

**TELKOM SA LIMITED'S SUBMISSION ON ICASA'S REVIEW OF
UNIVERSAL SERVICE AND ACCESS OBLIGATIONS AS PUBLISHED IN
THE GOVERNMENT GAZETTE NO. 33467 OF 17 AUGUST 2010.**

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1. INTRODUCTION

Telkom SA Limited ("Telkom") appreciates the enquiry undertaken by the Authority and also welcomes the opportunity to submit its comments on the review of the regulatory framework for Universal Service and Universal Access, including the framework for Universal Service and Universal Access Obligations ("USAO's").

Telkom acknowledges the Authority's extensive research and preparatory work that led to the publication of the Discussion Document and Report as per Government Gazette 33467 of 17 August 2010. We are equally grateful to the Authority for placing these Discussion Documents in the public domain for comment and for possible representations, and we trust that our comments and responses to the accompanying questionnaire will contribute towards the attainment of a suitable regulatory framework for Universal Service and Universal Access in South Africa.

Should the Authority decide to hold Public Hearings on this matter, Telkom would like to actively participate therein.

2. DEFINITIONS AND DETERMINATIONS

Telkom's response to the published Discussion Document is premised on the definitions found in the Electronic Communications Act, 36 of 2005 (the ECA), as well as the determinations with regard to Universal Access and Universal Provision of Electronic Communications Services and Electronic Communications Network Services, as outlined in the February 2010 Ministerial Determination.

Telkom's response is also informed by the analysis on USAO's that have been imposed on licensed operators since 1997 when Telkom was issued a PSTS license. All these obligations are well summarised in the BMI-TechKnowledge Compliance Report that forms part of the Documentation on the Review of Universal Service and Access Obligations.

3. BACKGROUND

Telkom acknowledges that governments across the globe advocate universal service and universal access policies and programmes so as to attain several strategic goals, in particular to “bridge the digital divide” by:

- Driving physical proximity/ownership to electronic communications services in areas where it may be uneconomic for licensees to provide services,
- Facilitating affordable electronic communications services where residents cannot afford access to the services available at their locations.

In South Africa, the inequalities in telecommunications resources have been seen to exist not only along national lines (urban and rural), but also along race and class lines. To this extent policy directives and pieces of legislation, from the 1996 White Paper, the Telecommunications Act of 1996, through to the Electronic Communications Act of 2005, have over the years been geared to articulate a vision that balances the provision of basic universal service to disadvantaged rural and urban communities with the delivery of high level services capable of meeting the needs of a developing South African economy.

It is equally notable that despite all of the above legislative amendments, changes in the licensing regime, as well as other significant market forces, the regulatory framework on Universal Service and Universal Access has never been reviewed since the initial set of Universal Service and Universal Access Obligations (USAOs) that were imposed on the licensed operators from as far back as 1997 when Telkom was first issued with its PSTS license.

Furthermore, it is noted that the implementation and maintenance of existing USAOs has left the country with valuable experiences that cannot be overlooked going forward. Amongst others lessons that can be cited include:

- The disconnect between roll out targets and issues of affordability, culminated in mass disconnections and wasteful investment;
- Public payphones exemplifies a techno-centric obligation that has failed;
- The uncoordinated and selective rollout of CST's, mainly in commercially viable areas, has left most of the contemplated needy areas unserved;
- The lack of proper mechanisms to facilitate and monitor the implementation of obligations imposed on Mobile Operators for 1.800Mhz and 2.400MHz spectrum was an unfortunate set back;
- The model that promoted USAL's was fundamentally flawed and counterproductive.
- Regulatory coordination for the implementation of e-rate is lacking.

4. INSTITUTIONAL ARRANGEMENTS

The current institutional arrangements between the Ministry, the Authority and the Agency are adequately defined under Chapter 2 and Chapter 14 of the ECA and Telkom is of the view that these arrangements should not be tempered with, notwithstanding possible legislative amendments to make them more effective.

Telkom is also of the view that the Agency remains the best positioned hub to manage USAO tendering processes (section 90 of the ECA) and to administer the USAAF (section 87.4 of the ECA), despite the perceived lack of capacity and limited effectiveness of the Agency, notwithstanding the known and disabling definitional issues that fall outside the scope and mandate of the Agency. The long overdue review of the contribution of 0.2 percent of annual turnover to the USAAF (section 89.2 of the ECA), the definition of under-served areas (section 88.2 of the ECA), and the requirement that all levies paid into the fund be transferred to the national revenue fund (section 87.2 of the ECA), to the extent that funds can only be accessed through Parliament, are classical examples of issues that fall outside the precincts of the Agency.

It is a notable concern that the monitoring and evaluation of the implementation and impact of USAOs is less than pleasing. The successful implementation of the globally acknowledged "Gap Model" (as unpacked in Section 6 of this document), calls for the periodic review of the "Access Gap". Therefore going forward monitoring and evaluation is a crucial area that will require considerable attention.

Telkom takes note of a number of critical projects that have been undertaken by USAASA recently:

- Definitions of universal service, universal access, and underserved areas and determinations in respect of needy persons
- Quantification of the universal access and universal service gaps
- Standard operation procedures and fund manual
- Competitive tender process for universal service and access projects

Telkom is of view that these projects are of strategic importance to the contemplated regulatory framework, and the Agency needs to be supported in all of the above.

5. GENERAL COMMENTS

Telkom acknowledges the extensive groundwork that preceded the publication of the Discussion Document. It is a job well done. Notwithstanding the good springboard that the analysis is providing, it is regrettable that the review process is not informed by a clear, comprehensive and forward looking Policy on Universal Access and Universal Service.

Like many other fixed line incumbents, as outlined in the benchmark exercise that is cited in the Discussion Documents, to date Telkom still maintains a sizeable amount of unduly burdensome and equally unsustainable USAOs that were based on an outdated licensing regime that preceded today's converged era where mobile and broadband internet seem to reign.

Telkom's PSTS license subjected the company to the following Universal Service obligations:

- i. Provisioning of Basic Telephone Service
- ii. Provisioning of Public Pay-telephone Service - Telkom is writing off R700m per annum to maintain the public payphones obligation in spite of circumstances that are markedly different from those under which the obligation was imposed, a situation that is technically and financially unsustainable
- iii. Access to the Public Emergency Call Service
- iv. Access to the Directory Information Service
- v. Contributions to USAAF

The cumulative maintenance of these obligations is unduly burdensome on Telkom and can no longer be sustained. Telkom incurs a significant Access Line Deficit (ALD) particularly for the obligation to provide Basic Telephone Service.

The ALD is the shortfall between the cost of providing basic access to the fixed network and the revenue received from line rental and installation charges. Telkom is currently providing access to the fixed network at prices below cost and therefore have to cross-subsidise this shortfall. This is based on public interest considerations, such as the objective of providing universal access at the lowest possible price. It should be noted that due to the demographic, topographical and social features of the South African market, the cost of the ALD in South Africa is considerably larger than in other countries.

So far, Telkom has been making significant losses in the provision of network access services as part of its universal access and service obligations. Telkom's ALD for the 2008/2009 period on a CCA basis amounts to R8,2bn.

To this extent, Telkom requests that the determination of a new regulatory framework for USAOs takes into account all the burdensome legacy challenges that are entrenched in Telkom's battle for survival. In particular, the ALD should be considered as part of the calculation of Telkom's USAO.

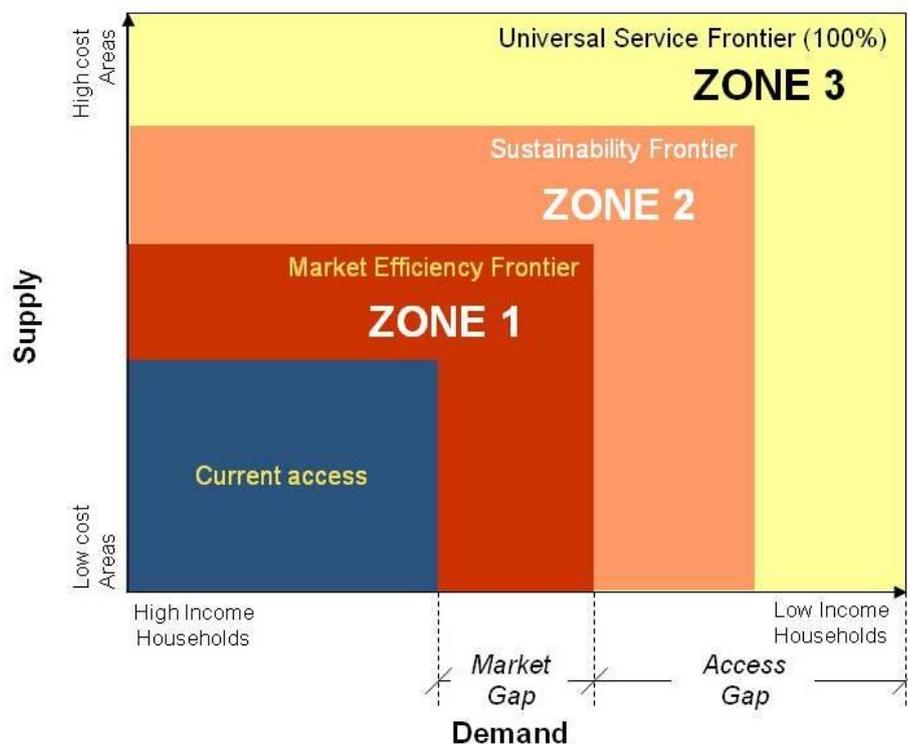
Telkom would also like to urge the Authority to consider the following additional set of principles when determining USAOs:

- i. The contemplated regulatory framework for USAO's should be informed by an overarching policy and be based on globally accepted principles of competition, transparency, non-discrimination, neutrality and freedom from unnecessary burdens on licensees.
- ii. The framework should be premised on a comprehensive cost-benefit analysis and equally be informed by proper quantification study of the regulatory burden placed on licensees.
- iii. Government subsidies (from taxation) should be given serious consideration, particularly for commercially non-viable areas/instances that require ongoing subsidies.
- iv. Effective pricing schemes that will incentivise uptake and also ensure sustainment of services, should be explored. Social discounting, price discrimination, de-averaged pricing are classical examples to be explored.
- v. All licensees should have a shared responsibility towards the advancement of Universal Service and Universal Access
- vi. USAO's must be proportional to the size of the business of licensees, to the extent that similar licensees carry equitable obligations
- vii. The contemplated regulatory framework on USAOs should not be considered in isolation, but should take into account the overall regulatory cost that will be carried by licensees – as indicated above
- viii. In line with section 90 (1) of the ECA, the contemplated regulatory framework should be designed with an emphasis on "incentives" rather than an accentuation of "penalties";
- ix. The contemplated regulatory framework should be complementary to the new, converged and technology neutral licensing regime - and thus promote the use of comprehensive and economically efficient solutions to drive universal broadband access
- x. All licensees participating in the USAO tendering processes must also be obliged to contribute to the USAAF

6. PROPOSED APPROACH TO THE REGULATORY FRAMEWORK

Taking all of the above into consideration, Telkom is of the strong view that:

- i. **Mobile technologies are the most economic and efficient manner for rapid deployment of universal broadband, and therefore spectrum license should carry significant rollout obligations, taking into consideration the fact that different frequency bands should carry obligations commensurable to the economic value of the frequency band.**
- ii. **The global approach of "Gaps Model" be used in determining a suitable regulatory framework for USAOs**



Source: Navas-Sabater et.al, 2002.

- Zone 1, the Market Efficiency Frontier, should be addressed with appropriate legislative amendments and/or changes in the regulatory framework;
- Zone 2, (areas that are commercially viable after "jump-start" subsidies), the Sustainability Frontier should be addressed with the competitive tendering processes and Smart Subsidies from the USAAF (costs could also be offset against the licensee's contribution towards the USAAF);
- Zone 3, (areas that are not commercially viable and would require ongoing subsidies), the Universal Service Frontier should be addressed with ICASA imposed USAO's. **It is in Zone 3 where:**

- i. Significant spectrum related rollout obligations should be imposed,
- ii. Costs can also be offset against the licensee's contribution towards the USAAF, and where such costs far exceed the USAAF contributions, then further subsidies can be solicited from the fund,
- iii. Or alternatively, state subsidies can be solicited.

7. REVIEW OF ICASA'S PROPOSED MODELS

- Telkom notes that ICASA has reviewed at least seven different models and has rejected two of these models.
- The tables below summarises Telkom's understanding of the five models under review (column on the left) , as well as Telkom's comments on these models (column on the right), given all of Telkom's views and considerations as outlined in the preceding sections of this document:

7.1. MODEL 1: PAY AND PLAY

- *(Coordinated with broadened competitive tendering process – This is ICASA's recommended option).*

Model 1 Description from the Discussion Document.	Telkom's Comments on Model 1.
<p><i>The licensee carry USAOs imposed by ICASA & contributes to the USAAF.</i></p> <ol style="list-style-type: none"> 1. No existing USAO licensing obligations to be carried over (due to implementation shortcomings); 2. Only existing obligations that have already been implemented have to be maintained; 3. ICASA can impose new appropriate obligations; 4. The ECA will have to be amended accordingly. 	<ul style="list-style-type: none"> • The two statements (i) “no existing USAO license obligations are carried over” and (ii) “only existing obligations that have already been implemented have to be maintained” are confusing. A new regulatory framework cannot build on existing obligations, otherwise the review exercise will be futile; • Existing obligations were based on the old licensing regime and thus cannot be carried over, nor can the fulfilled obligations be maintained without proper review. These obligations are unduly burdensome, particularly to Telkom.
<p>Telkom's Position: TELKOM DOES NOT SUPPORT THIS MODEL.</p>	

7.2. MODEL 2: PAY AND/OR NO PLAY

- (With more inclusive tendering – This is ICASA's 2nd best option)

Model 2 Description from the Discussion Document.	Telkom's Comments on Model 2.
<p><i>The licensee no longer carry ICASA imposed USAO's, but must contribute to the USAAF.</i></p> <ol style="list-style-type: none"> 1. All licensees (not only ECNS) can play by participating in the tendering processes. 2. Qualified contenders can also bid – and later get licensed if they are successful; 3. USAASA manages & administers the fund, ICASA has no further involvement. 	<ul style="list-style-type: none"> • Telkom does not support the suggestion that licensees should no longer carry imposed USAOs. Given the SA context, this will stifle government's objects of accessible and affordable ICT services for all South Africans; • It is not clear what will happen to existing obligations (implemented and outstanding); • Successful contenders will also have to contribute to the USAAF;
<p>Telkom's Position: TELKOM DOES NOT SUPPORT THIS MODEL.</p>	

7.3. MODEL 3: PAY AND NO PLAY

- (ICASA's 3rd best option)

Model 3 Description from the Discussion Document.	Telkom's Comments on Model 3.
<p><i>The licensee no longer carry ICASA imposed USAO's, but must contribute to the USAAF.</i></p> <ol style="list-style-type: none"> 1. Only current licensees can gain access to USAAF resources. 2. USAASA manages/administers both the fund & UAS projects, ICASA has no further involvement. 	<ul style="list-style-type: none"> • Restricted access to the USAAF does not promote competition, especially in a liberalised market. USAO tenders should be broadened, as long as successful contenders are made to contribute to the USAAF (if they aren't doing so already). • The lack of ICASA imposed USAOs defeats the very object of USAO's and this cannot be in line with government policy, notwithstanding the lack of clarity on existing obligations;
<p>Telkom's Position: TELKOM DOES NOT SUPPORT THIS MODEL.</p>	

7.4. MODEL 4: PAY OR PLAY

- (This is Telkom's preferred option)

Model 4 Description from the Discussion Document.	Telkom's Comments on Model 4.
<p>ICASA can still impose USAO's on licensees, however:</p> <ol style="list-style-type: none"> 1. Costs for fulfilling USAO's are offset against the licensee's contribution towards USAAF. 2. New obligations to be in line with US & UA strategy from USAASA. 	<ul style="list-style-type: none"> • The view that this model is difficult to manage and administer is noted, however any of the models chosen is faced with similar challenges; • Telkom welcomes the recommendation that existing obligations be replaced with new obligations; • The offsetting of related costs against the licensees' contribution to the USAAF separates this model from the rest of the pack. • Where costs for fulfilling USAO's far exceeds the licensees' contribution towards the USAAF, subsidies for such unbearable costs should either be solicited from the USAAF, from government, or should be offset against other fees, such as spectrum fees. • The model is suitable for the proposal that significant USAOs be linked to allocations to address Zone 3 of the Access Gap; • The broadened competitive tendering process can still be employed in Zone 2 of the Access Gap whilst the spectrum related USAOs are imposed to address Zone 3.
<p>Telkom's Position: TELKOM FULLY SUPPORTS ALL ELEMENTS OF THIS MODEL.</p>	

7.5. MODEL 5: PAY AND PLAY

- (This is the model that is currently in place)

Model 5 Description from the Discussion Document.	Telkom's Comments on Model 5.
<p>Licensees continue to carry existing USAO's & contribute to the USAAF.</p> <ol style="list-style-type: none"> 1. Enforce all previous obligations; 2. Impose new obligations to new entrants; 3. Only ECNS licensees can participate in tendering processes. 	<ul style="list-style-type: none"> • Previous obligations were based on the old licensing regime and thus cannot be carried over, nor can the fulfilled obligations be maintained without thorough review. These obligations are now unduly burdensome to operators, Telkom in particular; • Exclusive tendering processes do not seem to promote competition. USAO tenders (and access to the USAAF) should be broadened, as long as successful contenders are made to contribute to the USAAF (if they aren't doing so already). • The model does not promote proportional imposition of USAOs;
<p>Telkom's Position: TELKOM DOES NOT SUPPORT THIS MODEL.</p>	

8. PREFERRED MODEL

- **TELKOM PREFERS AND FULLY SUPPORTS MODEL 4 (THE PAY OR PLAY MODEL).**

9. CONCLUDING REMARKS

It's been thirteen years since Telkom was issued with a PSTS license (since May 1997) and to date Telkom is still maintaining most of the initial license conditions and obligations that were attached to the PSTS license. When Telkom was issued with the Individual ECNS and ECS licenses in February 2009, Telkom continued to be subjected to the same Universal Service and Universal Access obligations that were attached to its May 1997 PSTS license (General Notice with new licenses). It is for this particular reason that Telkom is calling for the review of existing obligations, with a clear intent to withdraw these obligations and have them replaced with new and appropriate obligations.

Telkom acknowledges that the dawn of new regulatory framework for Universal Access and Universal Service Obligations will be faced with numerous challenges, in particular the amendment of the ECA, the building of capacity within USAASA, the smoothening of competitive tendering processes, the overhauling of processes related to the USAAF, as well as the establishment of mechanisms to monitor and enforce compliance. With all of these challenges anticipated, Telkom is looking eagerly forward to a new dispensation.

END