

Summary of Requested Amendments in Operators’ Joint Submission 21 May 2003
and Administration’s Response

Item	Issue	Government Proposal	The Operators' Comments/Requested Amendments	Administration’s Response
1.	Triggers for exercise of the powers	Where there is a <u>change</u> in : a) the control exercised over a carrier licensee b) the beneficial ownership of any voting share in a carrier licensee; or c) the voting control of any of the voting shares in a carrier licensee.	<ul style="list-style-type: none"> ● Power to be exercised only where there is a “change of control” over a carrier licensee i.e. a true structural change in the licensee. ● It is a waste of public resource and an unnecessary burden to carriers and investors if transfer of shares in a licensee with no real change to the “control” of the company are subject to review by OFTA. ● It is also important to note that most mergers are pro-competitive or neutral in competition terms. LegCo should not give powers to the TA to review such mergers. It will be a waste of public resource to do so and will also unduly deter or delay positive mergers. ● Items (b) and (c) defeats any purpose in defining “change of control”. 	<ul style="list-style-type: none"> ● In M&A regulation, the key issue is whether the M&A may substantially lessen competition. ● We have already taken into account industry’s views that a change in principal officer or director of a carrier licensee may not constitute a change in control, and hence affect competition. A Committee Stage Amendment will be introduced to this effect. ● Items (b) and (c) are necessary provisions for implementation of the Bill to cater for situations where a person is already “in control” of a carrier licensee (i.e. have more than 15% shareholdings) but increases his shareholdings such that his influence over the affairs of the licensee will be substantially increased. This can be illustrated in a case where a person already holds 16% shareholding and increases his shareholdings to say 51%, which represents a majority control over the licensee. This change in shareholdings over the licensee may have impact on the competition of the relevant market. Items (b) and (c) are necessary to enable TA to look into such changes because no change in control will arise with respect to such a person who is regarded by the Bill to have already been in control of the licensee.

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				<ul style="list-style-type: none"> • Our present proposal is appropriate. To address the industry's concern, the TA will specify in the guidelines, which provide practical guidance to the industry in interpreting the law, that a change of shareholdings resulting in less than 15% shareholdings is unlikely to raise regulatory concern.
2.	Definition of change of control	Change of control includes a change in the beneficial owner or voting controller of more than 15% of the voting shares in the licensee.	<ul style="list-style-type: none"> • Even if we adopt an additional test by reference to a level of shareholding, 15% is too low. 50% is more appropriate as that is the level at which a party will invariably have control. Any lower percentage in a situation where there is a real "change of control" will be caught by the "effective control test" under Section 7P(12)(d). • Section 7P(12)(d) already provides an "effective control" test – where any person is given the "power to ensure that the affairs of the licensee are conducted in accordance with the wishes of that person". • Even Listing Rules and Takeover Code are only – concerned with "30%" as indicative of change for control. 	<ul style="list-style-type: none"> • As we mention in item(1), the key issue in M&A regulation is whether the M&A may substantially lessen competition. In overseas jurisdictions, the change of control in the context of M&A regulation does not cover only change of "majority control" recognized by company law, but also the ability of "material influence" over the affairs of a licensee which could substantially lessen competition. Therefore the high threshold of 50% in the context of "majority control" over the licensee in the context of company law is not relevant to the M&A regulation. • In USA, Australia and Singapore, the legislation empowers the authorities to review <i>any</i> change in shareholding which has anti-competitive effect. In UK, the threshold set out in the draft guidelines issued by the authority is 15% or more to implement the definition of "control" (which includes the concept of "material influence") in the legislation. • The threshold at 30% in the SFC Code on Takeover is for the protection of minority shareholders. We do not find it a relevant comparison.

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3.	Powers created by the proposed Section 7P – checks and balance	Powers to be exercised by the TA alone subject to appeal to the Competition Board.	<ul style="list-style-type: none"> ● International best practice is that powers to regulate the structure of an industry are vested in a panel of decision-makers, not an individual. Even CITB's own study confirms that among countries like Canada, US, Australia, EU, Singapore and UK, M&A decisions are all made by a panel/committee, not a single power. ● If however Hong Kong should decide not to have an independent body set up for reviewing Telecom M&A but to make use of OFTA's existing resources, the TA should only be empowered to make investigations and grant approvals to M&A. The TA should not be empowered to block a transaction. If the TA believes that an M&A will or will likely result in substantially lessening competition in the market, the M&A case should be referred to the Competition Board for more investigation and decision-making. ● The Competition Board consisting of members from various disciplines should be the only body empowered to make a formal ruling to object to an M&A or to impose conditions, thereby lessening the risk of human 	<ul style="list-style-type: none"> ● As we explain before, we believe that it is of utmost importance that we have an appropriate system with sufficient checks and balances for reviewing M&A matters. ● Under our present system, the TA makes decisions on competition provisions (i.e. sections 7K-7N of the Telecommunications Ordinance), which are subject to appeal to the Appeal Board with wide powers to uphold, vary or quash TA's decisions. This appeal mechanism works well, as the industry deputations testify, and to extend it to review the merits of TA's decisions on M&As would be appropriate. The carrier licensees and the acquirer who are aggrieved by TA's decisions should be allowed to appeal to the Appeal Board. ● The model proposed by the industry is an asymmetric model whereby some M&As (i.e. M&As which TA approve) are subject to appeal to the Appeal Board and some M&As (i.e. M&As which TA believes that they will be anti-competitive) are not subject to appeal to the Appeal Board. We do not find it an appropriate model, as there will be no appeal channel to the Appeal Board against some of the M&As. The integrity of our system would be in doubt without sufficient checks and balances.

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			<p>error by a single person.</p> <ul style="list-style-type: none"> ● A person aggrieved by the TA's decision to approve an M&A can appeal to the Competition Board. ● No statutory right of appeal from decisions of Competition Board except the usual judicial review proceedings. 	
4.	Time Limits	<p>The TA has 1 month from the time the change occurs or 1 month from the time the TA knows of or should know of the change to decide whether to start an investigation.</p> <p>Period for Investigation – 3 month.</p>	<ul style="list-style-type: none"> ● We suggest reducing the period during which OFTA must decide whether to initiate an investigation to 2 weeks. ● We suggest that the period of OFTA investigation be reduced to 1 month. If the TA sees grounds for further investigation or disapproval on the basis of competition concerns, the matter goes to the Competition Board which shall make a decision within 10 weeks. 	<ul style="list-style-type: none"> ● We have already taken into account industry's views to shorten the time limits for the TA to review M&A. In our paper on "Administration's Further Proposed Committee Stage Amendments and Other Improvements" in May 2003, we have reduced the time limits for TA to investigate into a completed M&A :- <ul style="list-style-type: none"> (a) Backstop date (during which the TA is empowered to initiate an investigation) from 3 months to 1 month; and (b) Time limits for TA to conduct investigation, which will be specified in TA's guidelines, from 4 months to 3 months. ● The reduced timelines represent the <i>maximum</i> time needed for the TA to make a quality decision on M&A matters, and comply with the due process requirement including giving sufficient time for the relevant parties to make representations. The actual time taken to review individual M&A may be shorter, depending on the nature and complexity of the case.

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				<ul style="list-style-type: none"> ● Our reduced time limits are shorter than those adopted in overseas jurisdiction : - <ul style="list-style-type: none"> (a) In UK (<i>ex post</i> regime), the Enterprise Act 2002 sets out that the OFT has to investigate a M&A and decide whether to refer it to the Competition Commission within 4 months. The Competition Commission has a further 24 weeks (i.e. 5-6 months) to carry out its investigation. (b) In EU (<i>ex ante</i> regime) the European Commission is obliged to finish investigation within 5 months (1 month for initial investigation, and four months for detailed investigation) from date of notification of the M&A.
5.	Costs for approvals of mergers and acquisitions	The amount of any costs or expenses incurred by the Authority to be recovered fully from the licensee or the applicant for approval. CITB has indicated that the fee will likely range from HK\$50,000 to HK\$110,000, depending on the complexity of the case but does not intend to put an amount in the Bill.	<ul style="list-style-type: none"> ● In deciding whether to allow an M&A to proceed, OFTA is only performing its obligations as a regulator in regulating the market, it is not conferring rights and benefits on the applicant or licensee for which a fee should be charged. ● Even if the Bills Committee should allow OFTA to impose a charge, it is inappropriate that the TA may incur and recover his costs without any limitations. ● Given CITB's indication, we propose a cap of HK\$100,000. 	<ul style="list-style-type: none"> ● OFTA operates as a Trading Fund under the Trading Funds Ordinance. It is required to recover the cost of services from the relevant revenue. This arrangement is similar to that already put into practice in respect of determinations on interconnections under section 36A of the Telecommunications Ordinance. As in the case of fees to be charged on making determination on interconnections, the fees for processing applications for prior consent under the Bill will depend on the actual costs and expenses incurred in processing the particular application. It is therefore not appropriate to set a cap on the fees to be levied. ● This levy of fees only applies to the cases where carrier licensee or the acquirer chooses to seek TA's prior consent. Hence, the TA is offering a service to the carrier licensee or the proposed acquirer (who do not pay any

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				<p>licence fee). It is therefore necessary for TA to recover the costs of the service by the levy of a fee. For those cases where TA investigates into a completed M&A on his own initiative, no fees will be levied.</p> <ul style="list-style-type: none"> ● OFTA envisages that, based on its experience in the levy of fees for interconnection cases, the level of fees for M&A cases would be around HK\$55,000 per case for minor cases; and around HK\$110,000 per case for major cases. Such level of fees will be comparable to those levied by competition authorities overseas for similar work. Examples are given below : - <ul style="list-style-type: none"> (a) Australia : Australian \$15,000 or HK\$60,000 PER case; (b) Canada : Canadian \$26,750 or HK\$133,750 per case; and (c) UK : Pound Sterling 5,000 – 15,000 or HK\$60,000 - \$180,000 depending in the value of the gross assets acquired.
6.	Conflict with licence conditions	Not dealt with.	<p>The Bill should expressly set out that the provisions of the Bill regarding change of ownership or control of a licensee shall override licence conditions on the same subject.</p> <ul style="list-style-type: none"> ● e.g. in the current 3G licence, there is a licence condition requiring a licensee to seek the consent of the TA on any change of control or 	<ul style="list-style-type: none"> ● This is not necessary. After enactment of the Bill, we shall seek amendment, by mutual consent, to carrier licence conditions which are covered by the Bill. ● As for 3G licence, special licence condition 21.2 already stipulates that TA may waive the requirement for the licensee to comply with the statements on control or ownership structure stated in its application for licence. Once the bill is enacted, TA may waive the condition.

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			ownership structure from that stated in its application for licence.	
7.	Guidelines	Guidelines to be published and consultation with industry to occur after the Bill is passed. The substantive provisions of the Bill will take effect on a date appointed by the TA (Section 2(b) of Bill).	Given the importance of the guidelines, it is critical that they are subject to independent review. This review should be conducted by the Legislative Council and accordingly the Bill should not come into force until such a review has taken place.	<ul style="list-style-type: none"> ● As we explained before:- <ul style="list-style-type: none"> (a) Guidelines provide the industry with practical guidance on the approach the regulatory authority will take in assessing M&As. None of them is in the form of subsidiary legislation in Australia, UK, EU, Singapore, USA and Canada; (b) We have already proposed to introduce CSAs such that the Government will commence the Bill only after the guidelines are ready after consultation (see paragraph 18 of the paper "Administration's Proposed Committee Stage Amendments and other Improvement" issued in March 2003); and (c) The TA is statutorily obliged to conduct consultation and issue guidelines after enactment of the Bill. The consultation will be a transparent process whereby the industry and public may give their views. To give Members more assurance, we will notify the Legislative Council Panel on Information Technology and Broadcasting of the consultation of the guidelines. If Panel Members are interested, the Administration can be invited to brief them on the guidelines.
8.	Safe harbours for mergers	None	<ul style="list-style-type: none"> ● The Bill should set out requirements for "safe harbours" to exclude transactions which have no practical effect on competition in the interest of business certainty and efficient use of regulatory resources. 	<ul style="list-style-type: none"> ● To address industry's concern for greater certainty, we will specify "safe harbours" which are not likely to cause competition concern in the guidelines to be issued. In the Explanatory Note on M&A Guidelines issued in Dec 2002, we have specified :

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			<ul style="list-style-type: none"> Such safe harbours can be based on the turnover of the parties, value of the assets to be acquired, or the market share of the parties concerned. 	<p>(i) that TA will normally not be concerned about changes in ownership which are purely transitory (for example, acquisitions by banks, insurance companies or stock brokers with a view to re-selling); and</p> <p>(ii) market share threshold.</p>
9.	Public benefit and Efficiency gain	None	<p>Certain transactions, if demonstrated to produce public benefit or gains in efficiency that will be greater than and will offset the effects of any prevention or lessening of competition that will result from the transactions, should be allowed.</p>	<ul style="list-style-type: none"> The objective of the Bill is to promote effective competition in the telecommunications market. Hence, our proposal to allow the TA to issue directions if there is a “substantially lessening of competition” is appropriate. It would be in the interest of the consumers/public to promote effective competition. “In the public benefit” covers a much wider scope of issues than promotion of effective competition, which is not the objective of the Bill. As we set out in the “Explanatory Note on the Guidelines on the Competition Analysis of M&A” issued in December 2002, efficiency will be considered as a factor in assessing a M&A. Details will be set out in TA’s draft guidelines for consultation after enactment of the Bill.

28 May 2003

Commerce, Industry and Technology Bureau