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16 July 2012

Mr. Charles Punaha
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NICTA
Frangipani Street, Hohola
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Dear Mr. Punaha,

Re: Public inquiry into the need for a Retail Services Determination (RSD) regarding certain mobile telephony services

The submission attached is in response to the redacted version of bemobile's submission. Digicel understands that the bemobile submission is the only submission that has been made with respect to NICTA's Second Discussion Paper of 4 May 2012 in its RSD Public Inquiry.

Relevantly, despite this being a "Public Inquiry", the only party that appears to be interested in having Digicel's retail rates regulated is bemobile, a competitor of Digicel. No other party has provided any evidence or analysis to support the regulation of Digicel's retail rates. On the contrary, the only other party to provide a submission in this inquiry, Telikom, indicated its opposition to retail regulation. In addition, PNG's competition regulator, the ICCC, found that Digicel's conduct is unlikely to be anti-competitive.

1 The public inquiry has been framed incorrectly

This Public Inquiry was initiated as a result of a complaint by bemobile about pricing practices of Digicel that bemobile alleged were anti-competitive. Bemobile's submission pursues that line of argument. In the Terms of Reference set out in NICTA's First Discussion Paper,NICTA specifically focuses on this complaint, i.e. on whether Digicel's pricing of off/on-net calls is an abuse of dominance or otherwise anti-competitive. Although NICTA's Second Discussion Paper purports to conclude that the proposed RSD satisfies the retail regulation criteria, much of the Second Discussion Paper is devoted to the issue of whether Digicel has substantial market power and whether Digicel's pricing conduct is anti-competitive. Very little attention is given to whether the RSD would promote the efficiency objective of the NICT Act. Indeed, NICTA appears to conflate the efficiency objective with the competition objective. Having concluded (wrongly) that Digicel's pricing conduct is anti-competitive, NICTA disposes of the efficiency objective in a single paragraph, with a breathtakingly sweeping (and unjustified) claim that:

> "If Digicel's past or future investment are based on the low level of competition … then that investment will tend to be inefficient."

This completely misunderstands the important concept of efficiency. At a fundamental level, efficiency increases simply when more output is possible for the same amount of input. This requires increased investment and productivity, which Digicel has been delivering.

Bemobile's submission does nothing to correct this error on the part of NICTA and remains focussed on the competitive harm that it continues to allege is being caused to its business by Digicel.

Even the narrow question of whether Digicel's pricing conduct is anti-competitive has been framed incorrectly. NICTA applies network effects models that assume the relevant market is saturated. As Cave & Doyle(2012)[1] points out, the models do not apply in the PNG context where mobile penetration is still low.

Digicel does not deny the relevance of competition to NICTA's decision whether to recommend making an RSD. However, framing the inquiry in terms of market power and competition is fundamentally misconceived. This frame ignores PNG's historical, economical and developmental context. In particular, the context that the mobile market in PNG has only been effectively liberalised for five years, and that the key developmental goal in terms of ensuring that the ICT industry contributes to the greatest extent to PNG's long-term social and economic development is to raise mobile penetration in PNG to 100% as soon as possible.

The competition frame also causes NICTA to pay insufficient attention to the impact of the RSD on the things that matter, such as mobile penetration and the impact this has on the wellbeing of the PNG people.

Digicel submits that the public inquiry must be reframed. At a minimum, NICTA should view Digicel's behaviour and those of bemobile through the lenses of productivity, efficiency and growth. This broader frame encompasses both competition and efficiency. It gives NICTA a coherent frame for assessing likely benefits and likely detriments that takes full account of wellbeing (of both existing and future mobile subscribers) and the contribution that increasing mobile penetration makes to PNG's long-term economic and social development.

2 NICTA cannot confirm its proposed conclusion that the RSD satisfies the retail regulation criteria based on the evidence and analysis available to it

Bemobile wants NICTA to proceed immediately to a conclusion that the proposed RSD (with extensions urged by bemobile) meets all of the retail regulation criteria. Digicel submits that NICTA would be committing a profound error of law if it were to take this step. The case for finding that the RSD meets the retail regulation criteria is far from made. To date, the inquiry has focused primarily on whether Digicel has substantial market power and whether Digicel's pricing adversely affects competition. Even this issue has not been properly addressed as NICTA and bemobile have misconstrued the competitive environment, ignoring the fact that the market is not saturated.

1 Cave & Doyle 2012, On-Net/Off-net Price Discrimination and Digicel in PNG: Independent Opinion, submitted to NICTA in the public inquiry on the RSD.

At a minimum, the following tasks remain outstanding before NICTA can be satisfied the RSD meets the retail regulation criteria:

- **Task 1 – review the competition models used:** First, NICTA must review its conclusion that Digicel's pricing is anti-competitive. The models that NICTA rely on to reach this conclusion does not apply in the PNG context where the mobile market is far from saturation. Even those models do not imply that price discrimination is inherently anti-competitive. Most forms of price discrimination are in fact normal competitive behaviour. It is a legitimate part of the competitive process for mobile operators to internalise network effects by charging a lower rate for on-net traffic.
- **Task 2 – study the productivity and efficiency of the mobile sector:** Second, NICTA shouldinquire into the productivity and efficiency of the mobile sector. There is an assumption in NICTA's analysis that all mobile operators in PNG are equally efficient. If this assumption is unwarranted, NICTA cannot assume that the only issue that matters is whether bemobile can compete. There is a prior issue of whether bemobile is an effective operator or competitor and whether its failings are as a result of its own investment and management decisions. Indeed, there is a legitimate question as to whether bemobile should remain in the market at all, or whether it should exit the market altogether so that more efficient rivals can take its place. It would be ironic if market failure arises in PNG as a result of regulatory protectionism that results in the introduction of barriers to exit. In competitive markets, inefficient incumbents should be taken over by more efficient entrants.
- **Task 3 – assess how the RSD affects mobile penetration:** Third, NICTA must pay greater attention to the goal of raising mobile penetration quickly, given the centrality of this goal to ensuring that the ICT sector contributes to the greatest extent possible to the long-term term economic and social development of PNG. At a minimum, NICTA should clearly identify a base case scenario for the path towards 100% mobile penetration in PNG. Neither bemobile nor NICTA have indicated howthey expect the imposition of this RSD to contribute towardsgreater mobile penetration and by when this should be achieved. Such a base case is essential for NICTA totake proper account of how the RSD will affect mobile penetration in PNG.
- **Task 4 – assess the likely benefits and likely detriments in terms of wellbeing:** Fourth, the likely benefits and likely detriments of a proposed RSD must be judged in terms of its impact on people's lives. The comparative analysis undertaken in the Second Discussion Paper is far from adequate. Not all benefits and detriments can be quantified,however a reasonable attempt at such quantification should be made. Otherwise, NICTA risks making decisions that are not accountable to reality and that may actually create more harm than good.

3 There is no case for continuing with the public inquiry

Each of these tasks is non-trivial. NICTA must consider whether there remains a case for continuing with the public inquiry. The answer is "no" for the following reasons:

- The prospect of finding an RSD that meets each retail regulation criterion is extremely remote.

- Even if NICTA were to find that Digicel's pricing has an adverse effect on competition, the proposed RSD plainly overreaches the proper ambit of regulation.
- Supposing there were an RSD that met every retail regulation criterion, Digicel submits that its current pricing is likely to be very close to meeting the requirements of that RSD.
- In any event, NICTA has no objective basis for determining what pricing is optimal having regard to the welfare benefits of raising mobile penetration in PNG. Under these circumstances, NICTA should simply let Digicel set prices on commercial grounds. Digicel has strong incentives to raise mobile penetration in PNG as quickly as possible, and any regulatory intervention is likely to cause unjustifiable delays.

NICTA should simply conclude there is no case for regulating the retail price of mobile services. At most, NICTA should conclude it is premature to regulate retail prices, and defer revisiting this matter until after mobile penetration reaches (say) 80%. (Experience overseas indicates that saturation is likely to be above 100%.)

Digicel urges NICTA to guard against a tendency to think of the resources consumed in the public inquiry as a "loss" unless a decision to recommend an RSD is made. Although Digicel believes this public inquiry was given unjustified priority, it has usefully exposed the shallowness of bemobile's arguments and demonstrated the lack of public support for bemobile's complaints about Digicel's pricing. If, after conducting a comprehensive public inquiry, NICTA concludes that the RSD is unwarranted, this would strengthen public confidence in the integrity of NICTA's decision-making process.

Yours sincerely

[Signed]

John Mangos
Chief Executive Officer

Digicel

DIGICEL (PNG) LIMITED

Submission to NICTA

Public inquiry into the need for a Retail Services Determination (RSD) regarding certain mobile telephony services

[REDACTED]

Monday, 16 July 2012

This submission is provided to NICTA for the purpose of the current public inquiry only and may not be used for any other purpose

1 Introduction

1 This submission is in response to the redacted version of bemobile's submission.

2 The submission contains Digicel's general views in relation to bemobile's submission and includes a number of further specific comments, which are set out in Schedule 1.

3 In addition, Digicel's independent advisors who have signed a non-disclosure and confidentiality agreement with bemobile have provided some separate comments in relation to that confidential information. In order to protect the confidentiality of bemobile's information, those comments are being made directly to NICTA.

4 This submission contains information that relates to Digicel's commercial dealings with bemobile and which is highly commercially sensitive and confidential to Digicel. Accordingly, two versions of the submission have been provided – redacted and un-redacted. The un-redacted version of the submission must not be published by NICTA but may be provided to independent experts and advisors of bemobile who have executed satisfactory non-disclosure and confidentiality agreements with Digicel.

2 Preliminary matters

2.1 Absence of public participation in the Public Inquiry is telling

5 Digicel understands that the bemobile submission is the only submission that has been made with respect to NICTA's Second Discussion Paper of 4 May 2012 in its RSD Public Inquiry. Relevantly, despite this being a "Public Inquiry", the only party that appears to be interested in having Digicel's retail rates regulated is bemobile, a competitor of Digicel. No other party has provided any evidence or analysis to support the regulation of Digicel's retail rates. In fact, over the course of the entire public inquiry, only bemobile has supported regulation. Telikom's only submission to the public inquiry indicated its opposition to retail regulation. NICTA also received a letter from the ICCC (reproduced in Attachment A)statingits unequivocal conclusion that Digicel's conduct is unlikely to be proved to be anti-competitive.

6 Thus not only is there an absence of public interest (let alone participation) in the public inquiry, PNG's competition regulator has found that there is no competition issue to be pursued in terms of protecting consumer interests. This is relevant given the purpose of the Part of the Act under which NICTA is proposing to regulate Digicel's retail pricing. Section 156(a) states:

> "This Part sets out a regime for the protection of retail customers and the regulation of the pricing of retail services."

7 To the extent that no person other than a competitor of Digicel's has shown any interest in this proceeding and given that PNG's competition regulator finds that Digicel's conduct is unlikely to be anti-competitive,either there is no real issue to be addressed, or NICTA has misapplied the legislation.An impartial observer would reasonably conclude that it is the commercial interests of a single competitor thatis the real focus, not the protection of retail customers.

2.2 Absence of a formal confidentiality regime is harmful to natural justice and procedural fairness

8 Digicel remains concerned aboutthe absence of a formal regime to manage the controlled and appropriate disclosure of parties' confidential information has resulted in a decision-making process that is fundamentally flawed. The approach adoptedto date has been*ad hoc*. While NICTA has provided bemobile's confidential submission to Digicel's external advisers, the ongoing uncertainty over NICTA's treatment of confidential information has deterred Digicel from presenting its full case against the imposition of a Retail Services Determination ("**RSD**").

9 Digicel also notes that bemobile's un-redacted submission was only provided to Digicel's advisors for review less than a week before submissions were required to be provided. Thisis unsatisfactory and effectively denies Digicel a reasonable opportunity to review and correct, contradict or comment on the evidence and arguments that have been made against Digicel's interests.

10 Accordingly, Digicel reserves all its rights as a result of the denial of natural justice and procedural fairness arising from the failure and refusal of NICTA to establish an appropriate (or any) confidentiality regime to manage the controlled and appropriate use of confidential information. The provision of this cross submission by Digicel should in no way be taken to constitute a waiver in any form whatsoever of its rights arising from a denial of natural justice and procedural fairness on the part of NICTA.

2.3 The proposed RSD is harsh or oppressive, and not warranted nor reasonably justifiable

11 Bemobile has characterised itself as the entrant into PNG market and that Digicel is thwarting its attempts to compete. This is simply untrue. The reality is that bemobile is itself (albeit with a relatively new ownership structure) the mobile arm of TelikomPNG, the former Government owned monopoly telecommunications provider. Digicel entered the PNG market, made significant investments and provided a world class mobile telecommunications service to the people of PNG, many of whom did not previously have access to telecommunications services of any kind. Unsurprisingly, the people of PNG supported Digicel and chose to use the services it provided. Digicel should not be punished for its efforts. Nor should bemobile be rewarded by being provided with a soft competitive environment by NICTA.

12 Regulating Digicel in the way that has been proposed by NICTA and is supported by bemobile would be unconstitutional. Section 41(1) of the Constitution provides:

> “*Notwithstanding anything to the contrary in any other provision of any law, any act that is done under a valid law but in the particular case–*
>
> *(a) is harsh or oppressive; or*
>
> *(b) is not warranted by, or is disproportionate to, the requirements of the particular circumstances or of the particular case; or*
>
> *(c) is otherwise not, in the particular circumstances, reasonably justifiable in a democratic society having a proper regard for the rights and dignity of mankind,*
>
> *is an unlawful act.*”

13 Digicel submits that, based on the self-serving arguments that have been proffered by bemobile to date, it would be harsh or oppressive (within the meaning of that term as it is used in section 41 of the Constitution) for NICTA to impose the RSD only on Digicel when it is likely that the sole beneficiary of that RSD would be Digicel’s commercial rival. Further, Digicel submits that the regulation proposed by NICTA is harsh and oppressive for the following reasons:

(a) The regulation would essentially be punishing Digicel for complying with its license conditions by completing its roll-out obligations and maintaining an efficient operation which has so far helped Digicel to be more successful in the market than its inefficient competitors that have chosen to build less coverage.

(b) The regulation would serve to reward or “featherbed” inefficient operators for failing to complete their roll-out obligations and soften the competitive environment in the mobile sector.

(c) The proposed regulation would give an unfair advantage to inefficient operators but harm most customers in the form of higher call prices. Around 80% of all mobile subscribers of PNG would be affected.

(d) The regulation would have the effect of diverting resources from Digicel to its less efficient rivals, protecting inefficient competitors and reducing productivity and efficiency in the mobile sector.

14 Digicel submits that the regulation proposed by NICTA is not warranted, within the meaning of that term it is used in section 41 of the Constitution, for the following reasons:

(a) The proposed regulation would in fact harm competition and customer welfare in that it would:

- raise the price of mobile calls currently enjoyed by 80% of mobile users in PNG;
- shelter inefficient operators from the discipline of real competition;
- soften price and non-price competition to the detriment of customers, which is also contrary to the objectives of the National ICT Act;
- impedegrowth of mobile penetration in PNG as it discourages investment in the mobile sector. PNG only has a mobile penetration

coverage of 30% which is well below regional average and further investment in coverage is required to increase penetration;

- restrictDigicel's efficient use of its network infrastructure, particularly during off-peak hours; and
- delay social and economic development of Papua New Guineans through the medium of mobile service by retarding investment in infrastructure.

(b) In arriving at its decision to recommend the regulation, NICTA failed to refute claims that mobile competition in PNG is healthy and that it is bemobile's inability to compete with Digicel as a direct result of its inefficient operation due to incompetence of its management that is affecting its operations. By the same token, NICTA failed to refute Digicel's claims that an equally efficient rival could profitably match Digicel's pricing or otherwise succeed in the market against Digicel.

3 Scope of the RSD should not be expanded

15 By it submission, bemobile has attempted to expand the scope of the RSD. This is unjustified and illustrates the danger of "regulatory creep". Since the proposed RSD is itself unjustified, widening the scope of the regulatory intervention further accentuates the reasons for not implementing the proposed RSD, would create additional detriments of regulation, and risks additional unintended consequences. Without seeking to be exhaustive, the reasons why the RSD and its further expansion are unjustified include that:

(a) Mobile penetration in PNG is low and prohibiting Digicel fromdiscriminating between on-net and off-net calls would slow down market expansion by weakening Digicel's incentives to expand coverage and attract new customers;

(b) Retail regulation carries a high risk of becoming self-justifying and irreversible, while the task of raising mobile penetration is becoming more challenging and will not be helped by regulation;

(c) Reducing on-net tariffs to internalise network effects within calling circles is a natural outcome of competitionamong mobile networks, and encourages networksto seek out new subscribers;

(d) Digicel's on/off-net price differential is not excessive given the present stage of development of the PNG mobile market when the market is far from saturation;

(e) bemobilehas given no evidence that it is efficient or an effective competitor,orthat an efficient rival could not profitably match Digicel's pricing or otherwise succeed in the market against Digicel. If bemobile currently struggles to match Digicel's pricing, it is because of bemobile'sinefficient operations. Citifon appears to have little difficulty undercutting Digicel'sand bemobile'spricing.

(f) At no stage during the public inquiry has NICTA sought to inquire into the efficiency of bemobile's and Citifon's operations. In a competitive market, efficient rivals gain market share at the expense of less efficient rivals, and this competitive process benefits consumers in the long run. Thus any finding that Digicel has market power or that price discrimination is a barrier to expansion could be unjustified if its rivals are inefficient.

(g) bemobilehas not refuted the reasonable hypothesis that Digicel'smarket share reflects its significant investment in building a network with larger coverage and a more efficient operation in terms of sales, distribution, marketing and customer care.Regulation on that basis would only serve to reduce the incentive of all mobile operators to invest in all of these things, to the detriment of consumers in PNG. It is highly relevant that bemobile was the incumbent mobile operator and thatboth Digicel and bemobile were faced with the same initial network roll out obligations. While Digicel honoured its obligations, bemobile did not. NICTA's regulatory response to bemobile's failure was to relax the rollout obligations as they applied to bemobile. In Digicel's submission this was inappropriate and should certainly not form the basis for adopting a view that Digicel had somehow achieved an unassailable advantage over bemobile because it has a more extensive network.

(h) Observable trends in the market suggest that Digicel's market position is being eroded. We refer to the data presented in Table 2 at page 30 of NICTA's second discussion paper.

(i) The proposed RSD will soften price and non-price competition, to the detriment of consumers. Bemobile knows that Digicel will be constrained in competing by lowering on-net tariffs and will have reduced incentives to expand coverage and attract new customers. Knowing this, price competition will weaken, and bemobile will also have weaker incentives to expand its coverage, improve its services, and attract new customers. The RSD also weakens Digicel's incentive to seek out new mobile subscribers since Digicel would be forced to share with bemobile any benefit that the additional subscribers bring in terms of network effects.

(j) The proposed RSD will lead to inefficient use of existing infrastructure as it will strongly discourage Digicel from offering discounted prices to encourage new customers to join the network and to boost the volume of traffic on its network during times of the day when demand is low.

(k) To the extent the RSD diverts resources from Digicel to its less efficient rivals, it will lead to a reduction in productivity and efficiency in the mobile sector. NICTA must confront the risk that regulation will serve to protect inefficient competitors.

(l) NICTA has notundertaken a comprehensive assessment of the benefits and detriments associated with the proposed intervention. There is a striking absence of any consideration of the likely impact of the proposed intervention on mobile penetration and on consumer welfare. Bemobile has also failed to provide any evidence to support the views that have been expressed by NICTA.

16 NICTA should not assume that the RSD would have no effect on Digicel's long-term investment strategy in PNG. Even if NICTA believes the RSD will have a modest impact on Digicel's return on assets, a decision to regulate retail mobile services ahead of more pressing concerns (such as international connectivity) will lead Digicel's investors to conclude that NICTA is, at best interventionist, and at worst reckless (especially if the scope of the RSD is expanded as suggested by bemobile).

17 In short, the RSD will have a lasting and uncertain impact on the "regulatory risk" that goes beyond its intended effects.

18 Digicel has yet to determine its commercial response to the RSD. There is a real prospect that Digicel will decommission marginally profitable towers and stop building out its network. In any case, greater regulatory risk will reduce the incentive to invest in PNG.

4 Interconnection rates are not the issue

19 Digicel notes for the record that bemobile has been misleadingby selectively quoting NICTA's Response Report (of 4 May 2012). Bemobile says (at p 13) NICTA staff state that they "have no reason for assuming that the current MTRs actually (*sic*) reflect actual costs" and then alleges that the MTR is above cost. The statement from the NICTA Response Report was in response to bemobile's complaint about NICTA using the MTR as a proxy for cost and is reproduced in full here:

> "*In the absence of any other information, NICTA staff considered that the existing mobile termination rates to be an adequate proxy for costs (for the purposes of its preliminary analysis) because those rates were originally set by the ICCC through an arbitration process in 2008. NICTA staff agree that a cost model would be a better source but none was (or is) available to NICTA staff.*
>
> *NICTA staff have no reason for assuming that the current MTRs accurately reflect actual costs.*
>
> *NICTA staff understand that the Samoan cost model (to which Ms Lanigan referred) is not particularly relevant to PNG, particularly given the very*

different topology in PNG, stating that the costs in PNG to those reflected in the Samoan cost model."

20 The entire statement shows that NICTA staff considers the MTR to be an adequate proxy for costs, albeit not accurately. In fact, the MTR may be less than actual costs as Digicel has continued to build out its network in high cost areas of PNG. Nothing in the NICTA Response Report indicates a view that the MTR is above cost.

21 Bemobile also misrepresents how the MTRs were arrived at. It alleges that the MTRs are artificially high due to Digicel's "greater negotiating power" and asserts that had agreement not been reached in a timely manner in 2010, Digicel would suspend interconnection.

22 The MTR that was agreed between Digicel and bemobile was well within the range of the possible values estimated by the ICCC in an interim determination. Bemobile offered to interconnect at the prices set out in the Interconnection Agreement and the offer was accepted by Digicel. The allegation that Digicel had pressured bemobile to accept the MTR is not only incorrect, it completely misrepresents the bargain.

23 Bemobile was, at the time, apparently very happy interconnect at the MTR it offered. In fact, bemobile rejected Digicel's offer to enter into a 5 year agreement on the MTR, and instead asked Digicel to enter into a 10 year agreement on the MTR. It would be odd for bemobile to insist that Digicel enter into a 10 year agreement had bemobile thought that the MTR rate was above cost.

24 Not only was the MTR sought by bemobile, it was also determined by the ICCC to be in compliance with the charging principles in force and the Telecommunications Act. In a letter dated 5 July 2010 to both Digicel and bemobile, the ICCC said:

> "The Commission had now completed its review of the Direct Interconnect Agreement between Digicel and bemobile dated 17 April 2010, pursuant to Section 86 of the Telecommunications Act (**Act**), and is satisfied that the interconnect agreement complies with the charging principles in force and the Act.
>
> Consequently, the Direct Interconnection Agreement between Digicel and bemobile has been accepted by the Commission."

25 Attachment B isa copy of the ICCC's letter.

26 Digicel has never threatened to suspend interconnection in order to attempt to force bemobile to agree on the MTR.Telikom, with whom the interconnection agreement on MTR had originally been entered into, failed to pay Digicel for interconnection for over 9 months. Telikom's position was that bemobile was responsible for interconnect payments. Neither bemobile nor Telikom would pay for interconnect. Digicel suspended interconnection with Telikom after not receiving payment from Telikom for over 9 months. Even then, Digicel continued to send

interconnect traffic to bemobile (via Telikom's network) and only blocked interconnect traffic from Telikom due to non-payment.

27 During a meeting held on 31 March 2010 between all stakeholders (including the Department of Communications and PANGTEL), bemobile obtained an injunction ordering Digicel to lift the suspension. The injunction was dissolved not long after (on 8 April 2010) after Digicel explained that it had not been paid for interconnect traffic for over 9 months. The court (Salika DCJ) said to the effect that bemobile and Telikom should sort out who is responsible for paying interconnect, and Digicel was entitled to be paid for providing termination access. Salika DCJ further stated that the public had been made to suffer because Telikom, bemobile and the ICCC had been unable to sort out the matter. As soon as Digicel was paid by bemobile and the parties entered into a direct interconnect agreement (at the reduced MTR proposed by bemobile), Digicel immediately resumed receiving interconnect traffic from bemobile. This happened on 17 April 2010.

28 It is also highly misleading of bemobile to imply that the interconnection payments it makes to Digicel are a cause of its apparent financial woes[2]. Digicel's records show that in the twelve months to 31 March 2012, Digicel invoiced bemobile **[XXXXX_redacted_XXXXX]** for interconnection services. This was offset by bemobile's charges to Digicel **[XXXXX_redacted_XXXXX]** resulting in a net payment by bemobile to Digicel of **[XXXXX_redacted_XXXXX]**. However this is only part of the story. In addition to the interconnection payments and receipts, bemobile also made a net margin on each and every call and message to the Digicel network. Digicel estimates that in the same period, **[XXXXX_redacted_XXXXX]**in retail revenue from calls and messages to the Digicel network. Far from being out of pocket, bemobile benefited from its interconnection relationship with Digicel by more than **[XXXXX_redacted_XXXXX]**during the twelve month period.

29 Bemobile also implies that bemobile was somehow "forced" to pay for the interconnection links between it and Digicel. The interconnection agreement was negotiated freely by bemobile, including with respect to the treatment of interconnection links. Bemobile's apparent additional complaint in relation to the provision of interconnection links that Digicel is attempting to misapply the provisions of the agreement with respect to additional Handover Points is similarly vexation and without substance. The interconnection agreement contains a set of dispute resolution provisions to deal with any difference of view over the interpretation of the Agreement. To the extent that bemobile has any issues with respect to the application of the Agreement it should address them through the mechanisms agreed rather than through an unrelated regulatory proceeding.

[2] Bemobile submission, page 14.

5 Price discrimination between on-net and off-net calls is not anti-competitive

30 Bemobile has attempted to characterise this proceeding as being about competition and the protection of bemobile as a competitor. However, Digicel respectfully submits that NICTA's primary role is to ensure that the ICT industry contributes to the greatest extent possible to the long-term economic and social development of PNG. It is not NICTA's role to protect competition per se. Competition is not the end goal, but at most the means to something else.

31 Digicel does not deny the relevance of competition to ensuring that the ICT industry contributes to long-term economic and social development of PNG. However, bemobile focuses exclusively on retail prices and substantially ignores efficiency concerns and the broader welfare impact of reduced mobile penetration that are relevant under the retail regulation criteria. Furthermore, bemobile misconstrues what it means to promote effective competition in some fundamental ways:

(a) first, bemobile confuses protecting the competitive process with protecting its own competitiveness;

(b) second, bemobile assumes that any price discrimination is anti-competitive; and

(c) finally, bemobile assumes that network effects are always anti-competitive.

32 It can be difficult to distinguish between protecting the competitive process and protecting competitors. NICTA must act cautiously.

33 A good example is "predatory pricing", where an incumbent may respond to new entry by pricing below the new entrant's average cost, but above the incumbent's marginal cost. In this case, the entrant cannot profitably remain in the market for long and will likely exit the market. This may appear to be anti-competitive behaviour,however, it is reasonably well-established in competition law that the incumbent's behaviour is in fact pro-competitive. In competitive markets, more efficient firms gain market share at the expense of less efficient firms. The fact that less efficient firms are prevented from entering the market may appear to be harsh, but nothing more than a feature of competitive markets.

34 Competition law does acknowledge that under certain conditions, very low prices can be anti-competitive. Even so, the courts are wary of any intervention to discourage incumbents from reducing prices, knowing that there is a significant danger such intervention will have the perverse and unintended effect of dampening price competition and denying consumers the benefits of lower prices. Accordingly, in the United States, predatory pricing is prohibited only if certain strict conditionsare met.

35 In the present public inquiry, bemobile and NICTA have sought to make a case that Digicel's pricing conduct is anti-competitive. The case is based on a theory about network effects. Specifically, with on-net pricing, subscribers will prefer to join the larger network due to network effects. The larger network therefore enjoys an advantage over smaller rivals only because of the size of its network. Given this, there is someeconomic literature suggesting that the larger network may have the ability touse price discrimination with the intention of harming smaller rivals.

36 However, the economic literature on on-net pricing requires careful interpretation. There is nothing inherently anti-competitive about network effects per se. Nor is there anything inherently anti-competitive about a network setting prices in order to internalise network effects among members of calling circles (i.e. people who call each other often). Indeed, the literature acknowledges that in competitive markets, network operators will do their best to internalise network effects, and on-net pricing can be seen as a competitive response that internalises the network effects among members of calling circles. This is part of a competitive process. Nothing in the literature implies that this is anti-competitive per se.

37 At most, the literature seeks to explore what pricing behaviour will emerge if the larger network seeks to go beyond internalising network effects in order to restrict the smaller firm's profitability, possibly with a view to driving out the smaller firm. This behaviour is similar to "predation"[3]. The notion of predation here is the Ordover and Willig (1981) definition of predation, being a:

> "response to a rival that sacrifices part of the profit that could be earned under competitive circumstances, were the rival to remain viable, in order to induce exit and gain consequent additional monopoly profit."

38 There is a close (but not exact) connection here with the more established concept of predatory pricing. For Digicel's pricing behaviour to be regarded as "predatory" based upon the above definition, it would be necessary (but not sufficient) for NICTA to show that:

(a) ("**profit sacrifice**") Digicel has sacrificed part of the profit that could be earned;

(b) ("**recoupment**") in order to induce exit and gain additional monopoly profit.

39 Nowhere in the public inquiry has NICTA sought to inquire into whether Digicel has sacrificed profit in order to induce exit. At best, all that NICTA has found is that there are network effects, and Digicel's pricing seeks to internalise that network effect.

40 Competition regulators are rightly cautious about finding that pricing to match or undercut a new entrant is anti-competitive even if the incumbent firm's intention is

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3 Hoernig 2007, On-net and off-net pricing on asymmetric telecommunications networks, **Information Economics and Policy 19 (2007), p 180.**

to "harm" the rival. This is because low prices and harming rivals are the hallmarks of competition. Similarly, NICTA should be cautious about finding that price discrimination (even if in excess of "objectively justifiable cost") is anti-competitive. Price discrimination implies lower prices for end users with lower willingness to pay and is generally welfare enhancing.

41 As discussed above, the distinction between competitive behaviour and predatory behaviour is difficult to establish in practice. It is therefore easy to mistake "competitive behaviour" for "predatory behaviour", and easy to confuse "protecting competition" with "protecting competitors". NICTA should act cautiously, especially in relation to off-net vs on-net pricing where the issues are complex and not well understood, especially in the context of developing economies such as PNG's. To Digicel's knowledge, no competition regulator has to date made out a case that pricing to internalise network effects is anti-competitive.

42 We also note that PNG's competition regulator, the Independent Consumer and Competition Commission ("**ICCC**"), was asked by bemobile to inquire into Digicel's pricing behaviour. In the ICCC's letter of 22 February 2012 (attached), the ICCC said:

> "The Commission has examined the issues against the elements of s.50 and s.58 of the *Independent Consumer and Competition Commission Act 2002* ("ICCC Act") and concludes that the conduct of Digicel is unlikely to be proved to have anti-competitive purposes; hence, they are unlikely to amount to a contravention of the ICCC Act."

43 The ICCC has considerable experience on competition matters. Digicel respectfully submits that NICTA should defer to the ICCC's views on this complex matter and adopt the ICCC's conclusion that Digicel's conduct is not anti-competitive. Digicel also notes that the ICCC has chosen not to make any submissions in the current Inquiry.

44 Digicel reiterates that its current position as the leading mobile operator in PNG is neither inherited from a government financed monopoly nor acquired during a period of legal monopoly. Digicel entered the market as a new entrant, competing with more established operators who had at least a 5 year opportunity (that included network rollout obligations) to build a national mobile network. Digicel's current market position was won by investing in a reliable national mobile network and establishing an effective sales and distribution network, marketing its services to new mobile subscribers and providing high quality customer care.

6 The proposed RSD would lead to inefficiency and loss of productivity

45 Much of bemobile's submission has focussed on competition and static efficiency. Bemobile has paid very little attention to the impact the proposed RSD will have on

dynamic efficiency, including efficient investment in ICT infrastructure, and efficient use of that infrastructure. This is perhaps unsurprising as even a cursory analysis would show that including these considerations would strongly undermine the case for regulation.

46 Any investment for which the social returns exceed social cost is efficient. Since mobile investments quite clearly have positive externalities, any investment that is privately profitable must be efficient from a social perspective.

47 bemobile's apparent presumption that efficient investment can only take place in competitive markets is unjustified and incorrect. Even if the mobile market were a monopoly (which it obviously is not), investments that raise mobile penetration and are privately profitable would be efficient. There is no presumption in economics that competitive markets are necessary for efficient investments.

48 The proposed RSD would lead to inefficiency and loss of productivity in the following respects:

(a) (**dynamic inefficiency**) First, it would divert resources away from Digicel to bemobile and Telikom. As the latter two have a poor track record of making efficient investments, the overall result of the RSD would be to reduce efficient investment in the ICT sector.

(b) (**productive efficiency**) Second, the RSD (as currently drafted) would prevent Digicel from optimising the use of its network, especially during off-peak periods. Absent the RSD, Digicel would set prices to stimulate on-net traffic during off-peak periods. This decision would be made independently of the price charged for off-net calls. The RSD ties Digicel's on-net tariff to its off-net tariff. The effect is to force Digicel to take account of the impact its on-net pricing has on its off-net margins, thereby deterring Digicel from setting its on-net tariffs optimally.

(c) (**technical inefficiency**) Third, the RSD would prolong the time required for bemobile to redress its existing internal management and investment strategy failures. Bemobile does not have stable management; its owners and managers appear to have very short horizons and are unable to make long-term commitments. The RSD will only shield bemobile from competition and encourage bemobile to rely on regulatory intervention rather than address its own internal failures.

49 We would observe that when a market is newly liberalised, it is normal to find a large divergence in the productivity and efficiency of the firms competing in the market. (See Schedule 2.) A new entrant (such as Digicel) brings into play organisational efficiencies, know-how, managerial competence and new talent that is previously unknown in the market. These competencies are not easily transferable across firms. Some incumbent firms (such as Telstra in Australia) succeed in adapting to the newly liberalised environment while other firms (such as

the State-owned banks in Australia which collapsed following liberalisation of the financial sector in the 19080s) fail to adapt, lost market share to more competent rivals, and eventually exited the market entirely.

50 PNG's telecommunications sector has gone through a similar liberalisation process. However, unlike the Australian experience, bemobile appears to have neither adapted to competition nor exited the market. Rather, it continuesto exist, attempting to rely on regulatory intervention rather than commercial endeavour to sustain itself.

51 Digicel's success in acquiring a market share of around 80% is no more than a reflection of the large degree of heterogeneity that one expects to find following liberalisation. As bemobile has not been able to adapt nor allowed to fail, more efficient firms are prevented from taking over the spectrum and other assets held by bemobile. The natural consequence of bemobile's state is that Digicel ends up seemingly (but not in reality) dominating the market.

7 The proposed RSD would harm PNG's long-term economic and social development

52 We would first observe that even in the short-term, the proposed RSD (with or without the "enhancements" proposed by bemobile has very little to offer to existing or prospective mobile subscribers. At best, the RSD may lead to reduced off-net tariffs and more inter-network traffic. However, due to "waterbed effects" it would necessarily also lead to lower service levels, higher on-net tariffs and reduced on-net traffic. Thus the overall impact on subscriber welfare is ambiguous at best, although for reasons given elsewhere, overall welfare, taking into account incentives to invest and expand penetration, will likely be harmed.

53 The only beneficiary of the RSD is bemobile. While at first blush it seems that bemobile benefits because its subscribers can expect to receive more calls from Digicel subscribers, Digicel submits that bemobile's true motive is to dampen price competition. bemobile originally proposed(in its letter of 27 January 2011) that NICTA should cap Digicel's off-net tariffs. However, this could potentially lead to Digicel becoming even more price competitive.

54 Fearing this, bemobile subsequently argues for NICTA to impose a non-discriminatory rule, knowing that its true impact is to force Digicel to raise its effective on-net price. The direct effect is that most of Digicel's subscribers will face higher prices for most calls that they make, and the ultimate effect is to dampen price competition.

55 The long-term effect of the RSD is therefore to delay mobile penetration in PNG. NICTA greatly underestimates the contribution that higher mobile penetration makes to PNG's long-term economic and social development.

56 In the Asian Development Bank ("**ADB**")'s 2012 report "Papua New Guinea: Critical development constraints", the ADB explains the contribution of infrastructure investments to long-term economic growth (at page 24):

> "Low levels of economic growth and investment can be caused by low social returns to economic activities, which in turn can be due to inadequate human capital, infrastructure and other public goods that complement private investments. Inadequacy in these complementary factors can lower the productivity of factors of production and increase the cost of doing business, which in turn can reduce returns to investment."

57 The ADB also highlights the appropriability of returns to investment as an issue, noting (at page 37) that:

> "Private parties will invest only when they expect to capture adequate returns from their investments. Anything that weakens the capture discourages investment and, ultimately, slows growth."

58 The ADB highlights inadequacies of infrastructure as a key constraint on private investment (at page 99):

> "PNG lags far behind most other major economies in Southeast Asia and the Pacific in key infrastructure, including transport, electricity and water supply. Inadequacies in infrastructure, in particular, affect the access of rural communities and connectivity between main centres and regions.
>
> … The lack of investment and maintenance has suppressed private investment …"

59 With respect to the telecommunications sector however, the ADB views Digicel's entry as being pro-competitive, observing (at page 28) that:

> "mobile telecommunications in PNG have been transforming rapidly due to the introduction of competition in the mobile telephone market. The new entrant, Digicel, was granted a licence in late 2006, and consequently the access to, efficiency of, and reliability of mobile phone services have improved significantly. Competition helped increase the network coverage and reduce the rates significantly. The government estimates that the introduction of competition led to an average GDP growth of around 2.5% points in the years immediately following Digicel's entry (Department of Treasury 2009).

60 The ADB notes that "indirect and multiplier effects are likely to be substantial, given that the increased access will enable the provision of other services in the future, including mobile banking".

61 That said, the ADB notes that more remains to be done in terms of improving the infrastructure and implementing reforms:

> "PNG compares poorly with other selected Asian countries in terms of mobile and fixed line subscription and internet use. … The state-owned

> enterprise, Telikom, still holds a monopoly over the international telephone and internet gateways. Despite competition in the retail markets for internet services, access and usage costs remain high, contributing to the limited internet use in PNG."

62 In summary, the ADB highlights the contribution that mobile communications makes to PNG's long-term economic growth, noting in particular that indirect and multiplier effects are likely to be substantial. These effects are possible only if people have mobile services. NICTA should also be wary about restricting the appropriability of Digicel's returns to investment.

63 It is striking that the ADB does not note any competition issues with the mobile communications sector. The only concern the ADB has is that more remains to be done in terms of raising mobile penetration in PNG.

64 To be clear, the objective of ensuring that the ICT sector contributes to the greatest extent possible to PNG's long-term growth does not mean NICTA is wrong to be concerned about promoting competitive markets. However, any diagnosis that competition in the mobile market is ineffective has nothing to do with Digicel's conduct. If competition is ineffective, it is because Digicel's rivals are inefficient as explained above.

8 The retail regulation criteria are not met

65 Bemobile, has not offered any compelling evidence or argument to show that an RSD would satisfy the retail regulation criteria ("**RRC**"). In particular bemobile have not provided any evidence or analysis to correct the fundamental misconceptions that currently exist:

(a) **Misconception 1 – the RSD would promote competition**.
If competition is ineffective, it is because bemobile is inefficient, not because Digicel's pricing is anti-competitive. It is legitimate for Digicel seek to internalise network effects through on-net discounts. It is illegitimate for bemobile to seek to free ride on Digicel's past investment to expand its mobile subscriber base in PNG.

(b) **Misconception 2 – the mobile market is made up of equally efficient rivals.**
In fact, there are large differences between Digicel and bemobile. This heterogeneity is a normal result of market liberalisation. Not all firms adapt equally well to liberalisation. Over time, the heterogeneity among firms should decline as inefficient firms exit the market or adapt to the more competitive environment. bemobilehas yet to adapt, nor has it exited the market. The RSD would, together with NICTA's recent decision to relax bemobile's network coverage conditions, merely prolong

bemobile'scurrent state and harm efficient investment in, and efficient use of, ICT infrastructure

(c) **Misconception 3 – the RSD would promote consumer welfare.** NICTA appears to have construed consumer welfare too narrowly, focussing on the high off-net rates and the relatively low level of inter-network traffic. NICTA should adopt a comprehensive and inclusive view of consumer welfare:

i A comprehensive view would take account of the benefit consumers derive from lower on-net tariffs and increased on-net traffic.

ii An inclusive view would take account of the wellbeing of prospective mobile subscribers. It would take account of the contribution that higher mobile penetration would make to the long-term economic and social development of PNG. In short, an inclusive view would take account of the wellbeing of all Papua New Guineans, both current mobile subscribers and future mobile subscribers, both the current generation and future generations.

66 Each of these misconceptions must be investigated and addressed before NICTA can be satisfied that the RRC are met. NICTA has not addressed the hypothesis that the reason why competition seems ineffective is because bemobile remains far below the production possibility frontier and the reasons for this are purely internal to bemobile. Even the Minister for Public Enterprise, the honourable Sir MekereMorauta, has attributed bemobile's difficulties to "terrible management decisions taken in the last couple of years by Bemobile under GEMS direction" (see Attachment C).

67 Digicel submits that rigorous analysis remains wanting in NICTA's assessment of the issues.

Schedule 1 Additional responses to bemobile's arguments

Issue:	Bemobile's argument	Digicel's response
SMS	SMS is part of a cluster of mobile services	Digicel agrees that SMS is part of a cluster of mobile services and included in the relevant market definition, but this is not a reason to extend the RSD to include both voice and SMS traffic. NICTA's proposal seeks to use an RSD for the purpose of sheltering Digicel's rivals. This is contrary to the legislative purpose of an RSD (which is consumer protection in situations where effective competition is absent). It is also contrary to the objective of promoting competition, which is widely understood to be very different to promoting the interests of (i.e. sheltering) particular firms. These are serious errors of law. However, even if we were to accept that it is legitimate for NICTA to seek to protect Bemobile from competition, the proposed intervention would not achieve that goal *because* SMS is part of a cluster of mobile services. NICTA's proposed intervention on voice traffic would shelter bemobile and make its offering look better, thereby shifting market share toward bemobile. As customers shift their voice calls to bemobile, they will also shift their SMS activity to bemobile.
	Network effect could be stronger for SMS	The network effect arises from externalities, which only occur if and to the extent that subscribers derive benefits from receiving communications that are not otherwise taken into account by the party that initiates the communication. If SMS traffic is generated as part ofconversations as bemobile suggests, then text messages must flow in both directions. This process of two-way exchange must reduce any externalities (and therefore any network effect) because both parties will be contributing to the cost of the conversation. In any event, the proposed intervention to regulate voice calls is already extremely intrusive. Digicel considers that the proposed RSD is harsh, oppressive and disproportionate and therefore contrary to section 41 of the Constitution of the Independent State of Papua New Guinea. Any proposal to extend the intervention to SMS would be even more harsh, oppressive and disproportionate.

Issue:	Bemobile's argument	Digicel's response
		In fact, Digicel submits that the proposed intervention should not take place for the reasons set out in the body of this submission.
	NICTA should act because Digicel has an intention to price discriminate and there is no "downside" doing so	There is no evidence that causally connects Digicel's SMS pricing to a coherent theory of harm, and there are consequently no grounds for regulating Digicel's SMS pricing. The proposal that NICTA should regulate in anticipation of harm is extreme and unjustified. It would set a very dangerous precedent at a very early stage of the regulatory regime. This is a period in which NICTA should be seeking to develop a reputation for carefully considered and principled decisions, along with a commitment to protect the rights of investors in order to minimise regulatory uncertainty and not undermine incentives to invest. The fact that Digicel differentiates on-net SMS prices in other countries does not mean Digicel will necessarily do so in PNG or that on-net differentiation of SMS pricing is harmful. Pricing decisions in each country are made independently of other countries. There may be good reasons for differentiating on-net pricing in other countries. Nothing can be inferred from the fact that Digicel differentiates on-net SMS in other countries. Moreover, as we have previously explained, there is no basis for assuming that price discrimination is anti-competitive, even if the price difference is not based on cost. Subscribers benefit from being able to make on-net calls and SMS and promoting traffic through low prices is both efficient and welfare enhancing, particularly in a market with such low mobile penetration. Finally, but critically, it is very dangerous to regulate on the assumption that there will be no "downside" from doing so. Regulation always has direct and indirect costs which (under the retail regulation criteria) need to be compared with any identified benefits. For example, as we have explained previously, the proposed RSD will lead to price increases for Digicel's on-net calls, which will impose extra costs on consumers. These price rises might be an unintended consequence of the proposed RSD, but under section 158(d) of the Act, NICTA is obliged to acknowledge that they will occur and to compare their cost with any offsetting benefits.
	SMS and voice are complementary and	Bemobile cites two papers in support of its claim that SMS and voice services are "complementary services and are weak substitutes". Neither of these studies is relevant to PNG. One uses data from Norway where mobile

Issue:	Bemobile's argument	Digicel's response
	weak substitutes	penetration is 116% of population and GDP per capita is 23 times that of PNG. The other uses data from an unknown operator in an unknown Asian country. More fundamentally, bemobile's claim is logically impossible. Depending on the cross-price elasticity of demand, two services might be substitutes or complements, but they cannot be both at the same time. Bemobile's argument for including SMS relies on this logically impossible claim. It is therefore without foundation.
	International precedents are relevant	Bemobile cites certain statements made in several other countries and relies on them to argue that "there is credible international precedent for banning any retail price differentiation for SMS on pro-competition grounds". This argument completely ignores the normal procedures that NICTA must apply under the laws of PNG. As we have shown in our previous submission, PNG's mobile market is in a unique position, and that position is of critical relevance to NICTA's decision-making. Sound regulatory decision-making needs to start from a factual base, include a coherent and falsifiable theory of harm, and test that theory in a careful and objective manner. This process is required by the National ICT Act, and NICTA is also obliged to respect the Constitution of PNG. The process cannot be avoided on the grounds that some other regulator, in a different country, facing with different market conditions and different facts made a particular statement or decision. Bemobile also draws the New Zealand Commerce Commission's ("NZCC") statements as being support of its position that on-net price discrimination "makes it difficult for small operators to compete". Importantly, retail pricing for mobile services remains unregulated in New Zealand. It is also relevant that Telecom New Zealand has introduced its "Smart Prepaid" pricing which provides "[o]ne rate for calls and texts no matter what network your friends and family are on"[4]. Minutes and Text messages that are included in Telecom New

[4] http://www.telecom.co.nz/mobile/mobile/plansandpricing/prepaid/

Issue:	**Bemobile's argument**	**Digicel's response**
		Zealand's postpaid plans can also be used to call any network. This is not as a result of regulatory intervention. It is a commercial response to the market as it changes over time. Imposing a RSD will interfere with the PNG market's ability to change and evolve to meet the needs of consumers over time.
	Speed is more important than care.	Bemobile urges NICTA to include SMS in an RSD even though it is clear that no proper analysis has been undertaken that would support such a decision. Bemobile also urges NICTA to act quickly, that "urgency is of the utmost importance". There is a deep and obvious conflict between these positions. NICTA is obliged by law to apply all of the retail regulation criteria in s158, to be satisfied that they are met, and (under section 42(a)) to consult with parties that would be adversely affected prior to making any recommendation in a RSD. Digicel submits that it would be an error of law for NICTA to add SMS to its proposed RSD without explaining its reasons for doing so, and seeking feedback on that proposal. We trust that NICTA recognises that Digicel's comments in this cross-submission do not give NICTA grounds for avoiding due process in the event that it wishes to add SMS to its proposal.
Postpaid	Postpaid and prepaid are in the same market.	bemobile says it is "unconvinced that sufficient analysis has been conducted in order to rule out post-paid services from the Determination."This betrays a bias towards "regulating everything" which Digicel hopes NICTA does not share. The Act contains strict hurdles (s158), all of which must be cleared to justify retail regulation. These are supported by the Regulatory Principles contained within section 3 of the Act and in particular, section 3(b) which requires that "*regulatory measures should be proportionate and crafted to achieve results that are no more burdensome than necessary to achieve their stated regulatory objectives*".So the legal presumption is against regulation, not in favour of it as bemobile seems to believe. NICTA should consider whether there is a distinct corporate market forretail mobile servicesthat is largely a post-paid market. If so, pre-paid and post-paid services are in separate markets and must be analysed as such. Digicel observes that bemobile does not have a post-paid billing platform and therefore is not even competing

Issue:	Bemobile's argument	Digicel's response
		in this arena.
	Digicel has more market power in respect of post-paid than pre-paid services	Bemobile cites data reported by NICTA that shows Digicel's revenue market share exceeds its customer market share whereas the reverse is true for bemobile. From this, bemobile infers that Digicel's total average ARPU is higher than bemobile's. The next step in bemobile's thinking is that this must mean that Digicel has a higher market share in a post-paid mobile services market, from which bemobile concludes that Digicel has more market power the market for post-paid than pre-paid services. The first point to note is that market share is a very unreliable indicator of market power. To use the words of the distinguished British economist John Vickers[5] "Shares of properly-defined markets are at most a way to screen out cases that deserve nomore attention. High shares alone never imply dominance." Secondly, post-paid customers are more likely to be well informed corporate customers that make buying decisions for a fleet of mobile services. This is a highly contestable market where the customers have significant countervailing bargaining power. Digicel has previously explained why it does not have substantial market power in the supply of pre-pay services. The position is even more clear-cut in respect of post-paid services. Digicel considers that it would be harsh, oppressive and disproportionate (to use the terms in s41 of the Constitution) for NICTA to reach the view that Digicel has substantial market power in this market on the basis of the unsubstantiated submission by bemobile on this point. As a consequence it is not open to NICTA to consider regulating Digicel's post-paid prices.

[5] John Vickers, 2007, "Some Economics of Abuse of Dominance", Discussion Paper 376, Department of Economics, University of Oxford

Issue:	Bemobile's argument	Digicel's response
	Price discrimination softens competition	Bemobile argue that not extending the RSD to post-paid services would "soften competition in the wider high value community". This argument reflects a misunderstanding of the critical difference between promoting the process of competition, and promoting the interests of any particular competitor. There are many authorities for this distinction, but the following quote from the US Department of Justice, discussion Section 2 of the Sherman Act, is a good example:[6] "Section 2 also advances its core purpose by ensuring that it *does not prohibit aggressive competition*. Competition is an inherently dynamic process. It works because firms strive to attract sales by innovating and otherwise seeking to please consumers, even if that means rivals will be less successful or never materialize at all. Failure--in the form of lost sales, reduced profits, and even going out of business--is a natural and indeed essential part of this competitive process. "*Competition is a ruthless process. A firm that reduces cost and expands sales injures rivals--sometimes fatally." While it may be tempting to try to protect competitors, such a policy would be antithetical to the free-market competitive process on which we depend for prosperity and growth*. To explain why the proposed RSD (and/or any extension of it) is pro-competitive, NICTA needs to go well beyond merely pointing to the fact that Digicel is an effective competitor. Digicel submits that this has not been done, and that there is no basis for assuming that Digicel's pricing damages the competitive process. What bemobile seeks is an easier life, where Digicel is punished for its success and required to post prices that give less value to its customers. In the words of the Department of Justice "such a policy would be antithetical to the free-market competitive process on which we depend for prosperity and growth". Digicel also submits that the proposed RSD (and/or any extension of it) would be clearly contrary to section 158(b)(ii)of the NICT Act which requires that, "in the absence of the RSD ... substantial [market] power is likely

[6]http://www.justice.gov/atr/public/reports/236681_chapter1.htm

Issue:	Bemobile's argument	Digicel's response
		to persist ... and expose [Digicel's] customers to a material risk of higher prices...". In fact, as Digicel has previously explained, the RSD will have the effect of increasing prices for the vast majority of calls made by Digicel's customers. On-net prices will *rise* under the RSD due to the waterbed effect as Digicel has previously explained. This is the outcome bemobile seeks because it will protect bemobile. The proposed RSD will not promote competition; on the contrary, it will tie Digicel's hands and soften competition. Nor will it protect consumers: prices will rise for the vast majority of calls made in PNG. The proposed RSD is therefore anti-competitive and contrary to the Retail Regulation Criteria in section 158.
Cost-based discrimination	MTRs are not an objectively justifiable cost	Bemobile says NICTA should look at how MTRs were arrived at, and until this is done, there can be no objective basis for NICTA to assess objectively justifiable cost differences. How MTRs were arrived at is irrelevant to this proceeding. Digicel pays a MTR for off-net calls. The MTR is therefore a cost Digicel incurs in respect of off-net calls and can be objectively justified as such. The MTR is not a cost that Digicel incurs when it sells on-net calls however. The MTR is therefore a cost justifying a difference between the on-net price and off-net price. NICTA's proposal to limit price discrimination would slow down market expansion, for the reasons set out more fully in Cave & Doyle (2012)[7].
Impact on market share	Digicel's pricing has resulted in bemobile's customer numbers falling as of end of April despite bemobile	At page 23 of its submission bemobile implies that its subscriber numbers fell suddenly at the end of April 2012. It is implausible that Digicel's pricing can be linked to the fall in bemobile's subscriber numbers in April. None of the models on network effects provide a mechanism that links Digicel's pricing to such short-term effects. If anything, the data on market share NICTA's Second Discussion Paper (p 30) indicate that Digicel's market share is falling, particularly when the impact of Telikom is taken into account.

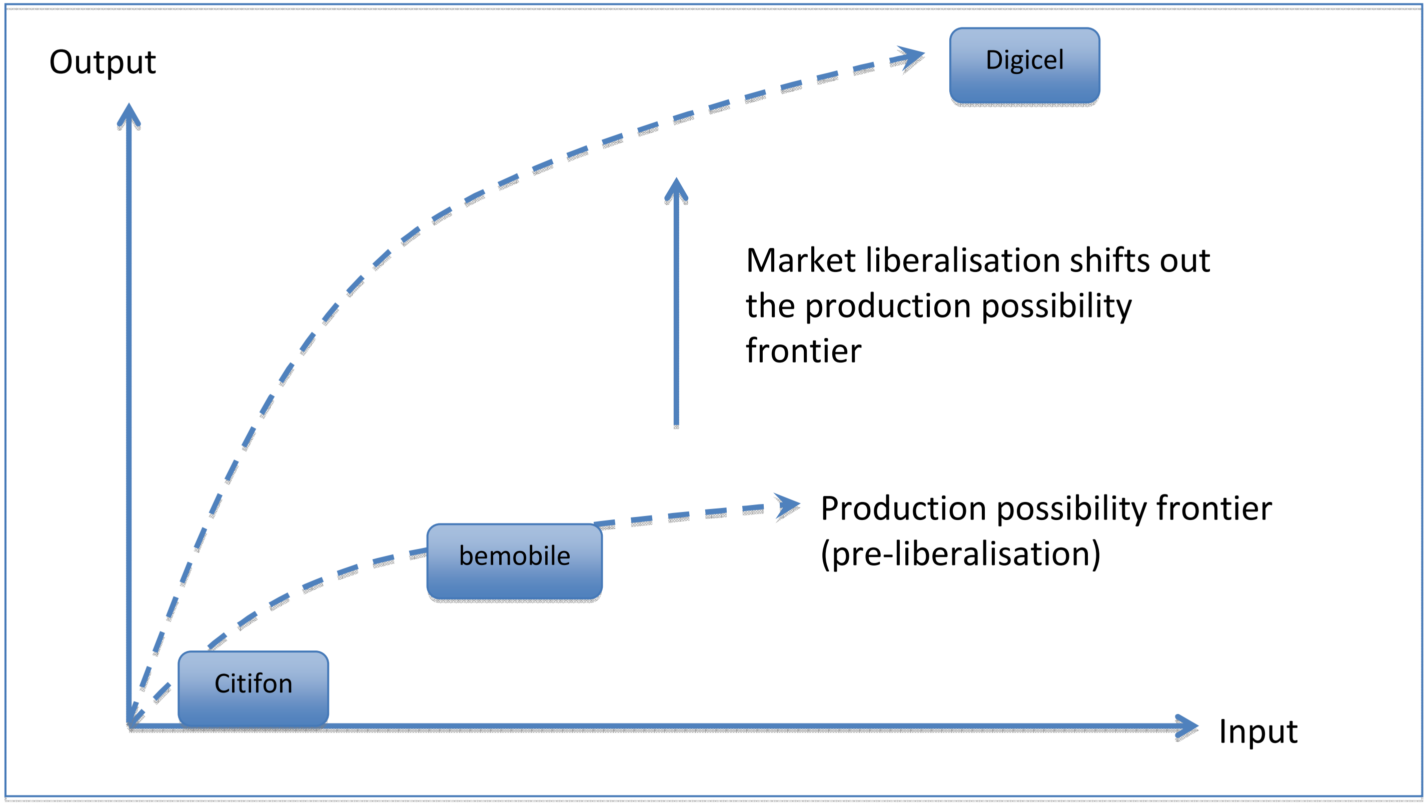
7 Cave & Doyle 2012, On-Net/Off-net Price Discrimination and Digicel in PNG: Independent Opinion, submitted to NICTA in the public inquiry on the RSD.

Issue:	Bemobile's argument	Digicel's response
	matching or undercutting Digicel's pricing	A more plausible hypothesis is that bemobile unsuccessfully attempted to substitute improvements in its network and service and sales and marketing expenditure for price reductions. Price reductions by themselves will not deliver more sales without having a quality network and making an effort to maintain an effective sales and marketing channel. This "lazy management" hypothesis (i.e., relying on price cuts to make up for management inactivity and poor decision making) is the likely explanation for bemobile's April results. Digicel notes that there has been no press, radio or TV advertisements from bemobile in recent months. Bemobile appears to have cut back on sales staff and top up points. Bemobile does not make handsets available to the market. In short, bemobile has been inactive in the market. NICTA should conclude that bemobile's difficulties have nothing to do with Digicel but simply a symptom of management incompetence and absence of long-term commitment. **[XXXXX_redacted_XXXXX]** A graph showing the number of discrete bemobile customers calling the Digicel network since July 2007 is set out below.

Issue:	Bemobile's argument	Digicel's response
		[REDACTED GRAPH] The graph shows that decline in bemobile's subscriber numbers is relatively gradual phenomenon, likely coinciding with a period of management instability since August 2011. The long-term trend indicates that bemobile has been able to increase its mobile subscriber base, albeit slowly, since Digicel's entry into the market in 2007. The trends in subscriber numbers and bemobile's claim also do not accord with the interconnection traffic that bemobile hands over to Digicel. The graph below shows interconnection traffic handed over from bemobile to Digicel for the period April 2011 – June 2012. While there was a decline in voice traffic for the period August 2011 – November 2011, that trend has reversed this calendar year with traffic levels growing and being at or about the levels that existed in mid 2011. In particular there is no evidence of any significant falls in interconnection traffic in the past six months. There is certainly no evidence of "network effects" that can be derived from this data.

Issue:	Bemobile's argument	Digicel's response
		[REDACTED GRAPH] This shows that there has been no sudden change to bemobile's fortunes in recent times. Bemobile's performance failures have been long running – it has not been effective at attracting new customers since Digicel's first entry into the market at which time Digicel had very little market share.

Schedule 2 Market liberalisation expands the production possibility frontier



Attachment A: ICCC letter dated22 February 2012finding that Digicel's conduct is unlikely to be anti-competitive

INDEPENDENT CONSUMER AND COMPETITION COMMISSION

Office of the Commissioner

Our Ref: 07-7000-5.4/a

22 February 2012

Mr. Charles S. Punaha
Chief Executive Officer
National Information & Communications Technology Authority
P O Box 8444
BOROKO
NCD, Papua New Guinea

Dear Mr. Punaha,

RE: BEMOBILE COMPLAINTS – Allegation on Excessive Off-Net Retail Pricing and Handset/SIM Swapping/Destruction by Digicel

This is to inform you of the Commission's decision on the above complaints of bemobile Limited.

The Commission has examined the issues against the elements of s.50 and s.58 of the *Independent Consumer and Competition Commission Act 2002* ('ICCC Act') and concludes that the conduct of Digicel is unlikely to be proved to have anti-competitive purposes; hence they are not likely to amount to a contravention of the ICCC Act.

If NICTA considers it appropriate to open a Public Inquiry in relation to the issue on 'excessive off-net retail pricing', it may do so to prove a breach of the retail price regulation criteria under the relevant provisions of the NICT Act.

Yours sincerely,

Dr Billy Manoka, (PhD)
Commissioner and Chief Executive Officer

Cc: **Honourable Jimmy Miringtoro, M.P**
Minister for Communications & Information
Ministry of Communications & Information;

Mr. Andy Rolt
Acting Chief Executive Officer
Bemobile Ltd;

Mr. John Mangos
Chief Executive Office
Digicel (PNG) Ltd.

"Friend to Businesses, Friend to Consumers"

Attachment B: ICCC letter dated 5 July 2010 confirming registration of the direct interconnect agreement between Digicel and bemobile dated 17 April 2010

INDEPENDENT CONSUMER AND COMPETITION COMMISSION

Office of the Commissioner/CEO

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Our Ref: 06 – 6303.3.2/10: AH

5 July 2010

Mr. John Mangos
Chief Executive Officer
Digicel (PNG) Limited
PO Box 1618
PORT MORESBY 121
National Capital District

Mr. Steward Kelly
Chief Executive Officer
Bemobile Limited
PO Box 1105
WAIGANI 131
National Capital District

Dear Messrs Mangos and Kelly,

SUBJECT: REGISTRATION OF DIRECT INTERCONNECTION AGREEMENT

The Commission has now completed its review of the Direct Interconnection Agreement between Digicel and Bemobile dated 17 April 2010, pursuant to Section 86 of the *Telecommunications Act* (**Act**), and is satisfied that the interconnect agreement complies with the charging principles in force and the Act.

Consequently, the Direct Interconnection Agreement between Digicel and Bemobile has been accepted and registered by the Commission.

I would also like to take this opportunity to once again congratulate both companies on reaching this significant agreement.

Yours sincerely,

ASSOC. PROF. BILLY MANOKA, (PhD)
Commissioner & CEO

" Friend to Businesses, Friend to Consumers"

Southern Regional Office
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Attachment C: MekereMorauta (Nov 2011), Statement in Parliament, the state of PNG's public enterprises

Only an extract concerning bemobile is reproduced below:

Bemobile

This is another example where the previous government, and Arthur Somare in particular, entered into bad deals which have got progressively worse over time.

In 2008, Telikom sold half of its mobile phone company to a private consortium, dominated by a Hong Kong venture capitalist, GEMS. But in doing so, Telikom entered into an extraordinarily lopsided agreement for this new joint venture where, notwithstanding Telikom having half the shares, GEMS, with less than 40 per cent of the joint venture shares, was guaranteed a majority of directors and complete control over the management of Bemobile (including management selection). The agreement locked in Telikom to this arrangement with no prospect of changing it.

Earlier this year Telikom's share of Bemobile was transferred to IPBC and the Asian Development Bank became a minor shareholder. A revised shareholder agreement was signed by the then Managing Director of the IPBC, which is just as lopsided as the original agreement, if not more so, still giving GEMS total management control and permanent domination of the Bemobile board.

The management of Bemobile has been anything but successful. I must be somewhat circumspect about what I say about Bemobile, as a company with private shareholdings (including PNG investors), but it is apparent to anyone that Bemobile is struggling to compete with Digicel. And some of the reasons for this are terrible management decisions taken in the last couple of years by Bemobile under GEMS direction.

It is inexplicable why anyone with the interests of the public of PNG in mind would (twice) sign such unfair and biased shareholder agreements, so plainly detrimental to this nation's interests, as occurred with the former Managing Director of the IPBC, in conjunction with the then Minister. We are trying to overcome these problems, to improve the management of Bemobile and have it managed in PNG rather than from Hong Kong, but it has not been easy and it is not yet resolved.