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**SUBMISSION BY MWEB CONNECT (PTY) LTD (“MWEB”) ON THE  
DRAFT LICENCE FEE REGULATION, 2012**

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**1. INTRODUCTION**

- 1.1 MWEB thanks the Independent Communications Authority of South Africa ("the Authority") for providing us the opportunity to comment on the draft Licence Fee Regulations, 2012 ("the Draft Regulations")<sup>1</sup>.
- 1.2 The Draft Regulations propose to repeal the General Licence Fee Regulation, 2009 ("the current Licence Fee Regulations").
- 1.3 MWEB agrees with the principles of the current License Fee Regulations and we do not see the need for an overall review of the current Licence Fee Regulations. We concede that certain clarifications may be required, but submit that the Authority does not provide sufficient, cogent and adequate reasoning for the changes proposed in the Draft Regulations.
- 1.4 We note that the Authority did not provide any substantiation for its decision to set the licence fee percentage at 0.75%. MWEB would like to understand the Authority's reasoning for and basis of determining the proposed licence fee percentage. We certainly believe licensees should have an opportunity to comment thereon.
- 1.5 The proposed amendments to the current License Fee Regulations must be considered in the context of the purpose sought to be achieved by these amendments and we do not believe that the proposed amendments is consistent with the objectives sought to be advanced by these amendments.

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<sup>1</sup> Notice No. 887, Gazette No. 35819, 24 October 2012

## **2. RATIONALE FOR CURRENT LICENCE FEE REGULATIONS**

- 2.1 The Authority previously took the position that annual licence fees should be levied on gross profit and correctly reasoned that licence fees should be levied on gross profit because:
- 2.1.1 only profitable entities will pay licence fees;
  - 2.1.2 levying based on percentage of gross profit is competition-neutral, in that it treats different entities differently;
  - 2.1.3 it takes into account the impact of economic cycles on profitability; and
  - 2.1.4 the methodology is easy to administer.
- 2.2 The Authority states in the explanatory memorandum to the Draft Regulations that it realised that the above methodology is not easy to administer and created a regulatory arbitrage. We do not dispute that this may be the case. However this is merely one factor to consider. All the other factors previously stated by the Authority as reasons for levying license fees on gross profit remain very valid and cannot be disregarded.
- 2.3 It also appears from the explanatory memorandum that another reason motivating the proposed amendments is a qualified audit against the Authority. The Authority states that its inability to verify the license fees collected led to this qualified opinion against it. Surely this is not the only reason (if at all) for the qualified opinion against the Authority?
- 2.4 Internet Service Providers (“ISPs”) play a vital role in the growth of broadband access at affordable prices and ensuring healthy competition in South Africa. However, this is extremely challenging in a cut throat industry, where margins are low and the cost of running the business high.
- 2.5 ISPs are largely dependent on Telco providers for network and infrastructure services, at extremely high costs. For example, the cost of IPC alone accounts for roughly 60% of the cost of providing ADSL services. Not allowing ISPs to deduct any costs from its revenue before paying licence fees at the proposed rate of 0.75% will therefore be financially detrimental to ISPs.
- 2.6 We further submit that paying licence fees based on revenue instead of gross profit inadvertently results in a “double tax” situation in some

instances. For instance, Telkom will pay licence fees to the Authority on revenue derived from IPC income; if an ISP is not allowed to deduct its costs of IPC, the ISP will again pay licence fees to the Authority on the services it sold using that same IPC, resulting in the Authority being paid twice for income derived from the same source.

- 2.7 Previously (before the inception of the current License Fee Regulations) license fees were also based on revenue and it was shown then already, for the reasons stated above, to be unjust. We find it perplexing that the Authority would revert to this methodology.

### **3. THE AUTHORITY'S OBJECTIVES FOR THE PROPOSED AMENDMENTS**

- 3.1 The specific behaviour the Authority is trying to address by the Draft Regulations is an apparent regulatory arbitrage by some providers. However this is not necessarily prevalent in all ISPs. It seems that the problem is not paying licence fees on gross profit, but the current lack of clarity on what constitutes "total cost directly incurred in the provision of such service [licenced services]"<sup>2</sup>
- 3.2 We submit that the Authority's intended objective could be achieved with a far less severe impact on ISPs and in a sensible manner if the Authority merely clarifies what costs may be deducted from revenue derived from licenced services. In this regard we suggest, that as a minimum, the following deductions should be allowed:
- 3.2.1 for the reasons stated in 2.6 above, all costs paid by one licensee to another licensee for the provision of licensed services. This can be verified by the Authority by requesting documentary proof, like invoices;
- 3.2.2 the cost of international capacity. This is a major cost for ISPs, but a crucial part of building a network and providing broadband services of international standards. This can equally be verified with invoices;
- 3.2.3 the direct cost of network and infrastructure build. The high cost of building a network and infrastructure is a big deterring factor for ISPs. Allowing this deduction would at least provide

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<sup>2</sup> Definition of "Gross Profit" in General Licence Fee Regulations, 2009

some relieve and promote infrastructure development, which is in line with government objectives.

#### **4. LICENSE FEE PERCENTAGE**

4.1 The Authority proposes license fees at 0.75% of revenue. We are not sure how the Authority arrived at this percentage. Before the inception of the current License Fee Regulations VANS providers paid license fees on revenue at 0.1%.

4.2 We request the Authority to provide us with the rationale for the increase from 0.1% to 0.75% so that we are provided with an opportunity to carefully consider it and comment thereon.

4.3 As stated before, imposing license fees of 0.75% of revenue will have an unjust financial impact on ISPs, which inadvertently will have various adverse effects.

#### **5. GENERAL COMMENTS**

5.1 We submit that the proposed definition of “Licensed Services” does not provide any clarity on what constitutes licensed services.

5.2 The proposed definition also does not clarify that it only refers to “broadcasting services”, “electronic communications services” and “electronic communications network services” provided pursuant to a license issued to a Licensee in terms of Chapters 3 and 9 of the Act. We believe this is an important clarification, which is correctly contained in the current License Fee Regulations.

#### **6. CONCLUSION**

6.1 We believe that the proposed changes will have a significant and unjust impact on ISPs.

6.2 We further believe that the adverse effect of the proposed amendments outweighs the objective sought by the proposed amendments.

- 6.3 We trust that the Authority will seriously consider this submission and carefully consider the effect of the proposed amendments on ISPs and the industry.
- 6.4 We would welcome the opportunity for further engagement with the Authority.
- 6.5 Please do not hesitate to contact Wilmari Hannie on 021 596 8533 or [whannie@mweb.com](mailto:whannie@mweb.com) should you have any queries or should you require any additional information from MWEB.