

**For Discussion on
9 June 2003**

**Legislative Council
Panel on Information Technology and Broadcasting
Consultation on Review of Type II Interconnection**

Introduction

The Government issued a consultation paper on the review of the policy and regulation of Type II Interconnection on 23 May 2003. This paper aims to brief Members on the consultation.

Background

2. Type II interconnection refers to interconnection at the customer access network level so that operators without such networks can also provide services to customers through the networks of other operators. The Telecommunications Authority first implemented the interconnection policy in 1995 with a view to promoting the telecommunications industry, encouraging investment in network, and facilitating effective competition in the telecommunications market and enhancing consumer choice.

3. In view of the rapidly changing market landscape, the advent of new technologies as well as the fact that more than seven years have passed since the liberalization of the local fixed telecommunications market and the implementation of the narrowband interconnection, the Government considers that it is opportune for the Government to conduct an overall policy review on Type II interconnection. In January 2003, the Secretary for Commerce, Industry and Technology announced that one of the major tasks of the bureau in 2003 was to conduct an overall review on the policy and regulatory regime on Type II interconnection.

Importance of the Review

4. The availability or otherwise of, and the arrangements for, Type II interconnection have major implications on service provision by operators, benefits to consumers, incentive to operators to invest in facilities, and competitiveness of our telecommunications infrastructure. The review on the future arrangements for Type II interconnection will have impact at all levels of public policy considerations, from the evolution of the Government's policy objectives on telecommunications, the shaping of the future structure and development of the industry to the regulatory regime.

The Consultation

Current Market Conditions

5. The current market conditions are very different from those in 1995. As at end December 2002, the incumbent operator PCCW-HKTC has a market share of 81.7% and the new entrants have 18.3% for narrowband services (i.e. voice services). Among the 18.3% market share of the new entrants, 9.7% is via self-built network and 8.6% is via Type II interconnection.

6. For the broadband services market, competition is keen. As at end December 2002, the incumbent operator has 55.3% market share and the new entrants 44.7%. The market share of new entrants is basically achieved through self-built networks, as Type II interconnection for broadband services is still at initial stage.

7. Customers however have wider choice of services than that reflected through market share. While the incumbent's networks (for both broadband and narrowband services) have virtually covered the whole of Hong Kong, new entrants are also extending their own networks. For narrowband services, the three new entrants Hutchison Global Communications Limited, Wharf T&T Limited and New World Telecommunications Limited have extended their network through Type II interconnection to enable over 50% of the residential customers would have the choice of an alternative service provided by one of the them. For broadband services, Hong Kong Cable Television Limited (HKCTV)

provides telecommunications services using cable modem technology over its hybrid fibre coaxial cable network. Its cable modem service has already achieved over 80% home passed. In addition, the local wireless fixed network operators are also extending their networks. They all provide alternative choices to customers.

Current Regulatory Framework

8. The regulation of narrowband and broadband Type II interconnection is separate. Narrowband Type II interconnection is governed by a series of statements issued by the TA on “Interconnection and Related Competition Issues”, last revised on 18 March 2002. Broadband Type II interconnection is governed by the TA statement on “Broadband Interconnection” dated 14 November 2000.

9. For both narrowband and broadband Type II interconnection, Type II interconnection is available for copper-based networks only. It is not applied to optical fibres in customer access networks for the time being.

10. For both narrowband and broadband Type II interconnection, the principle of “long run average incremental costs” (LRAIC), including a reasonable cost of capital commensurate with investment risk, is used. The LRAIC standard is suitable for a market environment where the new market entrants are still establishing their foothold in the industry. The LRAIC-based interconnection charges would fairly and adequately compensate the party providing interconnection while providing an economically efficient “build versus buy” signal.

Matters for Review

11. The review will examine whether the policy on Type II interconnection remains relevant and necessary to facilitate effective competition and promote investment in the telecommunications market. The issues to be looked at include whether Type II interconnection should continue and if so, in what way, taking into account factors such as the nature of services (narrowband and broadband); technologies adopted (copper wires and fibres); and points at which interconnection is to be

made (at telephone exchanges or at individual buildings). The review will also consider whether the existing charging principles adopted for interconnection continue to be appropriate.

Way Forward

12. In view of the importance of the review, comments on the issues are invited on issues set out in the consultation paper by 22 August 2003. Interested parties are invited to submit their views supported by market data and economic analysis on the issues raised in the consultation paper. The Government will consider the submissions to the consultation paper. If necessary, we may conduct a further round of consultation later before concluding the review.

Commerce, Industry and Technology Bureau
2 June 2003