

Further Discussion on Intrinsic Benefits in Universal Service Provisioning

Telecommunications Regulatory Affairs Advisory Committee
23 June 2016

Background

- At the last meeting on 21 January 2016, Members were briefed on the research findings of Wharf T&T Limited about intrinsic benefits in universal service provisioning
- OFCA agreed to look into the calculation methodologies adopted in various European jurisdictions to facilitate further discussion
- Members were invited to submit written comments on the matter

Further Discussion Today

- This paper summarises
 - views received from Members on whether intrinsic benefits should be included in the calculation of universal service contribution (“USC”) in Hong Kong
 - results of OFCA’s enquiries made on the calculation methodologies adopted in various European jurisdictions for assessing intrinsic benefits

Members' Positions - Whether the Intrinsic Benefits should be included in the USC Calculation

Members	Positions
Certari	Great care should be exercised before a decision is made
HKT	Disagree
Hutchison	Fair and proper as a matter of principle
SmarTone	Study should be carried out for further discussion
TraxComm	More information is required for further consideration
Wharf T&T	Support

Members' Views (1)

- Those in support:
 - it is fair and proper to include such benefits in USC calculation, as they are included in other jurisdictions
 - jurisdictions that have not adopted intrinsic benefits can be distinguished
 - a consultant should be commissioned to estimate the value of intrinsic benefits for further discussion with Members

Members' Views (2)

- Those against:
 - intrinsic benefits are theoretical in nature and entirely arbitrary. Only a small number of jurisdictions recognise intrinsic benefits and there is no uniform or convincing approach
 - existing methodologies are subject to double counting due to possible overlap, e.g. enhanced brand recognition benefit vis-à-vis ubiquity benefit
 - cost of estimating intrinsic benefits may exceed the value of those benefits

Members' Views (3)

- Those against:
 - no enhanced brand recognition benefit: not many people are aware of HKT being the universal service provider (“USP”) but its investment on an extensive network and comprehensive advertising
 - no ubiquity benefit: HKT’s extensive network is not a result of its universal service obligation (“USO”). It is difficult to know whether customers still choose HKT after moving elsewhere is because of its USP status

Members' Views (4)

- Those against:
 - no marketing benefit: block licence from the Lands Department does not allow advertising on payphone kiosks
 - no life cycle benefit: assumptions used to ascertain whether unprofitable customers will become profitable are highly subjective, and the calculation per customer is not possible under the current methodology based on aggregation at the distribution point level

OFCA's Enquiries on Practices of Relevant European Jurisdictions

- Since last meeting, OFCA has made enquiries with the regulators in France, Ireland, Italy, Portugal and Spain about their calculation methodologies on intrinsic benefits
- Ireland, Portugal and Spain replied. Their calculation formulae are simplified for easy illustration

Enhanced Brand Recognition Benefit (“EBRB”)

- It refers to the benefit of greater brand recognition, corporate reputation and associated goodwill as a result of being the USP imposed with the USO

EBRB Formulae (1)

■ Ireland

$$\text{EBRB} = (a) \times (b) \times (c)$$

Where:

(a)	-	total number of universal service customers of USP
(b)	-	percentage of universal service customers willing to pay USO related premium
(c)	-	USO related premium based on 'trigger price increase'

EBRB Formulae (2)

■ Portugal

$$\text{EBRB} = (a) \times (b) \times (c)$$

Where:

(a)	-	brand value of USP
(b)	-	annualized factor
(c)	-	percentage of universal service revenue over total revenue

EBRB Formulae (3)

■ Spain

$$\text{EBRB} = (a) \times (b) \times (c)$$

Where:

(a)	-	total number of universal service customers of USP
(b)	-	percentage of 'loyal' universal service customers due to USP imposed with USO
(c)	-	average margin per universal service customer

Ubiquity Benefit (“UB”)

- It refers to the benefit 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

UB Formula

■ Ireland, Portugal and Spain

$$UB = (a) \times (b) \times (c)$$

Where:

(a)	-	total annual number of universal service customers moving from unprofitable to profitable areas
(b)	-	percentage of universal service customers choosing USP with choice of alternative service provider(s)
(c)	-	average margin per profitable universal service customer

Marketing Benefit (“MB”)

- It refers to the potential savings as a result of advertising through the use of public payphones

MB Formula

■ Ireland, Portugal and Spain

$$\text{MB} = (a) \times (b) \times (c)$$

Where:

(a)	-	space available for placing advertisements on public payphones, including space for USP logo
(b)	-	100% (Spain) or percentage of unprofitable public payphones (Ireland and Portugal)
(c)	-	value of advertising space

Life Cycle Benefit (“LCB”)

- It refers to the benefit of serving unprofitable customers because of their potential to become profitable customers

LCB Formulae (1)

■ Ireland

$$\text{LCB} = (a) - (b)$$

Where:

(a)	-	net costs of USO after applying a mark-up on revenue to reflect the expected change in future revenue due to the change in the characteristics of unprofitable customers
(b)	-	net costs of USO without consideration of LCB

LCB Formulae (2)

■ Portugal

$$\text{LCB} = (a) \times (b) \times (c)$$

Where:

(a)	-	total number of unprofitable universal service customers
(b)	-	percentage of universal service customers that become profitable in the last 5 years
(c)	-	average margin per profitable universal service customer

LCB Formulae (3)

■ Spain

$$\text{LCB} = (a) \times (b) \times (c)$$

Where:

(a)	-	total number of unprofitable universal service customers
(b)	-	estimated percentage of unprofitable universal service customers with subscription of new service in the future
(c)	-	average margin on new service

Observations (1)

- Intrinsic benefits are adopted in some jurisdictions, but not in others
- Examples

Adopted	France, Ireland, Italy, Portugal, Spain, UK
Not Adopted	Australia, Canada, Germany, Japan, Luxembourg, New Zealand, Singapore, USA

Observations (2)

- There are variations in the formulae adopted among different jurisdictions which have included intrinsic benefits in the USC calculation
- If the initiative is to be further pursued, there may be a need to conduct a local survey as funded by the Special Revenue Pool to assess the presence and if so, the significance of the intrinsic benefits in Hong Kong market

Advice Sought

- No conclusion could be drawn for the time being in view of the divisive views from Members and a lack of an objective and consistent methodology for inclusion of the intrinsic benefits in the USC calculation
- Views of Members are sought on the way forward including but not limited to the conduct of a local survey

Thank you