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Panel on Information Technology and Broadcasting

Meeting on 12 November 2001

**Background brief on liberalization of the local fixed
telecommunications network services market**

Purpose

This paper provides a summary of past discussion on major issues relating to the progressive liberalization of the local fixed telecommunications network services (FTNS) market.

Background

2. Competition in the local FTNS market was introduced on 1 July 1995 when Hutchison Telecom (Hong Kong) Ltd (now Hutchison Global Crossing Limited (Hutchison)), New T&T Hong Kong Limited (now Wharf New T&T Limited (New T&T)) and New World Telephone Limited (New World) were licensed as FTNS operators in addition to the former monopoly operator, Hong Kong Telephone Company Limited. The Administration also introduced a three-year moratorium on the issue of further local FTNS licences to enable the three new operators to roll-out their networks and establish their position in the market.

3. The Administration conducted two rounds of consultation in April and September 1998 to review, inter alia, the progress of liberalization of the local FTNS and whether the moratorium should be extended.

4. In May 1999, the Administration announced, inter alia, the following decisions:

- (a) to extend the moratorium on the issue of further local FTNS licences up to 31 December 2002, subject to satisfactory commitments from the three existing new FTNS licensees on further network roll-out during the moratorium; and

- (b) to issue licences for the operation with effect from 1 January 2003 of external telecommunications facilities based on submarine or land cables to those who have acquired capacity through the purchase of Indefeasible Rights of Use (IRUs) of cables.

5. Members noted that the commitments provided by the three new FTNS licensees under paragraph 4(a) would have the effect of enabling at least 50% of the residential line customers to have an alternative choice of service provider to the dominant FTNS operator by end 2002. To be consistent with the decision on the moratorium, the Government would require all external facilities licensees to use the circuits of the local FTNS licensees for their back haul until 31 December 2002.

Discussion at Legislative Council meetings

6. A motion was passed at the Council meeting on 30 September 1998 urging the Government to adopt positive measures to expeditiously implement the full liberalization of the local and external telecommunications and television markets. In its progress report issued to Members, the Administration has re-affirmed its commitment to implementing progressive liberalization in the telecommunications sector.

7. From time to time, individual Members have expressed concerns on the local FTNS market. In the last (2000-01) session, for example, Hon Howard YOUNG raised a written question on 14 February 2001 on whether unfair competition existed in the market and the difficulties faced by the new FTNS licensees in competing with the dominant operator. On 6 June 2001, Hon CHAN Kam-lam asked an oral question on the progress of network roll-out by the three new FTNS operators and their network coverage.

8. In its replies, the Administration reiterated its policy objective to provide a regulatory environment which encouraged competition and maintained investment incentives. To safeguard competition, anti-competition provisions had been incorporated in the Telecommunication (Amendment) Ordinance 2000 enacted in June 2000. The Administration also detailed measures to assist new FTNS operators, including arrangements for Type II interconnection, accelerating the establishment of "Customer Access Network", enabling the price of residential lines to be determined by economic principles etc.

Discussion at the Panel on Information Technology and Broadcasting

9. Issues relating to the liberalization of the FTNS market have received ongoing attention at the Panel. A chronology of the meetings where such

issues have been discussed is at **Annex I**. The Panel has also exchanged views with the industry and other interested parties.

Moratorium on the issue of further local FTNS licences

10. On the initial three-year moratorium set in 1995, Hutchison, New T& T and New World submitted to the Panel in September 1998 that the moratorium should be extended. They cited difficulties in rolling out their networks, either through interconnection with Hong Kong Telecommunications Limited (HKT), the incumbent dominant operator, or by building their own networks because of difficulties in access to buildings and tunnels. They also considered the three-year moratorium insufficient for establishing a market presence under a flat-rate local tariff regime which would not be fully re-balanced until 2001. In their view, issuing further FTNS licences would only dilute competition and fragment the market.

11. Most of the other submissions received by the Panel, including those from concern groups and overseas telecommunications operators, were in favour of lifting the moratorium so as to encourage competition and innovation. Their view was broadly shared by HKT which also considered that the Government should not perpetuate policies which denied customers the benefits of the full capabilities of HKT. The Consumer Council was concerned that despite competition in the three years since 1995, the three new FTNS licensees had achieved no more than 3% of the market share.

12. The Panel also exchanged views with the Government following its announcement in May 1999 that the moratorium on the issue of FTNS licences would be extended to 31 December 2002 subject to satisfactory commitments from the three new FTNS licensees on further network roll-out during the period. Some members expressed disappointment at the extended moratorium which might not be conducive to enhancing market competition, promoting entry and benefiting consumers.

13. In explaining its decision, the Administration advised that given the long lead time required for constructing networks, an extension of the moratorium would be the quickest way to create effective competition as the three FTNS licensees had already built up their backbone networks. As a result of the extended moratorium, they would be able to have a further period to generate sufficient revenue from basic and premium local services to fund further investments and to help recoup the infrastructure investments already made.

14. To take advantage of new developments in wireless technologies as a faster means to provide competitive network coverage, the Administration would issue licences for the provision of fixed telecommunications services using non-wireline-based networks. Subject to certain binding commitments, the Hong Kong Cable Television Limited was also permitted to provide local

FTNS over its Hybrid Fibre Coaxial Cable Network.

Commitments on network roll-out

15. In September 1999, the Panel was informed that the three new FTNS operators had offered commitments on capital investment and network coverage backed up by a performance bond of \$50 million each to the satisfaction of the Administration. The operators were also required to submit interim progress reports on their rollout commitments. According to the Administration's latest information, only one milestone had not been met on time and remedial action had been taken. As at June 2001, the Administration estimated that more than 30% and 45% of residential line and commercial line customers respectively can choose to subscribe to the services provided by one of the three new operators.

16. Some members questioned the significant difference in the new capital investments offered by the three FTNS licensees and its implications on the market. In response, the Administration pointed out that each FTNS licensee had made its commercial decision on the minimum level of investment which it was prepared to commit. However, competition might provide the incentive for further investment and market expansion.

17. Regarding concern about service standards for the three new FTNS operators, the Administration referred to existing licence conditions which already stipulated the basic requirements and the initiatives undertaken by the individual operators to compete for subscribers. As to the estimated number of households that might switch from HKT to one of the three existing new FTNS licensees as a result of the latter's extended service coverage, the Administration advised that its objective was to widen consumers' choice and it would be entirely up to consumers to choose the FTNS providers they desired.

Interconnection issues

18. In a multi-network environment, interconnection between networks is important to enable :

- (a) customers connected to one network to communicate with customers, or to have access to services, connected to another network (Type I interconnection);
- (b) customers can be reached by one network operator through the customer access network of another network operator (Type II interconnection).

19. In the course of reviewing the progress of network roll-out and the relatively small market share (about 5%) currently achieved by the three new

FTNS licensees, the Panel was deeply concerned about the difficulties cited by some of the operators in effecting Type I and Type II interconnection with the incumbent dominant operator, PCCW-HKT Limited (HKT). The Panel also noted HKT's submission about its difficulty in having to meet demands for interconnection support in the absence of concrete commitments by the requesting FTNS licensees to support their forecasts. A cable-based external FTNS licensee also submitted to the Panel that it had difficulties in building the final segment of its network, or to buy an appropriate element from a local FTNS operator. Members were keen to ensure that arrangements were in place to enable licensees to interconnect promptly and efficiently so as to promote entry and enhance competition.

20. In response, the Administration had referred to overseas experience where it took time to break market dominance. It also stated that the current interconnection framework was based on market-driven principles. Members noted that amendments were introduced to the Telecommunication Ordinance (Cap. 106) in June 2000 to clarify the powers of the Telecommunications Authority (TA) in making determinations on interconnection. Other measures included informal mediation conducted by TA, the publication of a code of practice in April 1999, and the setting up of an industry forum by TA in 1999 which was participated by all the four wireline-based local FTNS operators to work out an agreed procedure on Type II interconnection. The Panel will continue to follow up the progress of interconnection issues.

External FTNS operators

21. Members have taken note of the Administration's decision to progressively open up the external telecommunications facilities market as follows:

- (a) starting from 1 January 2000, to issue licences for the operation of non-cable-based external telecommunications facilities and of external telecommunications facilities based on submarine or overland cables only to those who invest directly in bringing physical cable(s) to Hong Kong; and
- (b) from 1 January 2003 onwards, to issue licences for the operation of cable-based external telecommunications facilities to those who have acquired capacity through the purchase of IRUs of cables.

As at early November 2001, 22 external FTNS licences have been issued while letters of intent to grant licence have been issued to nine companies. The Administration considers that like local wireless FTNS operators, existing external FTNS operators should be allowed to apply to operate local wireline-based FTNS.

The way forward

22. The Government has pledged in the 2000 and 2001 Policy Addresses to invite applications by end 2001 for new local wireline-based FTNS licences to commence operation from 1 January 2003.

23. A consultation paper has been issued by TA on 16 October 2001 to seek the comments of the industry and other interested parties on the implementation of the decided policy on full liberalization of the local FTNS market.

Legislative Council Secretariat

7 November 2001

LegCo Panel on Information Technology & Broadcasting

Panel meetings where FTNS - related issues have been discussed (up to November 2001)

| Date of meeting | Issue |
|----------------------|---|
| 1. 28 July 1998 | 1998 Review of Fixed Telecommunications |
| 2. 3 September 1998 | Briefing by the Secretary for Information Technology and Broadcasting on 1998 Review of Fixed Telecommunications |
| 3. 25 September 1998 | “The 1998 Review of Fixed Telecommunications - A Considered View” (Meeting with deputations and the Administration) |
| 4. 9 November 1998 | 1998 Review of Fixed Telecommunications - the Administration’s response to concerns raised by non-government organizations (including concerns about the local access charge) |
| 5. 8 February 1999 | 1998 Review of Fixed Telecommunications |
| 6. 5 May 1999 | 1998 Review of Fixed Telecommunications |
| 7. 10 May 1999 | 1998 Review of Fixed Telecommunications |
| 8. 12 July 1999 | Moratorium on the issue of further FTNS licences |
| 9. 13 September 1999 | Progress report on the moratorium on the issue of further local fixed telecommunication network services licences |
| 10. 8 January 2001 | Interconnection issues |
| 11. 12 February 2001 | Interconnection issues (Meeting with deputations and the Administration) |
| 12. 12 November 2001 | Implementation of the full liberalisation of the local fixed telecommunications network services market from 1 January 2003 |