

10 January 2005

The Clerk to the Subcommittee
Legislative Council
Legislative Council Building
6 Jackson Road
Central, Hong Kong
By email and fax (2121 0420)

Dear Sir/Madam

Subcommittee on Telecommunication (Designation of Frequency Bands subject to Payment of Spectrum Utilization Fee) (Amendment) Order 2004 (L.N. 208), Telecommunications (Method for Determining Spectrum Utilization Fees) (Third Generation Mobile Services) (Amendment) Regulation 2004 (L.N. 209) and Telecommunications (Level of Spectrum Utilization Fees) (Second Generation Mobile Services) Regulation (L.N. 210) – Invitation for submissions

I refer to the letter of Ms Debbie Yau on behalf of the Clerk to the Panel on Information Technology and Broadcasting dated 22 December 2004. Hong Kong CSL Limited ("CSL") is pleased to provide its views about the above subsidiary legislation ("Legislation") and its comments are set out below.

(1) Spectrum utilisation fees

CSL does not disagree with the introduction or the proposed level of spectrum utilisation fees ("SUF") for the use of assigned 2G frequency under the proposed 2G mobile carrier licence ("2G Licence"), however believes this is an opportune time to examine whether the SUF under the 3G mobile carrier licence ("3G Licence") is appropriate in the current operating and regulatory environment.

The per kHz rate of the initial SUF (\$145 for the first five years) and the subsequent minimum SUF (\$1,450 for the sixth year to the fifteenth year) under the proposed 2G Licence (collectively, the "2G SUF") are significantly lower than the minimum SUF kHz rates under the existing 3G mobile carrier licence (being \$1,450 in year 1 to \$4,370 in year 15 ("3G SUF")). The differences in unit rates and absolute amounts are set out in Schedule 1.

When the 3G Licences were issued in 2001 the marketplace was particularly bullish about the future of 3G services. Since that time, opinions about revenues attributable to 3G are less optimistic and mobile operators around the world have delayed the launch of 3G services, waiting until more handsets which are acceptable to consumers (ie. similar in size and weight to 2G handsets) have been made available by handset manufacturers, and more useful and interesting 3G applications have been created by developers. Even the Government, in the 2004 Legislative Council Brief about the Legislation, has recognised that the mobile market environment "has become much less bullish"¹.

From CSL's perspective, given the changed operating environment and outlook for 3G services, the kHz rate for 3G SUF should be aligned with the 2G SUF kHz rate. In other words, the kHz rate for 2G SUF should be set at \$1,450 (after the initial transition period where the per kHz rate is \$145) and the 3G SUF kHz rate should be aligned with the 2G SUF rate, so the 3G SUF kHz rate remains at \$1,450 per kHz for the entire period (ie. no rising minimum).

In the 2004 Legislative Council Brief, it is argued that the rising minimum 3G SUF was implemented as "a measure to prevent irrational bidding by bidders of 3G licences, e.g., through over-stretching themselves by submitting aggressive bids"². CSL is not aware of this being the primary reason for implementing a rising minimum 3G SUF. In a Legislative Council Brief released in 2001 in connection with the 3G SUF, it states, amongst other things:

"The proposed method will capture the advantages of deferred cash payment and royalty and best meet our policy objectives. It is "pro-entry" by lowering the financial burden of successful 3G licensees, and allows the Government to share the upside of the future 3G services market...the guaranteed, minimum royalty payment requirement will minimise credit risks for the Government."³

¹ Paragraph 5, Legislative Council Brief: Telecommunications Ordinance (Chapter 106) - Telecommunication (Designation of Frequency Bands subject to Payment of Spectrum Utilization Fee) (Amendment) Order 2004, Telecommunications (Method for Determining Spectrum Utilization Fees) (Third Generation Mobile Services) (Amendment) Regulation 2004 and Telecommunications (Level of Spectrum Utilization Fees) (Second Generation Mobile Services) Regulation, 8 December 2004. File Ref.: CTB(CR)7/23/11 ("2004 Legislative Council Brief").

² Ibid at paragraph 8.

³ Paragraph 12, Annex 3, Legislative Council Brief: Telecommunications Ordinance (Chapter 106) - Telecommunication (Designation of Frequency Bands subject to Payment of Spectrum Utilization Fee) Order. Telecommunications (Method for Determining Spectrum Utilization Fees) (Third Generation Mobile Services) Regulation. 31 May 2001. File Ref.: ITBB CR 7/23/10(01) Pt. 17

As such, it appears that the primary reason for the rising minimum 3G SUF was to ensure the Government met its objectives of receiving a minimum amount of cash from the 3G licensees. The Government's rationale was not predicated on influencing or shaping the decision-making of potential bidders.

Indeed, at the time of introducing the 3G SUF, the Government had not publicly contemplated the levying of 2G SUF. Now, with the proposed introduction of a 2G SUF, the Government will receive further royalties from mobile network operators, a windfall in terms of what it expected to receive in 2001. Comparing CSL's proposal to align the 3G SUF kHz rate with the 2G SUF kHz rate, with the Government's budgeted receipts in 2001, the Government will still receive \$650 million more from the industry as a whole than the amount which it would otherwise have received had it not proposed the imposition of 2G SUF on the 2G licensees and merely levied SUF on 3G licensees. The calculation of this is set out in Schedule 2.

CSL also notes that the Government intends to conduct a spectrum policy review this year. One of the outcomes of the review could be that licensees are able to trade allocated spectrum (which is not uncommon in other jurisdictions). If spectrum trading becomes a reality, Government royalties associated with spectrum (such as SUF) should be set at the same level for spectrum used for substantially similar services, so as to not create an imbalance between licence holders. As such, in order to maintain the technology neutral approach favoured by the Telecommunications Authority ("TA") (in other words, one technology should not be favoured or given an advantage over another), CSL recommends that the per kHz SUF should be set at the same rate for both 2G and 3G spectrum. To maintain the level playing field between licence holders, 3G licensees should also be able to return 3G spectrum to the Government, should they wish to do so. Currently, it is proposed that under the 2G Licence, licensees will be able to return 2G spectrum to the Government, however a similar licence condition does not appear in the 3G Licence.

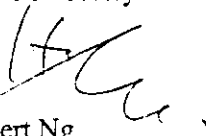
As the proposed level of the 2G SUF has already been disseminated to the public and any increase to the proposed 2G SUF would cause significant detriment to consumers, CSL suggests reducing the existing 3G SUF kHz rate so it is aligned with the 2G SUF kHz rate. A reduction in the 3G SUF kHz rate will be of benefit to consumers as the savings which 3G licensees would reap could be passed onto consumers either in the form of cheaper 3G subscriber fees or greater investment in 3G service innovations.

(2) Frequency bands

The frequency bands set out in Part 2 of the 'Telecommunications (Designation of Frequency Bands subject to Payment of Spectrum Utilization Fee) (Amendment) Order 2004' ("**Order**") are the same as those which the TA proposed to be issued to the existing 2G licensees in his statement 'Licensing of Mobile Services on Expiry of Existing Licences for Second Generation Services' of 29 November 2004 ("**Statement**"). It is interesting to note that Part 2 of the Order does not include spectrum which may be used for E-GSM purposes, despite the TA indicating in the Statement that the band 885-890 MHz/930-935 MHz ("**Band**") had been assigned for E-GSM services in mainland China and the Band would be used for E-GSM purposes in Hong Kong.

In the interests of legislative efficiency and administrative simplicity, CSL suggests to include the Band in Part 2 of the Order in preparation for parts of the Band to be used for E-GSM purposes. From CSL's perspective, it does not matter that the TA has not specified the actual divisions of the Band at this time as presumably those parts of the Band which may not be used (for example, for guard band purposes) will not be used to provide other kinds of services given the TA's comments about the need to align the Hong Kong and mainland China band plans and to only use the Band for E-GSM services.

Yours sincerely


Hubert Ng
Chief Executive Officer
Hong Kong CSL Limited

Schedule 1: Summary of Licence Fees payable by an operator holding 3G, GSM and PCS licences

(HK\$)	Licence year											Minimum SUF for 15-yr Licence period
	1 to 5 (note)	6	7	8	9	10	11	12	13	14	15	
3G SUF-minimum	250,000,000	60,124,000	70,249,000	80,373,000	90,497,000	100,622,000	110,746,000	120,870,000	130,995,000	141,119,000	151,243,000	1,306,838,000
per kHz rate (approx)	1450	1730	2030	2320	2620	2910	3200	3490	3790	4080	4370	
GSM SUF-minimum	12,035,000	24,070,000	24,070,000	24,070,000	24,070,000	24,070,000	24,070,000	24,070,000	24,070,000	24,070,000	24,070,000	252,735,000
per kHz rate	145	1450	1450	1450	1450	1450	1450	1450	1450	1450	1450	
PCS SUF-minimum	16,820,000	33,640,000	33,640,000	33,640,000	33,640,000	33,640,000	33,640,000	33,640,000	33,640,000	33,640,000	33,640,000	353,220,000
per kHz rate	145	1450	1450	1450	1450	1450	1450	1450	1450	1450	1450	

Assumes same spectrum is utilised through the licence period

Note: In each of years 1 to 5, 3G SUF is \$50,000,000, GSM SUF is \$2,407,000 and PCS SUF is \$3,364,000

Schedule 2: Financial effect of aligning the 3G SUF kHz rate with the 2G SUF kHz rate

(HK\$M)	CSL	SmarTone	Hutchison	Sunday	New World	Peoples	Total minimum SUF in 15-yr licence period
3G	750	750	750	750	0	0	3000
GSM	250	250	250	0	0	0	750
PCS	350	350	350	350	350	350	2100
Total Minimum SUF under scenario	1350	1350	1350	1100	350	350	5850
Original 3G minimum SUF	1300	1300	1300	1300	0	0	5200
Variance	50	50	50	-200	350	350	650

Note: references to “SmarTone”, “Hutchison” and “Sunday” in the above table are collective references to the entities holding the 2G Licences and 3G Licences