

Intrinsic Benefits in Universal Service Provisioning

Telecommunications Regulatory Affairs Advisory Committee
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Universal Service Regime in Hong Kong

- PCCW-HKT Telephone Limited and Hong Kong Telecommunications (HKT) Limited (collectively referred to as “HKT”) has the universal service obligation (“USO”) to provide “basic service” as defined in the Telecommunications Ordinance
- HKT, as the universal service provider (“USP”), is compensated by the telecom industry for the net cost it may incur in meeting the USO
- Net cost means the excess of relevant cost over relevant revenue normally on an actual basis

Research Findings from Wharf T&T Limited

- On 16 October 2015, Wharf T&T Limited (“WTT”) circulated to Members a paper on its research findings on intrinsic or intangible benefits to the USP
- WTT’s paper provides an overview of the treatment of intrinsic benefits by overseas jurisdictions in universal service provisioning

Intrinsic Benefits vis-à-vis USO Costs in Europe

	France	Italy	Spain	Portugal	Ireland
	(€)	(€)	(€)	(€)	(€)
	2002-2013 (annual average)	2004-2007 (annual average)	2006-2012 (annual average)	2007-2011 (annual average)	2009/10 (annual average)
Net cost without intrinsic benefits	70,979,892	28,380,774	63,916,862	26,564,295	7,139,331
Enhanced brand recognition <i>(% of total intrinsic benefits)</i>	30,246,332 <i>(95%)</i>	11,229,546 <i>(59%)</i>	8,568,065 <i>(73%)</i>	3,063,168 <i>(81%)</i>	1,843,698 <i>(90%)</i>
Ubiquity benefit	510,701	150,000	2,283,728	6,899	15,091
Marketing benefit	267,483	7,690,593	570,063	721,910	20,437
Life cycle benefit	696,467	7,500	348,474	-	164,560
Total intrinsic benefits <i>(% of net cost)</i>	31,720,983 <i>(45%)</i>	19,077,639 <i>(67%)</i>	11,770,330 <i>(18%)</i>	3,791,977 <i>(14%)</i>	2,043,786 <i>(29%)</i>
Net cost after intrinsic benefits	39,258,909	9,303,135	52,146,532	22,772,318	5,095,545

Source: WTT's submission on 16 October 2015

Purpose of this Paper

- To provide Members with a summary of WTT's research findings on intrinsic benefits
- To invite views from Members on whether intrinsic benefits should be taken into account in the calculation of universal service contribution (“USC”) payable to HKT

Intrinsic Benefits (1)

- Intrinsic benefits are generally categorised into four types: (a) enhanced brand recognition; (b) ubiquity benefit; (c) marketing benefit; and (d) life cycle benefit
- They are recognised in the UK and member states of the European Community, but not in Australia, Canada, United States and New Zealand, etc.

Intrinsic Benefits (2)

(a) Enhanced Brand Recognition

- It refers to the benefit of greater brand recognition, corporate reputation and associated goodwill as a result of being the USP
- It can be estimated by way of survey on customers' knowledge of the USP having the USO, and whether they use the USP because of its USP status
- An estimate of the benefit is the product of the number of “loyal” customers in profitable areas and the average revenue of those customers

Intrinsic Benefits (3)

(b) Ubiquity Benefit

- It refers to the benefits of having an overall presence through being the USP, which will be reflected in a latent preference for the USP when customers move to other areas
- An estimate of the benefit is based on the number of customers continuing to subscribe to the USP when they move from unprofitable areas to profitable areas

Intrinsic Benefits (4)

(c) Marketing Benefit

- It refers to the potential savings as a result of advertising through the use of public payphones
- An estimate of the benefit is based on the amount charged by the USP for outside companies to purchase advertising space in the same public payphones, and the market research on advertising space

Intrinsic Benefits (5)

(d) Life Cycle Benefit

- It refers to the benefit of serving unprofitable customers because of their potential to become profitable customers
- An estimate of the benefit is to apply different assumptions on the future costs and revenues of unprofitable customers over a fixed period and to determine whether the USP will become profitable in serving these customers

Issues pertinent to Intrinsic Benefits (1)

(a) Enhanced Brand Recognition

- Are customers aware of HKT being the USP?
- What are the customers' considerations when choosing a service provider? (e.g. USP status, quality of service, service charge, after-sale customer service and etc.)
- How to single out the benefit of brand recognition as derived from being the USP? How is it distinct from the benefit of brand recognition as derived from being a large and well established fixed network operator in the market?

Issues pertinent to Intrinsic Benefits (2)

(b) Ubiquity Benefit

- Is the benefit due more to the incumbent status of HKT in the fixed telecom market since 1925 than the USP status of HKT under the USC regime since 1998?
- Where there is a choice to basic service, do HKT's customers choose HKT because of its offer/service or its ubiquitous coverage?
- Is there the information available to calculate the ubiquity benefit? (e.g. the actual number of customers moving from unprofitable distribution point (“DPs”) to profitable DPs with alternative service provider(s))

Issues pertinent to Intrinsic Benefits (3)

(c) Marketing Benefit

- Does HKT advertise on its public payphones?
- Is there any mechanism in place to factor marketing benefit in the USC calculation?
- Should HKT's logo on the public payphones be regarded as advertising?

Issues pertinent to Intrinsic Benefits (4)

(d) Life Cycle Benefit

- How likely will the unprofitable DPs turn to be profitable in the future?
- Are the assumptions on future revenues and costs fair and reasonable?
- Should the benefit be assessed on a historical basis rather than on a forward looking basis so that the USP is compensated based on the cumulative loss?

Advice Sought

- Is it appropriate and practical to take into account any types of intrinsic benefits in the calculation of USC? Views of Members are welcome

Thank you