

## Review of Local Access Charges

**Statement by  
The Telecommunications Authority of  
Hong Kong**

**28 June 2001**

### Introduction

On 25 October 2000, the Telecommunications Authority (TA) issued a Statement on the review of methodologies for calculation of interconnection charges for value-added services, public mobile radiotelephone services and local access charges (LAC). In that TA Statement, it was concluded that it is premature to replace LAC with the interconnection charges but the relevant cost components would be updated in the review of the LAC level. Using the latest available data, the TA has completed a review on the cost components and decided on the revised LAC level to be effective from 1 July 2001.

### Review of LAC cost components

2. According to paragraph 48 of the TA Statement entitled Local Access Charge and Modified Delivery Fee Arrangements issued on 25 November 1998, the LAC is made up of the following components:

Cost items	Outgoing Direct	Outgoing via Transit	Incoming Direct	Incoming via Transit
Switching and transmission	7.3 (note)	7.3	7.3	7.3
Number portability			0.7	
Local loop and customer line terminating equipment	5.6	5.6	5.6	5.6
Administrative costs	2.2		2.2	
Local Access Charge	15.1	12.9	15.8	12.9

Note: All costs in cents per minute.

3. The TA has reviewed the cost components and the related traffic data for the calculation of LAC. The findings of the review are summarised in the following:

### *Cost of capital*

4. The TA has engaged the economic consultants, National Economic Research Associates (NERA), to conduct a study in August 2000 on the cost of capital for fixed telecommunications services in order to update the cost of capital for the incumbent operator and new entrants. The NERA report has been published on the website of the Office of the Telecommunications Authority (OFTA) on 25 October 2000.

5. NERA recommended the cost of capital should consist of estimates of local and international rates in view that telecommunications markets around the world nowadays have access to world financial markets. Hong Kong, being an open economy, attracts foreign investments. The cost of capital for both the incumbent and entrants would be somewhere between the local and international rates. They considered that the international rate would be more relevant for PCCW-HKT Limited (PCCW-HKT) than 'stand alone' new entrants. However they also indicated that since it is not standard regulatory practice to base a cost of capital estimate on the world market, they were cautious about relying too heavily on the international estimate even for the incumbent. They recommended that the cost of capital for PCCW-HKT should be set in the middle of the pure local and pure international estimates. For new 'stand alone' entrants, they recommended that the local cost of capital estimate should be more relevant. Taking into consideration their recommendations, the TA decides to revise the cost of capital from 21.5% to 18%. The revised rate has included more weighting on the local estimates.

### *Traffic sensitive costs of switching and transmission and number portability*

6. Given that there was no substantial change in the network of the incumbent since the last review, the TA decides not to revise the basic cost elements. By applying a cost of capital of 18%, the switching and transmission cost will be revised from 7.3 cents to 6.4 cents per minute. Number portability cost is also revised based on the longer current duration of 2.26 minutes per International Direct Dial (IDD) call. This will be reduced from 0.7 cent to 0.5 cent per minute.

### *Non-traffic sensitive costs of local loop and administrative overhead*

7. In the current review, the TA has taken on the commercial rentals of the local loops as the basis for the calculation. As the objective of the LAC is to provide

a fair compensation to fixed telecommunications network services and to encourage investment in the customer access network territory-wide, the TA decides to take into account the higher cost of rural local loop. Based on the penetration ratio of urban and rural local loops of PCCW-HKT, the cost of local loop for the current review is \$61.4 per month. With the increase in the number of outgoing and incoming traffic minutes carried by the loop, the cost of the local loop and customer line termination has reduced from 5.6 cents to 4.2 cents per minute. A lower administrative overhead rate of 22.8% has also reduced administrative cost from 2.2 cents to 1.5 cents per minute.

### **Revised LAC Level**

8. The revised LAC applicable to the originating and terminating of external calls, direct or indirect (through a ‘transit’ network) are summarised in the table below:

Cost items	Outgoing Direct	Outgoing via Transit	Incoming Direct	Incoming via Transit
Switching and transmission	6.4 (note)	6.4	6.4	6.4
Number portability			0.5	
Local loop and customer line terminating equipment	4.2	4.2	4.2	4.2
Administrative costs	1.5		1.5	
<b>Total Local Access Charge</b>	<b>12.1</b>	<b>10.6</b>	<b>12.6</b>	<b>10.6</b>

Note: All costs in cents per minute.

### **Effective date for the revised charges and USC adjustment**

9. The revised LAC levels set out in paragraph 8 will be effective on 1 July 2001.

Office of the Telecommunications Authority  
28 June 2001