

**APPLICATION FOR RECLASSIFICATION OF
THE PHILIPPINES AND TAIWAN ROUTES AS CATEGORY A
BY CABLE & WIRELESS HKT LIMITED**

Statement of the Telecommunications Authority

3 October 2000

INTRODUCTION

The Telecommunications Authority (TA) has received from Cable & Wireless HKT Limited (CWHKT)¹ an application for reclassification of the Philippines and Taiwan routes as Category A routes (Application). CWHKT also requests that CWHKT be declared non-dominant in the retail market for the Philippines and Taiwan routes upon reclassification, in accordance with the TA Statement entitled “Application for a Declaration of Non-Dominance in the International Call Services Market for Non-China Routes by Cable & Wireless HKT Telephone Limited” issued on 4 August 1999 (August 1999 Non-Dominance Statement). The TA issued a consultation paper (Consultation Paper) on 21 September 2000 seeking views from the industry on the Application. In response to the Consultation Paper, the TA received six submissions. Respondents included CWHKT, CTI International Limited, Hutchison Global Crossing Limited, New T&T Hong Kong Limited, New World Telephone Limited and SmarTone Mobile Communications Limited. A summary of comments from the respondents is given in Annex.

COMPETITION TESTS AND NON-DOMINANCE DECLARATION

2. In considering the application for route reclassification, the TA would apply the same tests on the status of competition as stated in paragraph 7 of the TA Statement entitled “Local Access Charge and Modified Delivery Fee Arrangements” issued on 25 November 1998 (November 1998 Statement).

¹ Cable & Wireless HKT Limited (CWHKT) is the holding company of the group of companies holding several licences including the Fixed Telecommunications Network Services (FTNS) licence issued on 29 June 1995 held by Cable & Wireless HKT Telephone Limited, Cable & Wireless HKT International Limited, and Cable & Wireless HKT CAS Limited. Although the shares of CWHKT were acquired by Pacific Century CyberWorks Limited on 17 August 2000, and CWHKT has subsequently been rebranded as Pacific Century CyberWorks HKT, the FTNS licence continues to be held on a joint and several basis in the original names of the companies in the CWHKT group.

As regards the request for declaring CWHKT non-dominant in the retail market for calls to the Philippines and Taiwan upon reclassification, the TA has on 28 September 2000 issued a statement and a direction² extending CWHKT's non-dominant status in the market of international call services to Category A destinations, which status was granted in the Direction pursuant to General Condition 44 under CWHKT's licence issued on 4 August 1999 (Annex B to the August 1999 Non-Dominance Statement).

COMPETITION IN THE INCOMING DIRECTION

3. In the TA Statement entitled "Reclassification of Category B Routes on the Observation List" issued on 4 August 1999 (August 1999 Reclassification Statement), the TA lifted the gateway price control on the Philippines and Taiwan routes. However, in the incoming direction, the TA accepted that the terminating prices in Hong Kong were determined by the correspondent agreements which were all with a single carrier at the distant end. There appeared to be no genuine price competition in the incoming direction because of the same accounting rate adopted for all correspondent agreements with operators in Hong Kong. Hence, the TA concluded that the Philippines and Taiwan routes, together with the other eight routes³ should stay on the Category B Observation List until such time when *genuine price competition in the incoming direction can be established*.

4. In the TA Statement entitled "Application for Reclassification of the Singapore Route as Category A by Cable & Wireless HKT Limited" issued on 10 June 2000, the TA has stated that the competition tests for route classification in the November 1998 Statement consider the existence of alternative connections and whether or not the alternative connections can allow genuine price competition. Whether the competition has materialised is not necessarily a determining factor although the market share through the alternative connections could be evidence of whether or not the alternative connections could offer sustainable genuine price competition.

² The TA statement and direction are respectively entitled "Application for the Extension of the Direction Issued to Cable & Wireless HKT Telephone Limited on 4 August 1999 pursuant to General Condition 44 of its Fixed Telecommunications Network Services Licence in response to "Application for Declaration of Non-Dominance in the International Call Services Market for Non-China Routes" by Cable & Wireless HKT Limited" and "Telecommunications Ordinance (Cap 106) Fixed Telecommunications Network Services Licence Direction pursuant to General Condition 44".

³ These other eight routes are India, Indonesia, Malaysia, Pakistan, Singapore, South Africa, Sri Lanka and Thailand.

The Philippines route

5. On the basis of the data available from the Office of the Telecommunications Authority regarding the total traffic minutes from the Philippines, CWHKT appears to be receiving virtually all incoming traffic from the Philippines. However, the TA accepts that this may not represent the true picture. Where the traffic from the Philippines to Hong Kong is refiled, it will not be reported as incoming traffic from the Philippines but from the last point of the refile route. CWHKT has, since the Application, submitted further information that relying on the latest edition of the authoritative telecommunications journal *TeleGeography 2000*, the total outgoing traffic minutes from the Philippines to Hong Kong for the 12 months ended 31 March 1999 were 38 millions, whereas for the same period, CWHKT only received less than 40% of the total incoming traffic [actual figures supplied to the TA]. Although the figures supplied by the journal cannot be regarded as official, they are nonetheless an indication of the level of volume of traffic minutes to Hong Kong. Even allowing adjustment to the figures, CWHKT would still not be receiving an overwhelming majority of the traffic minutes, thus pointing to the fact that traffic has been bypassing its gateway.

6. Further, the real tests for route reclassification are whether there exist alternative connections and whether the alternative connections can allow genuine price competition. The TA is aware that correspondent agreements have been established between no less than one other operator with carriers in the Philippines. It is clear that alternative connections have been established. Further, there is evidence that the Philippines telecommunications market is in the process of liberalising. The own figures from the Philippines Long Distance Telephone Company (PLDT), the major carrier in the Philippines, show that their business revenue from international long distance service has been diminishing and it is engaging in price competition with its competitors. With the existence of competition in the telecommunications market in the Philippines, the TA is satisfied that not only alternative connections have been established, but these alternative connections also allow genuine price competition.

7. As to the argument that CWHKT still enjoys a net accounting benefit and makes its competitors unable to compete with CWHKT, the TA is of the

view that as the volume of incoming traffic through CWHKT's gateway is only less than 20% of its outgoing traffic [actual figures supplied to the TA], the actual benefit received through net accounting is limited. According to the information available to the TA regarding the cost of refile, the use of a refile option would still have a cost advantage of above 20% over that of CWHKT.

8. In view of the consideration above, the TA is satisfied that the Philippines route should be reclassified as Category A route.

The Taiwan route

9. The TA accepts that there has been a material migration of incoming Taiwan traffic from CWHKT external gateway. In August 1999, above 70% [actual figures supplied to the TA] of the reported incoming traffic from Taiwan transmitted through CWHKT external gateway but by July 2000, this proportion has fallen to just 50% [actual figures supplied to the TA]. Further, the TA is aware that at least one other operator has established correspondent agreement with a carrier in Taiwan. It is evident that alternative connections have not only been established but have been employed in competition with CWHKT.

10. As regards the cost advantage that CWHKT may have over its competitors by reason of net accounting, the TA is of the opinion that as incoming traffic increasingly bypasses the CWHKT gateway, inpayments that are available to offset the cost of CWHKT would only be diminishing. Further, according to the information available to the TA regarding the cost of refile, at present the use of a refile option would still have a cost advantage of above 40% over that of CWHKT.

11. Based on the above considerations, the TA is satisfied that the Taiwan route should be reclassified as Category A route.

NON-DOMINANCE

12. In the August 1999 Non-Dominance Statement, the TA has already stated his decision that reclassification of a non-China route at the wholesale level should be used as an automatic trigger for moving it from the non-competitive market to the competitive one and thus lifting the constraints at

both the wholesale and retail levels. This decision shall continue to be in force given that CWHKT's non-dominance status in the international call services market for non-China routes has been extended by the TA Statement and Direction issued on 28 September 2000.

CONCLUSION

13. The TA forms the opinion that the Philippines and Taiwan routes should both be classified as Category A routes. Further, the reclassification of a destination at the wholesale level should be used as an automatic trigger for moving it from the non-competitive market to the competitive one and thus lifting the price restraints at both the wholesale and retail levels. Accordingly CWHKT should be declared non-dominant in the retail call market to the Philippines and Taiwan.

Office of the Telecommunications Authority

3 October 2000

ANNEX

SUMMARY OF COMMENTS

1. **Cable & Wireless HKT Limited (CWHKT)**

1.1 CWHKT claimed that since submitting the application for reclassification of the Philippines and Taiwan routes as Category A routes, they had become aware of further evidence of incoming traffic competition on the Philippines route. An extract of the latest copy of *TeleGeography* was supplied to the TA showing that for the 12 months ended 31 March 1999 (the latest data available), there were 38.0 million minutes of traffic from the Philippines to Hong Kong, whereas during the same period, CWHKT received less than 40% of the total incoming traffic [actual figures supplied to the TA]. CWHKT submitted this to be evidence of refile or other means of bypass on the Philippines route.

2. **CTI International Limited (CTI)**

2.1 CTI submitted that it has no comments on the application to reclassify the Taiwan route as Category A. It was however unable to give its comments on the Philippines route within the deadline for submitting comments.

3. **Hutchison Global Crossing Limited (HGC)**

3.1 On the Philippines routes, HGC submitted that the reasons given by CWHKT to explain the low incoming traffic from the Philippines to Hong Kong are speculative. Focus should therefore be made on the fact that CWHKT still receives above 90% of the incoming traffic.

3.2 On the Taiwan route, HGC claimed that despite liberalisation in May this year, the Taiwan market has yet to turn competitive, as can be demonstrated by CWHKT's continuous dominance in the market of incoming traffic.

4. New T&T Hong Kong Limited (New T&T)

- 4.1 On the Philippines route, New T&T submitted that CWHKT's reliance on the refile and circuit cost given by one refiler to conclude that the cost of refiling is substantially lower than its external gateway cost is too subjective and one-sided, and may not reflect the general market price of the cost of refiling. Further, such 'substantially low refile and circuit cost' may not be available to CWHKT's competitors
- 4.2 New T&T also disagreed that the fact that one competitor cancelled all its international private leased circuits with CWHKT in May 2000 is evidence that there are no constraints on the competitors' ability to acquire capacity on the Philippines route. New T&T also stated that CWHKT failed to provide direct evidence that its competitors' incoming traffic from the Philippines has been refiled and has therefore bypassed its gateway.
- 4.3 Regarding the Taiwan route, New T&T similarly argued that reliance on the refile and circuit cost given by one refiler is too subjective. Further, despite the award of three international gateway licences in May 2000, it will be sometime before the facilities of the new licensees can be established and genuine price competition available. It was also argued that the migration of incoming traffic and net accounting cost should not be the only factors to be taken into account in a reclassification application.

5. New World Telephone Limited (NWT)

- 5.1 On the Philippines route, NWT disagreed with the three reasons (namely refile, price rigidity and uneconomical settlement through gateway delivery) put forward by CWHKT to explain why there is no genuine competition in the incoming direction. NWT further stated that CWHKT is free to use non-conventional delivery including refile, which is claimed to be more economical. If CWHKT's reliance on its external gateway for outgoing delivery was due to prior contractual commitment with the Philippines carriers, CWHKT should be alone held accountable for its consequences.

5.2 The same argument applies to CWHKT's claim that the net accounting cost for the Taiwan route is higher than the refile cost. It is up to CWHKT to use alternative method of delivery. As refile is heavily used to supplement traditional bilateral agreement, the genuine cost borne by CWHKT is likely to be lower than the extreme assumption of 100% gateway delivery. On the other hand, external operators would also rely on CWHKT's gateway to deliver their external traffic. As a result the refile cost achievable by CWHKT's competitors is likely to be understated.

6. SmarTone Mobile Communications Limited (SmarTone)

6.1 SmarTone claimed that external telecommunications service (ETS) operators are still at an inferior position in setting up bilateral traffic exchange arrangement with operators of the Category B group. They are unable to achieve the same cost advantage as the fixed telecommunications network services operators, especially CWHKT. A too early reclassification of Category B routes as Category A will put ETS operators in a more difficult position in the highly competitive external telecommunications market.

6.2 It also argued that although there are already alternative correspondent agreements between CWHKT's competitors and carriers in the Philippines and Taiwan, it is yet to prove that their cost of utilizing the connections allow genuine price competition in the supply of external services to / from the Philippines and Taiwan. Further, the provisioning cost by CWHKT was believed to be much lower than the determined gateway prices as a result of proper management of traffic balancing. Any extra outgoing traffic after the traffic balancing exercise would be routed via alternative refile routes. SmarTone believed that CWHKT is having a much better bargaining power than others and the refile rates available to it are much lower.
