

**Submission to**  
**Second Consultation Paper on**  
**Licensing of Mobile Services on Expiry of**  
**Existing Licences for**  
**Second Generation Mobile Services**

**By**  
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## **INTRODUCTION**

1. SmarTone Mobile Communications Limited (“SmarTone”) appreciates the opportunity to present its views on the consultation paper<sup>1</sup> issued by OFTA on 19 March 2004 (“the Second Consultation Paper”). As the issues raised in the Second Consultation Paper and any decisions made thereafter will have far-reaching implications for the entire mobile industry in Hong Kong, the consultation warrants careful deliberation. SmarTone hereby submits the following views for Government’s consideration.

## **LICENSING ARRANGEMENT FOR THE EXISTING 2G LICENCES**

### **Offer of ‘Right of First Refusal’**

2. Section 2(2A) of the Telecommunications Regulations expressly states that a public radiocommunications service (“PRS”) licence shall be valid for 10 years from the day on which it is granted, and, subject to the discretion of the Telecommunications Authority (“TA”), be extended for a further period of up to 3 years. The TA has exercised his discretion in 2001 to extend the GSM, CDMA and TDMA licences for 3 years, with the intention of aligning the expiry dates of these licences with the PCS licences. Therefore, the proposal in the Second Consultation Paper for the offer of “right of first refusal” is consistent with the TA’s stated policy.

3. Paragraph 9 of the Second Consultation Paper sets out five relevant considerations which the TA would take into account in deciding the future licensing arrangements for mobile services, namely 1) to ensure choice of services; 2) to provide stable investment environment; 3) to ensure efficient use of spectrum; 4) to ensure continuity of customer service and 5) to maintain technology neutrality. SmarTone is of the view that ‘efficient use of spectrum’ is the most critical and fundamental factor in determining whether an offer of the “Right of First Refusal” should be granted to a licensee.

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<sup>1</sup> “Licensing of Mobile Services on Expiry of Existing Licences for Second Generation Mobile Services – Analysis of Comments Received, Preliminary Conclusions and Further Consultation”, OFTA March 2004  
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4. *Efficient use of spectrum* - SmarTone supports the TA's view that "in granting the "right of first refusal", the TA is minded to take into account whether the existing licensee has achieved efficient use of the scarce public resource during the tenure of its licence."<sup>2</sup> Since radio spectrum is a scarce and valuable public resource, it should be efficiently utilized to derive the maximum benefit to the community.

5. SmarTone strongly supports the TA's proposal that the "right of first refusal" should be offered to the nine incumbent GSM/PCS licensees. There is no doubt that these licensees have been making efficient use of the frequency spectrum assigned to them at all times during the term of their licences, and is evident with the large customer base built up by each of the incumbent GSM/PCS licensee. It is important to ensure that these licensees can continue to offer their services to more than 7 million people in Hong Kong without any interruption.

**'Right of First Refusal' Not to be Offered to CDMA and TDMA licensees**

6. The TA has pointed out that "*the CDMA and TDMA licensees had not actively developed and marketed their services*"<sup>3</sup>. Furthermore, "*according to the statistics, in stark contrast with the continuous growth of the GSM and PCS services, the number of subscribers of the CDMA and TDMA services has been declining steadily over the years. For the CDMA network, the number of subscribers fell from 280,000 in year 2000 to around 40,000 in year 2003 whereas for the TDMA network, the figure fell from 140,000 to around 30,000.....Moreover, the number of installed CDMA base station dropped from about 460 in year 2000 to about 300 in year 2003. For the TDMA network, the figure is even more startling, dropping from 400 to around 50 over the same period.*"<sup>4</sup>

7. In view of the above, "*the TA is therefore of the view that the CDMA and the TDMA licensees have not achieved efficient use of the scarce spectrum resource. As such, the TA is of the view that for better utilization of the spectrum which will in turn benefit the community at large, the CDMA and the TDMA licensees should not be entitled to the*

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<sup>2</sup> Paragraph 25, Second Consultation Paper

<sup>3</sup> Paragraph 22, Second Consultation Paper

<sup>4</sup> Paragraph 25, Second Consultation Paper

*right of first refusal.*”<sup>5</sup> SmarTone strongly supports the notion of efficient use of spectrum and therefore concurs with the TA’s views as stated in the Second Consultation Paper.

## **ISSUE ONE NEW MOBILE LICENCE EMPLOYING BLOCK A IN THE 800MHZ BAND.**

### **Determining Factors for the Issue of a New Licence**

8. SmarTone is neutral as to whether the Government should issue a new licence. SmarTone takes the view that ‘market forces’ and ‘public interest’ are the two key factors in determining whether a new licence should be issued under the vacated 800MHz spectrum.

9. The Government must ensure that the issuance of a new licence is in the public interest; the auction process is fair and transparent; and there is a level playing field for both the new and existing licensees. Potential bidders for the new licence will automatically take into account the business and regulatory environment and the market demand before making a decision. SmarTone considers that the licensing process for the new licence must be fair and transparent, and that the terms applicable to the new licence should not give any advantage to the new licensee over the existing licensees.

10. SmarTone supports the current proposal in the Second Consultation Paper allowing the incumbent licensees to bid for the new licence in the vacated 800MHz band.

## **METHOD OF AWARDING THE NEW LICENCE FOR BLOCK A**

### **Auction rules of the New Licence**

11. The Second Consultation Paper merely sets out the broad principle that the auction will adopt a hybrid approach which is to be similar to the 3G licence auction process in 2001 (i.e., a pre-qualification stage plus an auction stage), and paragraph 58 of

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<sup>5</sup> Paragraph 26, Second Consultation Paper

the Second Consultation Paper provides that *“the current thinking of the TA is to conduct a simple single-round sealed bid auction”*.

12. SmarTone is of the view that the auction rules for the new licence should follow the same sets of rules for the bidding of the four 3G licences in 2001, as particularly stipulated in the “Information Memorandum for Hong Kong Third Generation Mobile Services Licensing” issued in July 2001. It is understood that the Government engaged consultants to design the comprehensive auction rules for the 2001 bidding with the prime objective to prevent collusive activities. The Government took the view that the 3G bidding process should be *“a very sophisticated and intense process. Procedures for the selection process must be efficient, fair and transparent, while at the same time legally sound and comprehensive. Overseas experience demonstrates that the bidding rules must be carefully designed, for example, to restrict bidding by connected parties and to prevent collusive activities.”*<sup>6</sup> As a result, various measures such as the “dark room”, the multi-round ascending auction and the connected bidders rules were designed and introduced to minimize the possibility of collusion and manipulation of the auction result. The 3G licence bidding process in 2001 was therefore conducted with the highest standard of probity and integrity. There is no reason to deviate from this well-established and proven process. In particular, SmarTone objects to any proposal for the award of the new licence through a simple single-round sealed bid auction.

13. SmarTone considers that the reserve price for the new licence should be higher than the reserve price for the 3G licences bidding in 2001 because the exposure on business and technology risks facing any potential bidder for the new licence, at the time of the proposed auction, will be much reduced when compared to the situation in 2001. Furthermore, by the time the new licence is granted (at around 2005 to 2006), 3G services will have been firmly established – a situation that will have been brought about largely by the efforts of the current four 3G licensees. It is therefore fair and reasonable and in the public interest for the TA to increase the minimum reserve price of the new licence to reflect the overall reduced business and technology risks faced by the new licensee. Under no circumstance should the reserve price for the new licence be lower

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<sup>6</sup> Legislative Council Brief, “Funding for Engaging Consultants for Licensing of Third Generation Mobile Services”, Information Technology and Broadcasting Bureau, November 2000

than the reserve price for the existing 3G licences, as that will constitute an unfair advantage for the new licensee.

## **POLICY OBJECTIVES OF PROMOTING MOBILE DATA SERVICES THROUGH ISSUING A NEW LICENCE**

14. As stated in the press release issued by the Commerce, Industry and Technology Bureau (CITB) on 19 March 2004 on the publication of the Second Consultation Paper, “*the objectives of issuing a new licence from the vacated spectrum are to facilitate the introduction of advanced and innovative mobile services*”. The Second Consultation Paper proposed to impose more stringent conditions on the new licence such as the requirements for a data transmission rate higher than the existing 3G licences and dedicated network capacity for mobile data services.

15. The success of mobile data services is driven by customer requirements and market demand rather than just technical requirements such as mandating certain minimum radio speed. Customers are seeking valid propositions and superior total user experience when selecting mobile data services. SmarTone questions whether a peak data rate per radio carrier of at least 2 Mbps would, per se, accelerate the adoption of mobile data services in Hong Kong. There are many other factors which are far more fundamental and germane to the uptake of data services than just speed.

16. SmarTone notes that there are several remarks in the Second Consultation Paper suggesting that the CDMA 2000 standard is better than the GSM 850 standard. SmarTone is of the view that the TA should maintain its technology neutral policy in all circumstances and allow the market to decide which technology should be adopted.

17. The Government’s policy objective to promote mobile data services may not materialize with the mere introduction of a new licence and the proposed “more stringent” licence conditions in the new licence. There are many factors other than speed and technology standard that would affect the development of mobile data services.

18. The most important factor hindering the adoption of mobile data services in Hong Kong is operators' lack of scale in an already small market. Mobile operators in Hong Kong are unable to achieve further economies of scale and this limits their ability to fund the development and marketing of even more varied services more aggressively.

19. Operators' attempts to achieve scale have been hampered by Government's interference in the market. For instance, the adoption of the proposed safe harbour thresholds in the recently adopted merger and acquisition regulation is actually contrary to the light-handed regulatory approach. Another example is the two time waiver of the submission of performance bond by the 3G licensees and thereby unduly favoring a financially stressed operator. Inability to scale constrains operators in the greater exploration of new services.

20. SMS or its equivalents constitute the vast majority of overseas operators' data revenue in both GSM and non-GSM markets. This is largely attributable to the still relatively high prices being charged for voice services in overseas markets and the consequent compelling rationale for mobile users overseas to adopt SMS as a serious alternative to voice for communication purposes. Wide adoption of SMS in P2P communication is important in educating users and familiarizing them for more sophisticated and interactive data services to come. Unfortunately, the pricing rationale for Hong Kong customers is not the same as overseas because of the very low pricing for voice services in Hong Kong. Together with the relative ease of making a call and the reluctance to text in English as well as the more cumbersome Chinese input, it is not surprising that the take up of SMS has been slow even when SMS sent and received within a network is now essentially free of charge.

## **PAYMENT OF SPECTRUM UTILIZATION FEE (“SUF”) FOR GSM/PCS LICENCES**

21. In its submission to the First Consultation Paper<sup>7</sup>, SmarTone has pointed out that it is important to first define the meaning of “3G services or similar advanced mobile services” before it can make any meaningful analysis of the proposed SUF options in the First Consultation Paper. The current proposal on SUF in the Second Consultation Paper requires existing GSM/PCS licensees to pay SUF, before 1 January 2010, on a structure that is to be different from that for the 3G licensees - regardless of whether they will or will not provide 3G or similar advanced mobile services. In the circumstances, it will not be necessary to have a definition of “3G services or similar advanced mobile services”.

22. The Second Consultation Paper merely sets out the broad principles applicable to the SUF for GSM/PCS licences without any details about the exact structure and level of SUF before and after 1 January 2010. SmarTone reserves its right to make further comments when more details on the structure and level of SUF applicable to GSM/PCS licensees are available for consultation.

23. As regards the SUF proposal in the Second Consultation Paper, SmarTone is in support of the principle that the GSM/PCS licensees should pay the same level of SUF as the 3G licensees on parity grounds. Since it has been the policy decision to require 3G licensees to pay SUF, it would only be fair to require GSM/PCS licensees to pay the same level of SUF under their new licences. This is also in line with the notion that spectrum is a scarce and valuable resource, and the use of spectrum should be subject to a usage charge.

24. Further to the principle of parity, SmarTone is in support of the view that the SUF applicable to GSM/PCS licences should eventually converge with the 3G SUF. However, there should be no need to impose a minimum fee requirement on the existing GSM/PCS licensees because they have already attained well-established business operations and

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<sup>7</sup>“Licensing of Mobile Services on Expiry of Existing Licences for Second Generation Mobile Services” OFTA, 1 August 2003

have built up large customer bases, thereby effectively providing a firm basis upon which the annual SUF can be calculated by reference to existing revenue.

## **LICENCE CONDITIONS APPLICABLE TO THE GSM/PCS LICENCES**

25. SmarTone welcomes the TA's decision to withdraw the proposals of mandating the existing GSM/PCS licensees to provide coverage to specified locations and the provision of Cell Broadcast Service/Multimedia Broadcast Multicast Service by the licensees.

26. However, the TA still intends to impose the 30% open network access ("ONA") requirement on the GSM/PCS licensees when they take up the "right of first refusal". SmarTone reiterates its objection against the ONA requirement whether it is to be imposed on the 2G or 3G licence. SmarTone strongly believes in the notion that the arrangement between mobile network operators ("MNO") and any mobile virtual network operator ("MVNO") or content service providers ("CSP") should be purely determined by market forces, or, through the process of commercial negotiation between the parties. The ONA requirement will inevitably hinder the operation of market forces.

27. There is no question that the mobile market in Hong Kong is very competitive by world standard. There is no need for regulatory intervention because market forces are the best regulator in such a highly competitive market. In fact, market forces have worked well for the arrangement between MNO and MVNO/CSP arrangement in the 2G market without any ONA requirement. There is also no evidence to support that ONA is the key contributor to the success of mobile data services in other countries.

28. There is an argument that the TA would not exercise its power under the ONA requirement until it is considered that the market is ineffective to sort out the arrangement between MNO and MVNO/CSP. Hence the ONA requirement is seen as a kind of "reserve power" of the TA and such power would only be exercised when there is market failure.

29. However, SmarTone is of the view that the above argument ignores the fact that the mere existence of the ONA requirement would hinder the operation of market forces. With the ONA requirement, it is expected that the MVNO/CSP will not negotiate with the MNO in good faith since they would rather rely on the assistance of the TA to get the best possible terms. This expectation alone will disrupt the operation of market forces and results in inefficiency and misallocation of resources.

30. Based on the foregoing, SmarTone would urge the TA not to impose the ONA requirement on any mobile licensee.

### **MANDATORY CODE OF PRACTICE**

31. The TA has maintained his view that certain Codes of Practice (“CoP”)<sup>8</sup> should be made mandatory in the new licences even though there is no industry support on the proposal. In addition, the TA intends to add the Quality of Service (“QoS”) requirement as a mandatory CoP in the new licences.

32. As regards the proposed mandatory CoP as stated in the First Consultation Paper, SmarTone reiterates its opposition to such proposal. It is neither necessary nor appropriate to make certain CoP mandatory in the licence. OFTA has issued a number of CoP in the past which deal with customer issues. Although most of them are voluntary in nature, there is no evidence suggesting that operators have not complied with such CoP under self-regulation. The proposal is contrary to the light-handed regulatory approach. Furthermore, making certain CoP as mandatory in the GSM/PCS licences is unfair to these licensees given that the issues raised in these CoP are also common to non-mobile operators. SmarTone is also concerned that the implementation of the above proposal will create inconsistencies in the licensing regime which may trigger further action by OFTA to impose similar conditions in other licences in the future.

33. SmarTone also opposes to the requirement on QoS as proposed in the Second Consultation Paper. SmarTone strongly believes QoS is a commercial decision for each

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<sup>8</sup> Code of Practice on Mobile Service Contract and Code of Practice on Protection of Customer Information  
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operator, which is driven by the relative position of operators in the market and market needs. The market should allow different QoS so that customers can make their own choice according to their needs. It is also envisaged that there will be practical difficulties in defining and having a standardized measurement of QoS and in that case any comparison of QoS is likely to be misleading to the general public.

## **SEED SPECTRUM**

34. The Second Consultation Paper has mentioned that certain frequency spectrum will be reserved as seed spectrum for future migration or upgrade plan. However, there is no detail about the allocation criteria of the seed spectrum.

35. SmarTone is of the view that the basic principle of allocation of spectrum should apply here, that is it should be determined by market forces. The allocation of seed spectrum should be subject to a competitive bidding process to ensure that seed spectrum is used and allocated in the most efficient manner.

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