

寶維斯律師事務所
香港及國際律師

12TH FLOOR, HONG KONG CLUB BUILDING
TELEPHONE (852) 2536-9933

3A CHATER ROAD, CENTRAL, HONG KONG
FACSIMILE (852) 2536-9622

WRITER'S DIRECT DIAL NUMBER

WRITER'S DIRECT E-MAIL ADDRESS

WRITER'S DIRECT FACSIMILE

PARTNERS
JEANETTE K. CHAN
JOHN E. LANGE
MICHAEL REEDE

Office of Telecommunications Authority
29/F Wu Chung House
213 Queens Road East
Wanchai
Hong Kong

Attention: Senior Telecommunications Engineer
(Technical Regulation) 2

By Fax and E-mail

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Memorandum

Licensing of Mobile Services on Expiry of Existing Licenses
for Second Generation Mobile Services

Background

This memorandum is submitted in response to the consultation paper issued by the Telecommunications Authority of Hong Kong (the "TA") on March 19, 2004, regarding the licensing of mobile services in Hong Kong upon the expiry of the current 2G licenses (the "Consultation Paper"). The TA has set out in the Consultation Paper his preliminary views on the licensing arrangements for the mobile sector following the expiry of the existing 2G licenses. One of the TA's preliminary views is that nine out of the current eleven existing 2G licensees should be offered a right of first refusal for new

licenses¹ to operate on the existing 2G frequency spectrum when their respective licenses expire (the "Right of First Refusal"), but that the operator deploying the IS-95 CDMA standard (the "CDMA Licensee") and the operator deploying the IS-136 TDMA standard (the "TDMA Licensee") should not be granted a Right of First Refusal². The reasons given by the TA for these proposals are that the CDMA Licensee and the TDMA Licensee have not actively developed and marketed their services and the number of subscribers of the CDMA and TDMA services has been declining steadily over the years. As radio spectrum is such a scarce public resource, the TA has formed the preliminary view that it would not be in the public interest to offer the CDMA Licensee and the TDMA Licensee the Right of First Refusal and that it would be preferable to re-allocate part of the vacated frequency spectrum (the frequency block referred to as "*Block A*" in the Consultation Paper) to a new licensee to introduce advanced and innovative mobile services to consumers in Hong Kong. In order to achieve this objective, the TA has proposed that the new licensee should be subject to more stringent license conditions relating to the provision of mobile data services. Furthermore, the TA notes in the Consultation Paper that the new licensee will be able to utilize cdma2000 technology to provide various advanced and innovative mobile data services that are currently not available in Hong Kong³.

As you may know, Paul Weiss Rifkind Wharton & Garrison is an international law firm, headquartered in New York and with many offices worldwide, including an office in Washington DC and one in Hong Kong. Our Hong Kong office is qualified to practice Hong Kong law. We are an all service law firm but one of the areas of our focus is telecommunications law and regulation. We have extensive experience on telecommunications regulatory matters and frequently advise on telecommunications

¹ A new license will be granted in lieu of a renewal of the existence license because of a change in the licensing regime in Hong Kong. For full details, refer to paragraphs 5 to 8 of the Consultation Paper.

² See paragraphs 11 to 15, and paragraphs 22 to 26 of the Consultation Paper.

³ See paragraphs 36 and 37 of the Consultation Paper.

regulatory issues, including advising and assisting telecommunications regulators on telecommunications laws and policies.

Commentary

While we understand that the TA's proposals outlined above are intended to introduce advanced and innovative mobile services to Hong Kong, spawn new industries and enhance Hong Kong's status as a mobile services hub in Asia, we are concerned that the TA has not fully considered the ramifications of his recommendation not to grant the CDMA Licensee and the TDMA Licensee the Right of First Refusal (which is in effect a right of renewal of their respective licenses). In addition, we do not believe such a proposal would in fact garner the result intended by the TA. We believe that TA should reconsider his proposals, and should grant to the CDMA Licensee and the TDMA Licensee the Right of First Refusal for at least three reasons: (a) it is inconsistent with internationally accepted practice to withhold renewal of mobile licenses in the manner proposed by the TA, (b) the decision not to grant the renewal will likely have a negative impact on investments in the telecommunications industry, hamper growth and deter new entrants, and (c) the TA's proposal may result in inappropriate regulatory influence on the choice of technology used by operators.

Internationally Accepted Practice

We believe that it is internationally accepted practice for mobile operators to have an expectation that their licenses will be renewed at the end of their respective terms. In the U.S., the Federal Communications Commission ("FCC") has had a longstanding policy (implemented by various rules and orders) designed to provide strong assurance to certain licensees and their investors that an FCC license will essentially be renewed as a matter of course.⁴ The Staff Report of the FCC Biennial Regulatory Review 2000⁵ states

⁴ See, e.g., 47 C.F.R. § 24.16; *Amendment of the Commission's Rules to Establish New Personal Communications Services*, 8 FCC Rcd 7700, 7753 (1993); *Amendment of Part 22 of the Commission's Rules Relating to License Renewals in the Domestic Public Cellular Radio Telecommunications Services*, 8 FCC Rcd 2834, 2836 (1993).

that: "*As a practical matter, granting renewal of wireless licenses has proved to be virtually automatic except where the licensee has violated Commission rules, which only occurs in a very small percentage of cases.*"⁶

We note that this "automatic" renewal policy has been applied even in the face of competing applications at the time the renewal of an FCC license is sought. The policy, known as a "renewal expectancy", has been applied to all commercial wireless services and certain other telecommunications services. Using personal communications services ("PCS") licenses as an example (some of which utilize CDMA or TDMA technology), the renewal expectancy provides a sound basis for PCS licensees to expect that they will be able to take advantage of their licenses well beyond the initial 10-year license terms. Under the renewal process, if the FCC determines that a renewal applicant is entitled to a renewal expectancy, the renewal application is immediately granted (assuming the applicant is otherwise qualified), and any competing applications are dismissed without consideration. Such a renewal applicant is therefore basically guaranteed to receive license renewals routinely. Moreover, qualifying for such a renewal expectancy is not difficult or burdensome, and occurs in the normal course of business.

Again, using PCS licenses as an example, under the renewal expectancy rules, a renewal applicant will obtain a renewal expectancy if it (a) has provided "substantial" service during its past license term; and (b) has substantially complied with applicable Commission rules, policies and the Communications Act.⁷ "Substantial" service is defined as service which is sound, favorable, and substantially above a level of mediocre service which might just minimally warrant renewal. A licensee that provides solid, reputable services, and complies substantially with the FCC Rules, is therefore effectively guaranteed to receive license renewals as a matter of course.

⁵ Federal Communications Commission Biennial Regulatory Review 2000 Staff Report dated September 18, 2000.

⁶ Id. at Paragraph 104.

⁷ 47 C.F.R § 24.16(a)-(b).

In order for Hong Kong to maintain its position as a leading telecommunications hub in Asia with a stable regulatory environment and a licensing regime that conforms with international practices, we believe that the TA should consider granting the CDMA Licensee and the TDMA Licensee the Right of First Refusal unless either licensee is in breach of its license conditions (e.g. if it has failed to fulfill its network rollout obligations set out in the license) or if sufficient advance notice has been given to the Licensees. Given that both the CDMA Licensee and the TDMA Licensee seem to have fulfilled their respective license conditions, and that the CDMA license is due to expire in November 2005 and the TDMA license in July 2005, we do not believe that sufficient advance notice will have been given to the licensees with respect to what would effectively be a non-renewal of their licenses.

Impact on Investments in the Industry

All telecommunication operators are required to invest and continually invest in their networks throughout the term of their licenses in order to maintain and improve the service provided to customers. If, contrary to international practice and industry expectation, the TA declines to grant the Right of First Refusal to the CDMA and the TDMA Licensees and fails to renew their licenses without sufficient advance notice, other existing licensees may be deterred from investing in their respective networks towards the end of their licenses as they would not wish to make any significant investments where there is a possibility that their licenses will not be renewed. This would naturally lead to a decline in both the quality and variety of services provided to customers during the last few years of the term of the licenses.

Furthermore, such a decision would set a bad precedent and would discourage new entrants. Local and overseas telecommunications operators would be reluctant to apply for new licenses and offer new services in Hong Kong if the operators are not confident that their licenses would likely be renewed after expiry of their term even if they had complied with all the license conditions and had made substantial investments in the services during the term of their licenses. This may lead to the opposite result from what the TA had intended to achieve.

Just as importantly, even if the licensees were willing to invest in their networks throughout the term of the license, they may find it difficult or even impossible to obtain financing for their capital expenditure requirements if they are not able to rely on a renewal expectancy. According to the FCC, the "*relatively long [license] period and high renewal expectancy [for NPCC licenses] will provide a stable environment that is conducive to investment, and thereby will foster the development of PCS.*"⁸ Because "*some capital expenditures . . . may not be recoverable before a particular license term expires . . . renewal expectancies provide assurance to investors and other sources of financing that their funds will not be placed in unreasonable jeopardy.*"⁹ Indeed, "*without a relatively long license term and a high renewal expectancy investors would be reluctant to make investments in equipment, training and marketing specific to a particular PCS system.*"¹⁰ We believe this principle applies equally in Hong Kong, and we urge the TA to consider the impact on future investments in telecommunication networks if he denies the Right of First Refusal to the CDMA and TDMA Licensees.

Regulatory Influence on Choice of Technology

The TA has consistently stated in the past that he wishes to adopt a technology neutral approach to licensing of mobile services and wishes to allow market forces to decide on the technology to be adopted. This approach would permit licensees to make full use of latest technological advances in the provision of services. We note, however, that in the Consultation Paper, the TA has highlighted the rapid and successful development of mobile data services that utilize the cdma2000 standard in other countries¹¹ and the advantages of using the cdma2000 standard in providing new mobile

⁸ Amendment of the Commission's Rules to Establish New Personal Communications Services, 8 FCC Rcd 7700, 7753 (1993).

⁹ Amendment of Part 22 of the Commission's Rules Relating to License Renewals in the Domestic Public Cellular Radio Telecommunications Services, 8 FCC Rcd 2834, 2836 (1993).

¹⁰ Amendment of the Commission's Rules to Establish New Personal Communications Services, 7 FCC Rcd 5676, 5707-08 (1992).

¹¹ See paragraph 36 of the Consultation Paper.

data services not yet available in Hong Kong. The TA has proposed to allocate the *Block A* frequencies to the new licensee, a block of frequency which would be well-suited to the deployment of services using the cdma2000 standard. Furthermore, the TA has pointed out the difficulties in adopting other standards (such as the GSM 850 standard) in the *Block A* frequencies¹² and proposes to impose targets on the levels of mobile data usage on the new licensee.

We appreciate that the TA has stated that the new license will not impose an obligation on the licensee to use the cdma2000 standard, but we are concerned that, given the technologies currently available and the proposed obligation on the new licensee to achieve certain mobile data usage targets, the TA may have inadvertently but effectively imposed a requirement on the new licensee to use the cdma2000 standard. We are concerned that the TA may not have taken into account the possibility that future technological advances may enable the existing CDMA and TDMA Licensees to also provide mobile data services by utilizing their current frequencies. We are also concerned that TA's proposals may lead to the perception that the TA has favored the cdma2000 standard over the IS-95 CDMA standard and the IS-136 TDMA standards, thereby contradicting the TA's stated policy of adopting a technology neutral approach to mobile licensing. This may also lead to the perception that the TA is imposing unnecessary regulatory intervention and pressure on the market.

Finally, we believe that the TA should respect the right of the licensees to exploit their assets as they see fit so long as they comply with the conditions of their licenses. If new services are developed which utilize a particular part of the spectrum that has been granted to existing licensees, the right to exploit such services should belong to the existing licensees. The TA should not be seen as interfering with the rights of the existing licensees by reallocating their exploitation rights to other licensees.

¹² See paragraphs 37 & 42 of the Consultation Paper.

Conclusion

We urge the TA to re-consider his recommendation not to grant the Right of First Refusal to the CDMA Licensee and the TDMA Licensee. We believe that to do so may harm Hong Kong's telecommunications industry in the long term. Both licensees and investors may be discouraged from making substantial investments in wireless ventures, as they may question whether the Hong Kong regulatory regime will continue to conform with internationally accepted practices on key issues such as renewal of licenses. This may in turn lead to an adverse impact on the future development of the industry as a whole. Additionally, the TA's proposal to re-allocate the *Block A* frequencies to a new licensee for the provision of mobile data services may lead to the perception that the TA is favoring the cdma2000 standard over other standards used by existing licensees and be regarded as unnecessary regulatory intervention on the market.

**Paul, Weiss, Rifkind, Wharton & Garrison
Hong Kong Solicitors**