

22 May, 2000

Senior Telecommunications Controller
(Competitive Services)
Office of the Telecommunications Authority
29/F., Wu Chung House
213 Queen's Road East
Wanchai
Hong Kong
By Fax : 2803 5112

Our ref: BD-TNI-2110

Dear Sir,

Consultative Paper – Third Generation

Introduction

CLP Telecom is grateful to OFTA for the opportunity to put forward its views on the licensing of third generation mobile services in Hong Kong.

OFTA's decisions on licensing and regulating players in the market for broadband mobile transport services will have profound effects, not only in that market but also in the wider market for so-called "m-commerce" services – that is to say in the market for digital content and e-commerce services consumed on the move.

M-commerce services will be key to achieving the objectives of the Government's *Digital 21* strategy and CLP Telecom believes that OFTA should have regard to the wider impact of its decisions on 3G licensing and regulation.

As a result, CLP Telecom's comments are concerned with four issues, all of which affect the prospects that Hong Kong will benefit from a wide range of innovative m-commerce services provided cost-effectively by a wide diversity of players. These issues are :

- whether any precedence should be given to new entrants in the licensing process (section 4.6¹)
- method of selection of successful operators – by auction or on merit (section 4.14)
- regulatory framework (section 5.7 and 5.12)
- the role of mobile virtual network operators (section 5.18)

Precedence for new entrants (4.6)

CLP Telecom believes that new entrants should be encouraged by reserving one or more licences for them. Involving new entrants in the industry will enable new capabilities and approaches to be deployed for the benefit of consumers.

.../P.2

¹ In this response, section references refer to OFTA's consultative document.

CLP Telecom believes further that OFTA should allow for the possibility of joint ventures between incumbents and new entrants. Such ventures may be able to combine the efficiency advantages of incumbents with the fresh thinking of new entrants. CLP Telecom proposes that any licence applicant in which new entrants have a 30% or greater shareholding should be classified as a new entrant for the purpose of 3G licensing.

Method of selection of successful operators (4.14)

CLP Telecom agrees with OFTA's analysis that auctioning the 3G spectrum will lead to higher prices for consumers. Although the cost of spectrum is a sunk cost, the management of successful bidders will be under pressure to deliver on their business plans in order to meet shareholder expectations and in order to comply with banking covenants. In an oligopolistic market, this can only lead to less intense price competition and hence higher prices.

Nevertheless, CLP Telecom does agree that it will be undesirable if the winning bidders are allowed to capture large monopoly rents and if the method of allocating licences is not seen to be fair and transparent. Not only will there be criticism of a lost revenue opportunity, Hong Kong also risks being criticised by its trading partners for a possible breach of WTO rules.

CLP Telecom therefore suggests that the case for a merit-based system of licence award will be strengthened by :

- ensuring that there is open competition between 3G licensees
- ensuring that the economic benefit of holding a 3G licence is restricted to the areas where this is necessitated by spectrum constraints: licensees should not be able to extend their oligopoly into adjacent markets such as service provision and m-commerce
- greater openness and transparency in the licensing process

CLP Telecom also believes that the licensing criteria should not put too much emphasis on the proposed launch pricing of the bidders. Over the period of the licence, the pricing will change significantly in response to market conditions (as has been the case for PCS operators). It will be better for consumers to pick licensees who will run efficient, low-cost operations and leave it to the market to ensure that benefits of a low cost base are passed to consumers.

Openness and transparency could be achieved by publishing the scoring system and by publishing the score achieved by each bidder based on their initial proposal. Bidders could then be invited to submit a second proposal on the basis of which a final decision was taken. CLP Telecom suggests a further round of consultation once OFTA has specific proposals for the scoring system.

Regulatory framework (5.7, 5.12)

Should the 2G framework be modified?

In launching WAP services, the various network providers have tried to make certain content available exclusively on their networks. For instance, Cathay Pacific's content is available exclusively to customers of C&W HKT's i-menu service.

Some network operators have also restricted their customers to content made available on their own WAP portal instead of allowing access to all WAP sites globally.

These developments show the danger of allowing network operators to tie proprietary content to a particular transport network. CLP Telecom suggests that 3G licensees should be allowed neither to give nor receive special consideration to or from any content or service provider.

How should fixed/mobile convergence be addressed?

This is a significant issue and one that merits a more detailed consultation exercise in its own right.

In the meantime, CLP Telecom would like to highlight the issue that 3G networks will require a substantial amount of fibre-optic transmission for backhaul from base stations and for interconnection.

In CLP Telecom's view, 3G operators should be allowed to make use of existing fibre-optic cables and of new cables placed in existing ducts, on overhead power lines and in similar locations. 3G operators and their suppliers should be allowed limited road opening rights where these are necessary in order to connect base station sites and switching centres to an existing backbone network. As this is facilitating the introduction of a new technology into the Hong Kong marketplace, CLP Telecom believes that this should be regarded as outside the scope of the existing FTNS moratorium.

Mobile virtual network operators (MVNOs)(5.18)

CLP Telecom believes that requiring the 3G operators to support MVNOs will in the long run be extremely beneficial for consumers. CLP Telecom does not believe that this will discourage operators from rolling out networks: an operator which fails to roll out its network will not gain much business, either at a retail or a wholesale level.

It seems clear from the UK auction experience that 3G operators expect to be able to extract significant monopoly rents from their licences. These rents do not appear to be solely due to a network oligopoly – instead they are likely to flow in large measure from an ability to extend the oligopoly into adjacent markets. This suggests that network operators are unlikely to do business with MVNOs on terms which enable 3rd party MVNOs to compete on an equal basis.

Page 4 of 4
22 May 2000
Our ref: BD-TNI-2110

In the Hong Kong marketplace, MVNOs for 2G are almost unknown and CLP Telecom believes that MVNOs for 3G will not emerge on fair commercial terms unless OFTA reserves the right to determine the terms and conditions on which MVNOs “interconnect” with 3G network operators.

Nonetheless, CLP Telecom is conscious of the disadvantages of requiring operators to support MVNOs – especially in the early stages when networks are being rolled out. CLP Telecom believes that incumbent operators have enough advantages that their roll-out plans are unlikely to be affected by their being required to support MVNOs but that new entrants may be more cautious.

CLP Telecom suggests a middle way of requiring incumbent operators to support MVNOs but allowing new entrants a 2-year moratorium before they are required to do so.

Yours sincerely,

Terry O'Neill
Marketing Director

ton:cy/letter1/59-62