Comments

On

IDA's

ADVISORY GUIDELINES GOVERNING APPLICATIONS FOR LICENSE ASSIGNMENTS OR CHANGES IN OWNERSHIP OF A LICENSEE IN CONNECTION WITH A PROPOSED CONSOLIDATION

By

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Pacific Internet Limited ("PacNet") is a Facilities-based Operator ("FBO") Licensee and its shares are listed on the Nasdaq National Market in the United States. We set out below our views and comments on IDA's Advisory Guidelines Governing Applications For License Assignments Or Changes In Ownership Of A Licensee In Connection With A Proposed Consolidation (the "Guidelines"). Save where it is otherwise expressly defined, all words have identical definitions as used and defined in the Guidelines.

A. GENERAL VIEWS

PacNet welcomes IDA's efforts to solicit feedback and comments for the Guidelines. We agree that the public as well as the industry would benefit from further clarification regarding the standards applicable to IDA's Consolidation reviews as well as a more formalized procedure for such reviews.

However one area of concern that we have over the Guidelines is whether sufficient consideration have been accorded to the identity and nature of the applicant as well as the commercial realities of a potential Consolidation.

Often in a proposed Consolidation, it may be the divesting shareholders or owners of the Licensee that would be dealing directly with the other Licensee or third party (in a Non-Horizontal Consolidation) or the shareholders or owners of such other Licensee or third party. In most of these instances, it would not be likely for the affected Licensees themselves to be driving or even substantially involved in such dealings. There may also well be other compelling commercial reasons for not involving the affected Licensees until at a much more final stage of the proposed Consolidation.

It should further be highlighted that the divesting shareholders or owners of the respective Applicants and/or the Applicants themselves may be listed on the local or other foreign stock exchanges and accordingly are subject to stringent take-over regimes as well as other listing obligations in relation to a potential take-over.

For these reasons, it is submitted that the Licensees themselves may not always be the most appropriate parties to file a Consolidation Application. We seek IDA's clarification as to whether the above issues have been considered in the formulation of the Guidelines.

We further note that in developing the Guidelines, IDA had drawn from the experiences of the United States, European Union and Australian jurisdictions. Apart from these jurisdictions, IDA may wish to conduct a review of jurisdictions that involve a smaller market such as Sweden, Switzerland and Israel. It is our opinion that these jurisdictions may provide more meaningful benchmarks given the greater similarity between the size of the Singapore market and the markets in these jurisdictions.

B. SPECIFIC COMMENTS

Consolidation Review Principles

1. Elimination of a potential competitor – Sections 2.2.2.1, 6.3.3.1

Under Section 2.2.2.1, one of the considerations that IDA will take into account in deciding whether the consolidation has an anti-competitive effect is whether it will eliminate the possibility that one of the parties in a Non-Horizontal Consolidation will enter, as a competitor, into a market that the other party currently participates in.

In this regard, it is not clear as to what a potential competitor is. The difficulty arises in ascertaining the degree of likelihood or intention of that competitor entering into the relevant market. Even though Section 6.3.3.1 further elaborates by stating that 'entry preclusion' is likely where the proposed consolidation is a Vertical Consolidation or that one of the applicants is obliged by the terms of a license to enter into the other party's market, these are by no means exhaustive and the determination of such a probability may well turn out to be a subjective exercise prone to many interpretations.

Furthermore such a requirement may unduly constrain the mode of entry by an external party as the decision whether to set up operations in Singapore organically or via acquisition of an existing Licensee would in most cases be largely a commercial one rather than to unreasonably restrict competition. However, such Consolidation risks being struck down for being likely to restrict competition under this requirement.

Accordingly we submit that such a requirement based essentially on the determination of the commercial motivation behind a potential Consolidation and the possibility of entry by a potential competitor would not be appropriate.

Consolidation Applications

1. Application for approval – Section 3.1.1

Section 3.1 provides that the Applicants of a Consolidation Application must be the target Licensee and the acquiring party.

For the reasons set forth under our "General Views" above, we are of the view that the persons who may file such an application should not be restricted only to these parties.

In addition to the possible non-involvement of the Licensee, the perspectives of the management of the Licensee and its shareholders or owners might also differ vis-à-vis a potential Consolidation. This is heightened in a situation where the Licensee is listed and the management of the Licensee owes a fiduciary a duty to all shareholders, divesting and non-divesting alike. If the Consolidation Application must be strictly submitted by the Licensee, this may prove to be a potential source of conflict between the requirement of the management of the Licensee to support the proposed Consolidation and the duty to advise its non-divesting and/or minority shareholders on the potential Consolidation.

We submit therefore that the divesting shareholders or owners of the Licensee should be given the opportunity to avoid the impositions of such obligations on the Licensee by choosing to submit the Consolidation Application themselves.

2. Definition of consolidation – Section 3.1.2

We seek further guidance from IDA in the determination of 'the ability to exercise control' over another entity as stated in Section 3.1.2. IDA could perhaps clarify the

circumstances in which it would consider a party to be in a position where it has the ability to exercise control over another entity.

3. Consolidation Agreement – Section 3.1.3

Under Section 3.1.3, the applicants are required to enter into a binding agreement prior to submitting the Consolidation Application. We propose that the applicants be allowed to submit the Consolidation Application with the proposed key terms and mechanics of the potential Consolidation rather than submit a binding agreement. In addition, we propose that other documents such as Letters of Intention (LOIs), which may already be binding on the parties, may be submitted in lieu of such binding agreement and could be deemed to suffice in the absence of further indications from IDA on its proposed direction with regards to the proposed Consolidation. The binding agreement may subsequently incorporate any conditions or guidance that IDA may have on the Consolidation Application and be submitted to IDA for final clearance should the approval of IDA be provisionally granted.

The concern for the above proposal is that for the proposed transaction to proceed to a point where the parties have entered into a binding agreement requires the commitment of considerable resources which would be wasted should the Consolidation Application be subsequently rejected for any reason whatsoever.

Furthermore, a large part of such an agreement would be dealing with the protection of the interests of the respective parties involved from a more legal and commercial perspective and would not be relevant for the determination of anti-competition.

More importantly, the other information needed to satisfy the Minimum Information Requirement is already fairly exhaustive and would provide IDA with sufficient information to decide whether the proposed consolidation would unreasonably restrict competition. The binding agreement would have little probative value and thus would not justify the level of expenditure the parties would have to make in order to produce one for the purposes of the review.

In any event, we believe that the filing period of 14 days from the time the binding agreement is signed may be too short a period to effectively prepare and compile a Consolidation Application. Perhaps the time frame could be further extended to thirty days.

4. Minimum Information Requirements – Section 3.2.4

Certain information required to satisfy the Minimum Information Requirements may be difficult to satisfy.

Under Section 3.2.4, the Applicants are required to submit a good-faith assessment of the likely impact on the proposed Consolidation on competition and a statement on why the proposed consolidation would serve the "*public interest*".

"*Public interest*" is a concept that is both wide and ambiguous. It is subject to many possible interpretations. It is instructive to note that there is a detailed elaboration on the competitive assessment in the same Section but no further guidance on this term. We are

of the view that the assessment of public interest is one that is best made by the regulator after having regard to all the relevant competing concerns, rather than the Applicants themselves. This becomes even more significant taking into account the concerns we raised under our "General Views" and our specific comments in respect of Section 3.1.1.

Applicants are also required to provide information on the '*likelihood that output would be increased… in response to a significant and non-transitory price increase…*' or the '*likelihood of End User switching in response to a significant and non-transitory price increase…*'. We seek IDA's further clarification as to the extent of due diligence or standard that IDA would hold the Applicants to in forming such assessments. Would the Applicants be required to obtain independent research or surveys in attempting to provide such assessments? All this would require significant resources of the Applicants. It is instructive to note that the Applicants are required to certify that they have made a "*diligent effort*" to complete the Consolidation Application Form and that all information contained therein (including such assessments) is "*current, accurate and complete*". Furthermore, IDA is empowered to impose "*appropriate sanctions*" under Section 5.1.5 if it "*concludes that a Licensee has engaged in wilful concealment or misrepresentation*".

5. Consolidation Application Processing Fee – Sections 3.3 and 3.6

We are of the view that the processing fee of S$10,000 as stipulated in Section 3.3 may be too high and it should take into account the size and value of the proposed Consolidation.

This is compounded by the fact that under Section 3.6, if there is any new or different fact that is reasonably likely to have a material impact on the application, IDA may require the Applicants to withdraw the existing Consolidation Application Form and submit a fresh one thereby presumably incurring another payment of the processing fee. Such payment would still be required despite the fact that the change in circumstances may have occurred through no fault of either Applicant.

We seek IDA's consideration of the various instances whereby it may consider waiving such processing fee. IDA may also wish to consider imposing a scale of fees pegged to the maximum of S$10,000.

6. Informal Guidance Prior to Agreement – Section 3.8

Given the onerous obligations and consequences attendant to the submission of a Consolidation Application Form, we certainly support IDA's decision to provide Informal Guidance on a proposed Consolidation.

As this is largely an informal process, having regard to the concerns we raised under our "General Views" and our specific comments in respect of Section 3.1.1, we seek IDA's confirmation that this very useful avenue can be resorted to by parties other than the Licensees, such as their respective shareholders or owners. This becomes more critical should IDA maintain the position that only Licensees may file a Consolidation Application.

While the Guidelines state that confidential treatment is accorded to all information submitted in an application for Informal Guidance and to any Guidance that is provided,

the Guidelines are silent as to whether confidential treatment will be accorded to the fact that an application has been submitted. We seek IDA's clarification on this issue.

We seek further clarification as to whether any fees are payable for such informal consultation.

Consolidation Period Review

1. Length of Review Period – Sections 3.5, 4.1 and 4.2

We respectfully submit that the maximum review period of 120 days is far too long. Potential Consolidations are typically very time sensitive. More importantly if any of the entities involved (be it the Licensees themselves or their shareholders or owners) are listed entities, a protracted review period may introduce further volatility or uncertainty to the stock price of such entities as such potential Consolidations are material and extremely price-sensitive transactions. This is not taking into account the take-over regimes that may potentially apply to the entities involved.

It should be further stressed that the review period represents a period of uncertainty not only for the stock price of the entities involved but also for their respective businesses and operations. A protracted review period will undoubtedly have an adverse impact on the Licensees' dealings with its business and joint venture partners, customers, suppliers, creditors and other third parties. Internally, the Licensees are also likely to face increased human resources issues given the uncertainty brought forth by a protracted review period.

Finally, a protracted review period might also in itself bring about a material change in circumstances and could lead to our concerns as expressed for Section 3.6.

While we appreciate the arduous nature of the review involved, given the potential difficulties the Applicants will face and the certainty that all businesses require, we strongly propose that the maximum review period be reduced to the absolute minimum possible, such as 60 days.

2. Tolling of Consolidation Review Period – Section 4.3

Under Section 4.3, IDA will 'toll' the running of the review period until such time as the Applicants are able to satisfy IDA's requests for Supplemental Information. Once IDA has determined that the Applicants have provided all the Supplemental Information, IDA will resume the running of the review period. As there is no mention of whether IDA will notify the Applicants that the running of the review period has resumed, we would request that in the interest of certainty and for the benefit of the Applicants, IDA effect such notifications to the Applicants in writing as and when it arises.

Information Gathering and Confidentiality

1. Public Consultation – Sections 5.2.1 and 9.2

While we appreciate the rationale for transparency, we query if the solicitation of comments from members of the public may significantly aid IDA in its determination of whether a proposed Consolidation may be anti-competitive. Since comments are likely to

be solicited for novel or complex issues, we believe that any feedback would be more appropriate and constructive if they are solicited on an invitational basis to certain pre-determined bodies, institutions or individuals, rather than as a free-for-all public forum. This is especially as under the Guidelines due to the submission of the Consolidation Application, IDA would have in its possession or would be able to obtain such information as to enable it to make a determination after its review. This information is likely to be more extensive or superior to the information available to any member of the public. More of a concern is what is the likely impact that such public consultation would have on the duration of the review period. In this regard, please see our comments on Section 4.2 above.

For the above reasons and given that any solicitation to the public for comments under Section 9.2 would mean the release of potentially sensitive information regarding the Applicants and their respective businesses (notwithstanding the exclusion of expressed confidential information), it would be helpful if IDA could provide more concrete and detailed guidelines as to when public consultation will be required in addition to the elucidation provided in Section 9.2.

2. Standards Governing Grant of Confidential Treatment – Section 5.4.2

It is heartening to note that provisions have been made to safeguard the confidentiality of any information provided by an Applicant that might be used in the review process. However we believe that the categories of information set out in Section 5.4.2 that IDA may deem confidential could be further refined, especially as to the standards required of the Applicant or other party/ies to "demonstrate".

For example, only commercially sensitive information that is subject to a pre-existing non-disclosure agreement (NDA) with a third party will be accorded confidential treatment. However there are other commercially sensitive materials that are not the subject of an NDA. Confidential treatment should be accorded to any commercially sensitive material regardless of whether or not it is the subject of an NDA.

Furthermore, we are of the opinion that the definition of '*commercially sensitive*' is too narrow as the three conditions set out in Section 5.4.2 are conjunctive. We would instead suggest that the three conditions be examples of commercially sensitive information or that the definition be inclusive and not exhaustive as it presently is.

Another criteria used in the Guidelines in deciding whether or not to accord confidential treatment is whether disclosure of such information would have a "*material adverse impact*". We are of the view that this test is too stringent and that it may be extremely difficult for an Applicant to prove in most instances. It is also unclear what is the test of materiality in this context.

3. Notification of Denial of Confidential Treatment – Section 5.4.4

Under Section 5.4.4, if the Applicant's request for confidential treatment is rejected, the information will not be used in IDA's review of the application. The Applicant would have to either relinquish confidentiality of the information or have the information excluded from the review process. This may operate unfairly against the Applicant who has to evaluate the risk of relinquishing confidentiality, having such information possibly

released in a public consultation and yet face the prospects of a rejection of the Consolidation Application. This is coupled with the uncertainty of when a public consultation is required and what is deemed as confidential information as mentioned above, especially if market conditions change in view of such consultation or any other reasons beyond the control of the parties. On the other hand, should the Applicant decide not to relinquish confidentiality, they assume the risk that the Consolidation Application might be rejected because IDA did not use such information in its review.

Analytic Framework

1. Market Share Assessment – Sections 6.2.1, 6.2.3 and 6.3.1

We are of the view that too much emphasis may have been placed on market share as a determining factor in deciding whether the proposed consolidation is likely to unreasonably restrict competition, whether as a starting point under Section 6.2.1 for Horizontal Consolidations, in determining market power under Section 6.3.1, or as a presumption of anti-competitive behaviour under Section 6.2.3. Market share alone should not be conclusive in determining that a proposed Consolidation is potentially anti-competitive. An entity with a small market share but has control over crucial infrastructure would still be able to carry out anti-competitive activities. Conversely, an entity with large market share may not necessarily be able to exhibit anti-competitive behaviour.

In any case, we believe that 35% market share may be too low or arbitrary a threshold for the presumption of anti-competitive behaviour and may operate unfairly against Licensees (especially non-Dominant ones) that already have such market share (pre-Consolidation) but with no dominant market power. Reference must surely also be made to the spread of market share amongst the other existing competitors and not just the market shares of the Applicants in isolation.

2. Granting of Approval Without Significant Review – Section 6.3.2

Section 6.3.2 states that significant review will not be carried out if neither applicant '*has more than a 15 percent share of **any** market in which it participates*' (emphasis added). We query whether this refers only to the domestic market or to any other markets outside of Singapore. We submit that only the domestic markets should be relevant as dominant market power overseas by it itself does not necessarily translate into dominant market power in domestic markets.

In any event, we are of the view that 15% is too low a threshold. Assuming even if both Applicants have just over 15% market share each, the collective market share would still be below the 35% threshold for the presumption of anti-competition to apply.

Special Situations

We note that no guidance has been provided to deal with Licensees that are listed in the local or foreign stock exchanges. Listed Licensees are subject to stringent take-over regimes and other reporting and listing obligations. Some of these requirements would require reconciliation with the Guidelines. We are of the view this ought to qualify as a special situation that requires further guidance from IDA.

Taking a purely hypothetical situation to illustrate the possible issues that may arise, when a take-over offer is made under the Singapore Code of Take-over and Mergers, the Board of Directors of the target listed company is required to advise its shareholders on such offer made by the offeror. The Board, in consideration of the interests of all shareholders involved, may conclude that such an offer is not beneficial to the shareholders. However the divesting shareholders may have signed a binding agreement with the offeror conditional upon IDA's approval in accordance with the Guidelines. The management of the target listed company will be placed in a potential conflict situation as it has to file a Consolidation Application and provide the necessary information and assessments (such as of impact on competition and public interest) to support such an application. The various perspectives required from the target company under the different regimes may very well expose the target listed company to potential litigation. In such a situation, the selling shareholders would not be able to alleviate the difficulties faced by the target listed company as they would not able to file the Consolidation Application directly themselves under the Guidelines.

Disposition of Consolidation Applications

Divestiture – Sections 8.3.1.1 and 8.3.1.5

Section 8.3.1.1 provides that IDA may require the divestment of certain assets of one or both of the Applicants as a condition for its approval. There is concern over the extent of involvement of IDA in the divestment process.

Firstly, pricing issues might arise in relation to the sale of an Applicant's operations. A potential buyer knowing that the divesting party is obliged to sell its assets within a limited period of time and only to "*qualified*" buyers under the Guidelines, is likely to take advantage of such constraints by demanding a price much lower than the true market value of the assets.

Secondly under Section 8.3.1.5, IDA has reserved the right to approve the proposed purchaser and may reject such purchaser on the basis that it lacks the ability and incentive to operate the divested assets as a viable, competitive business. We query whether this should be a concern that justifies the rejection of a proposed purchaser.

In most, if not, all cases, a purchaser would naturally be expected to use its best endeavours to realize the maximum value and return possible for any business that it has acquired for good consideration. Furthermore, such a purchaser would most probably be a recipient of an IDA license already. Finally, we also seek clarification on how the commercial assessment of the proposed purchaser in deciding whether it has the ability and incentive to operate the divested assets as a business would be carried out by the regulator and what are the factors that may influence its decision.

If the right to approve any proposed purchaser is to be retained by IDA, we would submit that such right be limited to determining whether the proposed divestment itself may bring forth any other possible anti-competitive behaviour on the part of the proposed purchaser. This would keep the exercise of such discretion within the spirit of the Guidelines.

C. CONCLUSION

While PacNet fully supports IDA's efforts to bring more clarity to the Consolidation review process, it is submitted that a number of the Guidelines require further clarification and refinement.
