in the first order[32]. Investment in these cell sites reflects the trade-offs between direct profitability and second order benefits arising from competitive differentiation. Reducing the MTR will not

[31] Cell site costs were derived by dividing the total costs of the radio network by the number of cell sites. In practice we would expect some variation in the costs of cell sites, with potentially a positive relationship between the costs of a cell site and its revenue, but consider using an average cost across the network is a reasonable proxy

[32] Cell sites which are loss-making in the first order do contribute to the profitability of the wider business by helping to acquire and retain customers

only further reduce revenues for all cell sites, thereby increase the proportion of cell sites that are unprofitable, but it will shift the trade-off on unprofitable cell sites, making them less financially viable. This in turn will have an effect on future investment decisions.

Furthermore, as Table 2 below shows the proportion of low revenue cell sites in different municipalities is reasonably varied, again suggesting that any impact from lower MTRs on investment incentives will not be limited to rural areas.

Table 2: Annual revenue distribution across cell sites by municipality

Cell sites in which revenue is between	City of Cape Town	Lesedi Local Municipality	Okhahlamba Municipality	Ubuntu Municipality	Witzenberg Municipality	Total
0 and 6,000,000	**18%**	**57%**	**11%**	**19%**	**9%**	**19%**
6,000,000 to 24,000,000	**27%**	**7%**	**32%**	**75%**	**45%**	**28%**
24,000,000 +	**55%**	**36%**	**57%**	**6%**	**45%**	**53%**
Total sampled cell sites	603	14	28	16	11	672

Source: Vodacom data

MTR revenue and low use groups

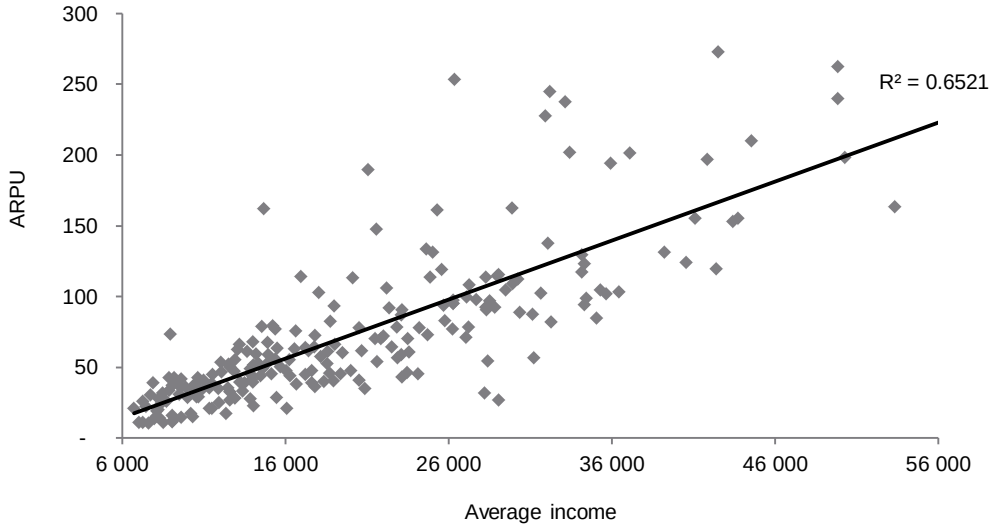
Finally, we considered the extent to which individual subscribers may be disadvantaged by significant reductions in MTRs. Vodacom data[33] which shows the distribution of the subscriber base by outbound revenue revealed that over one in eight users (13.4%) do not generate any outgoing voice revenue and so for these subscribers Vodacom only generates revenue from terminating services. Any material reduction in MTRs, therefore, will have a magnified effect on the profitability of such customers, potentially reducing operators' incentives to retain such subscribers, reduce provision of mobile broadband-enabled handsets or amend the

[33] Vodacom data was based on the call records of the entire pre-pay customer base for one month

commercial structures for such subscribers (e.g., by enforcing a minimum top-up amount per month).

Further, as Figure 5 below shows, there is a strong relationship between ARPU and income, with low ARPU customers disproportionately represented in lower income bands.

Figure 5: Relationship between income and ARPU



Source: Census 2011, Vodacom data

As a consequence, this implies a relationship between "inbound only" subscribers (who generate lower ARPUs than subscribers who both receive and make calls) and those on lower income levels, so again it is the most disadvantaged members of society that would be most affected by significant reductions in MTRs.

The outcome of this analysis shows that:

- There is a clear relationship between fixed line penetration, ruralness, and low income, highlighting the significant challenges facing policy makers in respect of the digital divide, and the fact that extending the reach of broadband services will rely on mobile, and not fixed technology. A significant reduction in MTRs would reduce the incentives for

this necessary investment to incur to the detriment of the specific areas, and indeed, to the wider economy;

- Terminating revenues are a significant element of total revenues in one in six cell sites. Although there is a rural bias towards the location of these cell sites even in urban areas, such as Cape Town, revenues from these cell sites will be adversely affected as a result of significant reductions in MTRs. This will reduce cell site profitability, and incentives to invest in technology upgrades; and
- Revenues from terminating services are the only source of revenue Vodacom receives for 13.4% of its subscriber base, and these are likely to be low income subscribers, given the relationship between low income and low ARPUs. Were MTRs to be cut significantly then a number of these subscribers may become loss making, and hence Vodacom (and other mobile operators in the market to the extent they service subscribers will similar usage profiles) will face reduced incentives to retain such subscribers, and may need to take steps (e.g., by enforcing a minimum top-up amount per month) to manage its low user subscriber base.

ANNEXURE C: THE ERG COMMON POSITION ON THE SYMMETRY OF FIXED TERMINATION RATES AND THE SYMMETRY OF MOBILE TERMINATION RATES

The European Regulators Group (ERG)[34] is of the view that the right of new entrants to recover their costs should be balanced with the objective of achieving the maximum level of efficiency in the supply of termination services, hence asymmetry should not be in place for too long and each operator's termination rate should be brought down to the cost of an efficient operator as soon as possible.

ERG further states that unlike unique efficient termination rates, asymmetric termination rates do not favour productive efficiency. Even though it allows operators (efficient or not) to recover their incurred costs, it imposes a constraint on more efficient operators to subsidise the relative inefficiencies of their competitors. The Regulators who allow asymmetric termination rates to prevail over a too long a period risk encouraging inefficient market entry.

ERG acknowledges that asymmetry may be justified on the following grounds:

- where there are cost differentials as a result of differentiated conditions of spectrum allocation that are outside the control of the licensee; and
- to encourage the growth of a new entrant that suffers from a lack of economies of scale due to late entry and not out of a licensee's inability to compete fiercely.

Having acknowledged the above, ERG further states that regulators should bear in mind that asymmetric regulation is only sustainable for a transitional period and that regulators should commit to a sunset clause and to guarantee that differences in prices reflect differences in costs.

In light of the above ERG concluded that according to economic theory, symmetric termination rates enhance static economic efficiency, investment and innovation and that asymmetric termination rates, because they encourage entry, potentially contribute to dynamic efficiency and favour competition, depending on the prior state of competition in

[34] ERG's Common Position on symmetry of fixed call termination rates and symmetry of mobile call termination rates.

the market. However, if the asymmetry is maintained for too long, the inefficiencies may be passed on in the downstream markets to the detriment of competition and welfare.

ERG stated that the average asymmetry granted to operators with a 3 to 5 year delay was 17% and operators with a 6 to 11 year delay were granted on average a 35% asymmetry. Based on market share, operators with less than 10% market share were on average granted 47% asymmetry and those with between 10% and 20% market share were on average granted a 13% asymmetry.