

Executive Summary

Internet Solutions (IS) commends ICASA for the work done in reducing termination rates. IS agrees with the definition of markets and those licensees with Established Significant Market Power (“ESMP”). Licensees with ESMP are hereinafter referred to as “Established licensees”. IS also agrees with the glide path proposed to regulate Established licensees. However, we are of the opinion that there are insufficient pro-competitive measures in place to increase competition in the sector. It can be demonstrated that Telkom’s pricing policies make calls originating from its network and terminating on new entrants’ networks uncompetitive. It can also be demonstrated that the Mobile Network Operators (MNO’s) charge end users the same retail rates irrespective of how much or how little licensees without ESMP (“Other licensees”) charge as call termination rates.

Based on the situation described above, IS proposes a policy of Symmetrical Interconnect rates for Other licensees. This affords Other licensees the opportunity to be reasonably competitive in the Fixed Market and to earn sufficient revenues to cover the cost of terminating calls. Given the limited scale of new entrants, we contend that the cost of terminating a call is significantly higher for new entrants than for Established licensees, whether Fixed or Mobile. Furthermore, we contend that the Authority has not fully taken into account the advent of Convergence which is blurring the line between Fixed and Mobile operators.

We acknowledge the risk of arbitrage through transit pricing that our proposed solution would introduce but are of the view that this can be regulated through the Reference Interconnect Offer framework.

Introduction

Internet Solutions (IS) commends ICASA for the work done in reducing termination rates and for the level of detail evidenced by the Explanatory note accompanying the Draft Regulations. We agree with the conclusions reached regarding the ineffectiveness of call termination markets for fixed and mobile services and the need to impose pro-competitive measures. The definition of licensees with Significant Market Power (SMP) and the differentiation between Established licensees and Other licensees provides a well thought out basis for regulating these markets. The proposed glide paths provide certainty in the industry and afford Established licensees the opportunity to manage the transition towards a cost-based interconnect rate. IS welcomes the guidelines provided in regulating Reference Interconnect Offers (RIO’s) to be prepared by Established licensees.

DO WHAT YOU LOVE.
LOVE WHAT YOU DO.



Competition in the market

While these Regulations appear to provide an effective remedy for high call termination rates imposed by Established licensees, we respectfully propose that there is insufficient guidance to ensure that Other licensees have an opportunity to compete in the voice markets. Other licensees find themselves “between a rock and a hard place” when it comes to competing in these markets.

In terms of the Fixed market, our Enterprise customers require a solution whereby it does not cost their end users more to call our network than Telkom’s network. One must assume that the vast majority of calls in the Fixed market will originate from the Telkom network given their monopolistic history. Telkom’s current pricing policy appears to be a simple addition of R0.44 to the call termination rate imposed by Other licensees. In doing this, they ensure that the cost to call Other licensees’ networks is always greater than the cost to call their own network. Given this situation, Other licensees need to be imposing as low an interconnection rate as possible in order to ensure that end users don’t have to pay too much of a premium to terminate on our networks. It may be that ICASA considers this a Retail problem which should not be considered in these Regulations. However the Retail and Wholesale markets are linked so we feel it is important to highlight this problem as part of this submission. IS proposes that ICASA consider this situation and impose a pro-competitive measure to afford Other licensees the opportunity to have a competitive offering for calls terminating on our networks. Failing the imposition of a pro-competitive measure, Other licensees need to charge as low a rate as possible to be somewhat competitive in the Fixed market.

On the other hand, Other licensees are not yet established in the voice markets. We therefore have comparatively little scale on our networks and consequently have significantly higher termination costs than Established licensees, be they Fixed or Mobile. As a result of this, Other licensees need to charge relatively high call termination rates in order to cover our existing costs and to be able to invest in our networks so as to increase competition in the voice markets.

Clearly the above-mentioned scenario of needing low rates to be competitive and high rates to cover costs places Other licensees in a precarious position. IS contend that the Draft regulations in their current form do not offer a solution to the plight of Other licensees. While the regulations do allow some flexibility in the form of an opportunity to charge higher termination rates on the evidence of higher costs, this only addresses half of the issue.

DO WHAT YOU LOVE.
LOVE WHAT YOU DO.



Proposed Amendments to Draft Regulations

IS proposes that the simplest and fairest means of addressing this predicament is to stipulate Symmetrical Call Termination Rates for Other licensees. It is our opinion that Symmetrical Call Termination rates are consistent with ICASA's call for "fair and reasonable" commercial agreements and that this cannot be considered discriminatory if the principle of Symmetry is applied consistently by all Other licensees in all situations.

Put simply, a policy of symmetrical call termination rates for Other licensees will empower us to charge Established Fixed Operators at a rate of R0.15 per call and the Established Mobile Operators at a rate of R0.65 per call.

The effect is that we will be reasonably competitive in the Fixed Market, with a premium of R0.15 probably being palatable for our Enterprise customers. This lower rate will also ensure that end users are not charged exorbitant rates to terminate on Other licensees' networks thereby bringing down the costs of telecommunications and providing a level of certainty in the market. By certainty, we are referring to the fact that certain Other licensees currently charge excessively high rates to terminate on their networks thereby making calls expensive to end users and creating a situation whereby end users don't know how much they will have to pay to call an 087 number. This will ultimately lead to avoidance of these numbers and a lack of competition in the market.

The problem will be heightened with Geographic Number portability (GNP) as even Geographic numbers could be priced exorbitantly creating chaos in the market. This situation exists because of Telkom's pricing policies and needs to be considered by ICASA.

If Other licensees were to charge R0.15 to all licensees, the outcome may appear to be reasonable. The problem lies in the fact that Other licensees have high termination costs due to low scale. If all calls were terminated at R0.15, Other licensees would soon be bankrupt and there would be less competition in the market. By applying Symmetry and charging MNO's at R0.65 per call, Other licensees are in a position to recover costs at a reasonable market rate. The added benefit is that it does not cost the end user anything extra because the MNO's already charge end users based on the highest call termination rate in the market. In other words, whether Other licensees charge R0.15 or R0.65 to the MNO's, they will still charge the end users based on a mark-up on the R0.65 rate. This is clear from the history of how they have priced in the market. There appears to be no logical reason for Other licensees to charge

SUBMISSION: DRAFT REGULATIONS REGARDING CALL TERMINATION RATES

lower call termination rates to MNO's as it simply results in the ridiculous situation of new entrants subsidising very profitable large operators.

By introducing the principle of Symmetry, on a non-discriminatory basis i.e Symmetry applied consistently by Other licensees, these licensees can be reasonably competitive in the Fixed market and can cover costs on a weighted average basis. By this, we mean that because approximately 80% of calls originate on MNO's networks and the remainder on Fixed operator networks, the weighted average cost recovery can be calculated at approximately R0.55. $(80\% \times R0.65) + (20\% \times R0.15) = R0.55$. Assuming a cost to terminate of approximately R0.40, this results in an average gross margin of R0.15 equivalent to 37.5%. We consider this reasonable in order to cover costs of overheads and network expansion.

Convergence

In order to implement the proposed principle of Symmetrical Call Termination rates for Other licensees, ICASA will need to consider the impact of Convergence. Convergence has arrived and the Draft Regulations don't fully consider the VoIP environment. 087 numbers can already be allocated to users with fixed end points or mobile devices and it becomes impractical and administratively taxing to charge operators different rates for different termination points. This will become increasingly complex as users are allocated one number which they can use as their fixed and mobile number.

Traditionally ICASA has been intent on differentiating between Fixed and Mobile call termination rates. The underlying rationale for this differentiation is not where the call terminates but the cost of terminating the call. Given that scale is at least as big a determinant of cost as mobility, we contend that it is fair and reasonable to assume that Other licensees have costs that are equal to or greater than those of the MNO's. It would be counter-intuitive to have a situation of asymmetry between new entrants and Established licensees where the new entrants are the parties penalised.

Arbitrage and Transit

IS concedes that there is one problem with the proposal of Symmetrical call termination rates for Other licensees. This problem comes in the form of an arbitrage opportunity through transit. Put simply, MNO's could transit calls to Other licensees via Telkom or Neotel. This would result in them paying only R0.15 plus a transit fee as opposed to R0.65. Fortunately this can be easily remedied by regulating that RIO's may include a clause prohibiting MNO's from

DO WHAT YOU LOVE.
LOVE WHAT YOU DO.



SUBMISSION: DRAFT REGULATIONS REGARDING CALL TERMINATION RATES

sending calls destined for Other licensees via Established Fixed Operators and similarly prohibiting Established Fixed Operators from offering such transit services to MNO's.

Alternate Option

Should ICASA view the above-mentioned recommendation as unworkable, an alternate solution needs to be considered for Other licensees, most of whom are VoIP or converged communications providers. As discussed in the section headed Convergence above, the traditional differentiation between Fixed and Mobile operators may no longer be relevant. It is therefore argued that a third category of providers should be considered and treated differently. The best alternative is for these licensees to each apply a cost-based termination rate to their networks, irrespective of whether the termination is at a fixed or mobile end point.

In this scenario, IS proposes capping the rate at R0.65 to prevent inefficient operators from creating uncertainty in the market through excessive call termination rates.

The challenge of inefficient competition in the Fixed market, caused by Telkom's pricing policies, would remain. This could possibly be remedied through other regulations or processes.

Conclusion

ICASA has a difficult task in facilitating reduced telecommunications costs, encouraging continued investment in infrastructure and promoting competition in the industry. This is a difficult balancing act which requires careful consideration. As a non-Established licensee, IS respectfully requests that ICASA consider the need for Other licensees to be competitive in the Fixed market while earning sufficient revenue from call termination to cover costs. Our proposed solution to this conundrum is the principle of Symmetrical call termination rates for Other licensees interconnecting with Established licensees.

IS thanks ICASA for the opportunity to submit this written representation and hereby requests an opportunity to make oral presentations to ICASA as per the published Draft Regulations.

DO WHAT YOU LOVE.
LOVE WHAT YOU DO.

