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Independent Communications Authority of South Africa

Attention: Mr P Mailula, Ms F Hlongwane – Project Leaders

Per email: pmailula@icasa.org.za, fhlongwane@icasa.org.za

SUBMISSION: DRAFT REGULATIONS IN RESPECT OF THE LIMITATIONS OF CONTROL AND EQUITY OWNERSHIP BY HISTORICALLY DISADVANTAGED GROUPS AND THE APPLICATION OF THE ICT SECTOR CODE

1. ISPA refers to the:

   1.1. Draft Regulations in respect of the Limitations of Control and Equity Ownership by Historically Disadvantaged Groups and the application of the ICT Sector Code ("**the Draft Regulations**"), read with;

   1.2. Findings Document and Position Paper on the Inquiry into Equity Ownership by Historically Disadvantaged Groups and the Application of the ICT Sector Code in the ICT Sector January 2019 ("**the Findings Document and Position Paper**"),

   and sets out its written submissions below. Should the Authority elect to conduct public hearings – to the extent that this currently possible – ISPA confirms its wish to participate.

Alignment between HDG requirement and ICT Sector Code

2. ISPA has understood throughout its participation in this process that it was an express intention of the process to align the application of current HDG requirements stipulated in the Electronic Communications Act ("**the ECA**") with the application of the Revised ICT Sector B-BBEE Code. ISPA's submissions have focused on how flexibility in reaching transformation targets could be introduced through such an alignment.

3. We note, however, that the position adopted by the Authority does not result in any alignment of the two sets of requirements; rather these are imposed alongside each other as separate yet overlapping

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obligations for licensees. While ISPA has argued for licensees to have greater flexibility in reaching transformation targets, the Draft Regulations create more rigidity.

Time periods for the consideration of applications for transfer of ownership of licences and transfer of control over licences

4. ISPA notes that:

   4.1. The Authority takes 12-15 months to process applications for transfer of ownership of individual licences and transfer of control over individual licences.

   4.2. The vast majority of such applications are straightforward and require no public hearings or additional processes.

   4.3. This means that the parties to such applications must wait for 12-15 months after reaching commercial agreement to receive a regulatory approval to implement the transaction requiring the application.

   4.4. This time period is at odds with commercial reality and disincentivizes compliance.

5. ISPA calls on the Authority to review its processes for considering and finalising these applications with a view to shortening the applicable time period.

6. Having reviewed the steps required to be taken by the ECA and applicable regulation – including publication and comment requirements – ISPA suggests that a time period of 3-6 months is achievable and desirable.

Application to class licences

7. ISPA has consistently opposed the expansion of limitations on ownership and control to class ECNS and ECS licences issued by the Authority under Chapter 3 of the ECA, seeing this as contrary to the clear intention of the ECA to create a licensing category with limited rights and an on-demand licensing system which is quick, inexpensive and requires only local registration as a prerequisite.

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8. The ECA clearly does not impose such limitations on class licences while expressly providing for transformation at the individual licence level.

9. The cost of compliance includes the imposition of a direct regulatory cost burden on class licensees in the form of the requirement to obtain a verification certificate from an accredited BEE verification agency. For SMMEs with limited staff capacity and internal expertise in complying with BEE requirements, this cost will be significant.

10. ISPA is concerned that the motivation for the Authority's decision to impose this requirement on class licensees is its perception that the class licence framework is being "exploited" by large providers to avoid transformation requirements applicable to individual licensees. This is incorrect reasoning.

    10.1. Any such concerns should be addressed with the licensees concerned instead of applying a blanket requirement on all other licensees.

    10.2. Such a motivation would implicitly acknowledge that the size and/or annual revenue of a licensee is a factor being considered by the Authority, despite statements to the contrary.

    10.3. There is precedent for the adoption of a more nuanced approach in the form of the Value-added Network Services (VANS) Regulations published by the Authority on 20 May 2005[1], which required the following:

    4. Empowerment

    4(1) A licensee shall within 12 months of issue of licence, demonstrate a minimum of 15 percent equity ownership by historically disadvantaged persons, and achieve a 30 percent equity ownership within 24 months of issue of the licence.

    (2) The provisions of sub-regulation (1) shall only apply where the licensee's annual license fee income is greater than R1 000 000.

11. It bears stating that the low barrier to entry for the registration of class licences encourages entry into the industry by Black People, who will now also need to bear an additional compliance cost.

[1] Available from https://internet.org.za/regs_vans_2005.html

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12. ISPA submits that the Authority should reconsider its position and the Draft Regulations insofar as these impose equity ownership obligations on class licensees.

13. If the Authority elects to persist on its current course, ISPA requests that obligations to be imposed are not applied retroactively to existing class licences. Rather these should apply on a prospective basis to new registrants and to entities renewing class licences.

Application of 30% HDG Equity Requirements (Regulation 3)

14. As regards sub-regulation 3(5), ISPA has been referred to developments in the mining sector relating to the "once empowered always empowered" rule as it is expressed in the Mining Charter 2018[2]. After a protracted legal and political contest, it is now settled as a matter of policy in that sector that previous empowerment transactions will be recognised for the purpose of compliance with BEE equity ownership requirements, notwithstanding the subsequent exit of the empowerment partner in a manner which dilutes BEE equity ownership.

15. In reaching this policy position, compelling arguments relating to the need to create investment certainty and avoiding restrictions of rights of exiting partners were adopted.

16. ISPA submits that the Authority should adopt the same approach with regard to the application of the 30% HDG and the 30% Black People equity ownership requirements, subject to the same forms of limitations to control abuse as utilised in the mining sector.

17. ISPA refers to sub-regulation 3(3):

    17.1. The Authority must – prior to finalisation – clarify what a "verification agency" is for the purposes of confirming HDG equity ownership and provide details of which such agencies are to be regarded as "recognised" and "accredited".

[2] Broad-Based Socio-Economic Empowerment Charter for the Mining and Minerals Industry, 2018. Available from https://www.gov.za/sites/default/files/gcis_document/201809/41934gon1002.pdf.

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17.2. ISPA understands the rationale for this provision and that it flows from the decision of the High Court in its judgement on the consolidated matters between various licensees and the Authority reviewing the Authority's decision to approve the transfer of control application brought by Neotel in respect of its acquisition by Vodacom[3].

17.3. However, licensees that are currently not compliant with the existing HDG equity ownership obligation may be required to make application to the Authority in order to become compliant. Sub-regulation 3(3) therefore requires amendment to clarify that such applications will be accepted and processed by the Authority.

Application of B-BBEE Requirements on Licences (Regulation 4)

18. ISPA notes the decision by the Authority to set level 4 certification as the benchmark for compliance by all licensees. This varies the position adopted in the Findings Document and Position Paper that the benchmark would be level 6:

17.19….In considering the various submissions made, the Authority is of the view that in the context of licensing - which differs substantially from procurement - mere compliance with the Revised ICT Sector Code is not sufficient as the Authority's objective is to promote and advance empowerment. For this reason, the Authority is of the opinion that a mandatory minimum B-Status Level Six in terms of the Revised ICT Code will be compulsory for all licensees and must be maintained for the duration of the licence.

…

18.14.15. …the Authority is of the opinion that a mandatory minimum B-BBEE Status Level Six will be compulsory for all licensees which status level must be maintained for the duration of the licence.

19. No justification is provided for the discrepancy between the Findings Document and Position Paper and that adopted in the Draft Regulations.

[3] Telkom SA Soc Limited v Mncube NO and Others; Mobile Telephone Networks (Pty) Ltd v Pillay NO and Others; Cell C (Pty) Limited v The Chairperson of ICASA and Others; Dimension Data Middle East & Africa (Pty) Ltd t.a Internet Solutions v ICASA and Others (55311/2015; 77029/2015; 82287/2015) [2016] ZAGPPHC 93 (26 February 2016) @ para 80, available from http://www.saflii.org/za/cases/ZAGPPHC/2016/93.html

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20. There is no indication that the Authority in making such a decision has considered its regulatory impact taking into account the structure of various verticals or value chains within the industry. The following submission from an ISPA members illustrates this:
"To get level four bearing the above in mind a company (especially on ICT generic) will need to maximise points across all other sections of the scorecard – now bearing in mind most with interconnects with the big four will find this hard to do as the majority of our spend will be with them and none of them are QSE or EME."

21. The separation of requirements relating to (1) certification under the Revised ICT Sector Code and (2) equity ownership by Black People creates artificial rigidity and constrains the flexibility afforded by the relevant scorecard to reach the required certification level. ISPA submits that the certification requirement by itself should be sufficient and that the Authority should impose further considerations over and above the Code.

Transfer of Control or Transfer of Ownership in a Licensee (Regulation 5)

22. The references in the heading and the body of this regulation to a "transfer of control of a licensee" and "transfer of ownership of a licensee" are incorrect. Section 13(3) of the ECA explicitly refers to "the ownership or control of an individual licence". It does not refer to the ownership or control of an individual licensee.

23. This is not mere semantics. The difficulties the Authority has experienced in creating a coherent legal framework for the processing of applications for transfer of ownership of licences and transfer of control over licences arise exactly because of the failure to distinguish between a licence and a licensee.

    23.1. A licensee is a person – generally a juristic one.

    23.2. A licence embodies a set of rights and obligations that the licensee must comply with.

24. South African law requires the separation of the person from the rights and obligation of the person.

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25. The Authority is requested to ensure that its approach is aligned with the clear language of sections 13 and 31 of the ECA.

26. If the Authority does review its approach as outlined above, ISPA notes that the submissions made below in respect of the definitions of the terms "control" and "control interest" will no longer be relevant. These submissions should therefore be read in the alternative, i.e. as applicable where the Authority does not amend its approach to align with the explicit wording of the ECA (or seek to have the ECA amended to align with the approach in the Draft Regulations).

Definition of "control"

27. The Draft Regulations define "control" with reference to the definition adopted in the Competition Act 89 of 1998 ("**the Competition Act**").

28. ISPA is advised that it is not permissible in law to attempt to adopt by way of a regulation the definition of a term which is not defined in the principle legislation (in this case, the ECA).

29. The proposed definition can only be applied through the amendment of the ECA.

Definition of "control interest"

30. ISPA notes that the definition proposed is an almost complete adoption of the definition of "control" set out in the Competition Act.

31. Crucially, however, the Authority has elected to change the percentage threshold for beneficial control of a firm from 50% + 1 to 20% for both companies and close corporations.

32. ISPA cannot find any motivation for this decision to vary from the referenced definition. It appears likely, however, that the Authority has considered provisions of the ECA relating to broadcasting service licensing. This is not a valid basis for setting the bar for a "control interest" at 20%: it is stating the obvious to point out that the history and current reality of broadcasting is fundamentally different from that relating to electronic communications.

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33. In the ICASA Regulations in respect of the Limitation of Ownership and Control of Telecommunication Services in terms of section 52 of the Telecommunications Act 103 of 1996, published on 16 January 2003 ("**the 2003 Regulations**") the corresponding threshold is set at 25%.

    33.1. The 2003 Regulations were drafted in response to a completely different licensing and market structure. This is directly reflected in the notion of "concentrated markets" and the fact that only seven licensees had, at that time, the right to operate and make capacity available on telecommunications infrastructure.

    33.2. How has the Authority determined that a reduction in the threshold for determining what constitutes a "control interest" is appropriate considering the current horizontal licensing framework and liberalisation of infrastructure rights post licence conversion in 2010?

34. The effect of setting the bar this low is to bring a large volume of transactions within the scrutiny of the regulator. No justification or regulatory impact assessment is offered in the face of the direct costs this will cause to licensees or the delays it will cause in finalising what would otherwise be day-to-day transactions.

35. This cost is particularly prohibitive for SMMEs, many of which will be required to file applications for transfer of control if the Draft Regulations are finalised as is. This follows from the fact that there is currently no requirement for 30% ownership by Black People; obtaining this requires at least a 30% change in shareholding or members' interest, i.e. a change in control.

36. ISPA notes that considerations of control in general must be separated from considerations of control by Black Persons. This is to be achieved through application of the Revised ICT Sector Code.

37. Further, the 20% threshold is not saved by use of the words "in the absence of evidence to the contrary". The default assumption is that any change of shareholding or members' interest of more than 20% will require at the very least that the Authority be satisfied as to why such a change should not be regarded as a change of control. No indication is provided as to how this is to be done and what forms of evidence the Authority will consider persuasive. Again, there will be costs and delays occasioned for no discernible good reason.

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38. In conclusion: in the Findings Document and Position Paper the Authority finds that it is "clear that certainty regarding when a change in shareholding triggers a requirement for the Authority's consent and when a mere notification will be acceptable is important"[4].

39. The proposed regulation 5 does nothing to clarify the current position or whether an applicant in this position should make application for a transfer of ownership of a licence or transfer of control over a licence.

40. The following example is offered as indicative of the difficulties presented by the low threshold set for a "control interest":

    A licensee has 6 shareholders, each holding 16.6% shares. One shareholder exits and sells its shares to the remaining 5 shareholders in equal parts. If the Draft Regulations are finalised as is, each of the remaining 5 shareholders would gain a control interest, thus requiring the Authority's approval.

    A year later, another shareholder is brought in on a capital raise (i.e. new shares are issued) and all shareholders dilute their shares proportionately. Now, shareholders that had a control interest have lost this as a result of a transaction – has a change of control occurred?

41. ISPA submits that the correct threshold to be set out is that contained in the Competition Act, i.e. more than half of the shares or members' interest.

42. Moreover, it is the Competition Authorities who are concerned about concentrations of ownership and control and which are utilising new powers afforded through recent amendments to the Competition Act to address such concerns. ISPA submits that the preferred outcome is for the Authority to defer to the established mergers and acquisitions jurisdiction of the Competition Commission in respect of matters of control.

[4] Findings Document and Position Paper para 13.9

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Contraventions and Penalties (Regulation 8)

43. ISPA submits that the proposed penalties are unduly harsh taking into account the difficulties with compliance as set out above.

44. ISPA also questions the creation of an offence under the Draft Regulations which is criminal in nature both in terms of whether this is proportionate and necessary and in terms of its lawfulness.

Transitional Period (Regulation 9)

45. Twenty-four months is too short a period in which to reasonably expect compliance, particularly given the proposed sanctions to be imposed where a licensee does not have the required HDG or level 4 certification or 30% ownership by Black Persons.

46. As discussed above, setting the benchmark for a "control interest" at 20% will result in many licensees having to file applications for transfer of ownership of a licence or transfer of control over a licence.

47. ISPA submits that:

    47.1. This period should be extended to 48 months or four years from date of finalisation of the Draft Regulations, in both sub-regulation 9(1) and 9(2).

    47.2. Given the lengthy period of time taken for the Authority to finalise any required approval for a transfer of ownership of a licence or transfer of control over a licence, compliance should be linked to the submission by a licensee of an application or notification which would result, if approved, in the licensee becoming compliant with equity ownership requirements.

48. The requirement to show 50% compliance within 12 months must be reassessed.

    48.1. ISPA as is unclear what "50% of a level 4 BEE rating" means in practical terms. What is the target to be achieved with reference to the applicable scorecard?

    48.2. For the reasons set out above, it is unreasonable to expect the transactions required for compliance to be completed within a 24-month period, much less a 12-month period.

48.3. This is captured in the following submission received from an ISPA member:

"For those that don't already have 15% black ownership realistically they are not going to do two half deals over a two-year period. This means effectively we only have 12 months to find an equity partner, negotiate, and conclude a transaction. This is an unrealistic timeframe. It's also particularly problematic considering the current economic climate to expect black entrepreneurs to seek funding on such short notice. Until the economy improves the feasibility of concluding such a transaction even within 2 years is slim.

The other problem is that once engaging in a BEE transaction, licensees are going to want to do transactions ideally more than 51%, however, such transactions are subject to ICASA approval. ICASA has demonstrated turnaround times of well over 12 months.

To place an effective requirement of 12 months to conclude such a deal and to obtain regulatory approval as well is impossible. The impact of this is that ICASA's policy while encouraging deals of exactly 30% will, without doubt, discourage deals over 30%."

48.4. Another member submission highlights the processes required to be undertaken before compliance is attained:

"1. Regulation gets promulgated on 1 September 2020.

2. Licensee's financial year is 1 Mar 2020 to 28 Feb 2021.

3. Licensee needs a few months to plan a BEE strategy in line with the actual target prescribed in the final regulation. Full implementation would take a few months to scale up to. There is no way to practically achieve target on the financial year for which more than six months have already passed (prior to full implementation of the BEE strategy).

4. For financial year 1 Mar 2021 to 28 Feb 2022, the licensee will finalise financials and its financial audit 6 months from year-end (31 Aug 2022) and the BEE audit will follow thereafter (as the BEE auditors will want to see that the financials have been audited as a requirement of their own audit process), potentially taking another couple of months (i.e. until 31 Oct 2022) before the audit is both completed and certificate signed off and issued.

5. In practical terms, the licensee will only receive their certificate by the end of October 2022, more than TWO YEARS after the regulation came into effect and after the compliance deadline,

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notwithstanding that the licensee implemented a BEE strategy in accordance with the targets as soon as the regulations were promulgated."

49. ISPA notes – by way of offering a reference point for the Authority – that the Implementation Guidelines for the Mining Charter 2018[5] state that a mining right holder must increase its BEE shareholding from a minimum of 26% to 30% once off or progressively within the 5-year transitional period.

The COVID-19 National Disaster

50. As an affected party itself, the Authority will appreciate the economic and commercial challenges in the current environment as well as predictions of severe recession notwithstanding measures taken by government to stimulate the economy.

51. This is a very real consideration for licensees that become obliged to enter into equity-related transactions in order to comply with finalised regulations within a defined period and subject to harsh sanctions for non-compliance.

52. ISPA anticipates that it will be extremely difficult to fund empowerment transactions in the short-to-medium term, with liquidity shortages and ongoing uncertainty making debt expensive and guarantees hard to give.

53. In its consideration of the finalisation of the Draft Regulations and the transitional period to be applied, the Authority is requested to take the fall-out from the COVID-19 National Disaster into account.

[5] Implementation Guidelines for the Broad Based Socio- Economic Empowerment Charter for the Mining and Minerals Industry, 2018, para 4.2. Available from https://www.gov.za/sites/default/files/gcis_document/201812/42122gon1399.pdf

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Repeal of prior regulation

54. The Draft Regulations erroneously omit to repeal the ICASA Regulations in respect of the Limitation of Ownership and Control of Telecommunication Services in terms of section 52 of the Telecommunications Act published on 16 January 2003.

Conclusion

55. ISPA thanks the Authority for its consideration of these submissions.

ISPA CHAIRPERSON