
The Submission of Truphone (Hong Kong) Limited and Truphone Limited in response to the Consultation Paper on “Application for prior consent under section 7P of the Telecommunications Ordinance in respect of the proposed acquisition of CSL New World Mobility Limited by HKT Limited” issued by the Office of the Communications Authority

4 February 2014

Executive Summary

- Truphone has serious concerns about the proposed transaction and we think that it may have the effect of substantially lessening competition (“SLC”) in the upstream wholesale market for mobile telecommunications services (“Market”).
- A vibrant market for wholesaling of services to MVNO operators is essential for encouraging and facilitating innovation in telecommunications services and maximizing price competition in Hong Kong.
- We advocate that the CA use its powers of investigation to understand the impact on the Market and that a comprehensive study into the competitive effects on the Market be conducted. We are not privy to data which would enable us to express a concluded view on whether the proposed acquisition would have the effect of SLC but the CA is able to obtain that data and other relevant information. We ask that the regulator disclose such data after the study is conducted and then provide a further round of consultation so that the stakeholders MVNOs can provide further feedback and raise specific concerns.
- The benefits to the public arising from the proposed transaction that HKT has attempted to enumerate are, at best, very limited. If an investigation by CA indicates that it may be difficult for MVNOs to obtain services on a wholesale basis or to do so on fair and reasonable terms after the completion of the acquisition, then the limited benefits to the public which have been identified will not outweigh the detriment to the public that will ultimately flow from the reduced competition in the Market.
- Truphone advocates that if the CA decides to grant consent to the application, that consent should be made subject to a direction to HKT:
 - requiring it to comply with the terms of existing MVNO agreements for the duration specified in those agreements; and
 - the terms of which will result in the continued availability of services to MVNOs on fair and reasonable terms (including, as to price) and for parties currently contracted with CSL, that should mean terms which are no less favourable than the terms of the party’s existing contract.
- The proposed transaction, if it proceeds, will mean that the Li family will control a substantial share of both the fixed and mobile telecommunications markets in Hong Kong. That dominance may give rise to broader concerns for the provision of telecommunications services in Hong Kong.

Introduction

Truphone (Hong Kong) Limited and its ultimate parent company Truphone Limited (individually "**Truphone HK**" and "**Truphone UK**" collectively "**Truphone**") are pleased to provide submissions under section 7(P)(8)(a) of the Telecommunications Ordinance (Cap. 106) in response to the Office of the Communications Authority ("**CA**")'s consultation paper on the Application for prior consent under section 7P of the Telecommunications Ordinance in respect of the proposed acquisition of CSL New World Mobility Limited by HKT Limited ("**Consultation Paper**").

Truphone is willing to expand on any of the issues raised or comment on other issues if requested.

Truphone's business and our products

Truphone is a global mobile network and service operator.

Truphone is not the same as other MVNOs in Hong Kong. We are not mere reseller of white labelled services operating in the prepaid and cost conscious segment of the consumer market. We see global businesses, as well as consumers, as the entities that stand to benefit significantly from technology and solutions that we offer.

Truphone has MVNO agreements with operators in Hong Kong, Australia, Germany, Poland, Spain, the Netherlands, United Kingdom and the United States. Those networks are united via a dedicated IP/VPLS network with our mobile core to form a single international Zone – which we call the "Truphone Zone".

We have two main products currently on offer in Hong Kong:

- a multi IMSI SIM based mobile service which offers customers improved voice and data performance, as well as standard local rates rather than roaming rates in the Truphone Zone. Our customers can have a local telephone number for each or any country in the Truphone Zone. The service includes Smart CLI – a functionality that selects the most appropriate telephone number to be displayed on the phone that the Tru SIM user is calling.
- the Truphone App which is an over-the-top content service that allows free VoIP capabilities, in addition to other features, for iOS, Android and BlackBerry devices.

In the Truphone Zone, our customers can talk, text and download as if they were a local, and at local rates, including having a home mobile number and at least one other international number. Our customers in Hong Kong currently have a Hong Kong number and a UK number. We believe that we are the first operator in Hong Kong to offer this service. Our presence marks a step-change for the many Hong Kong businesses which operate internationally and individuals who travel regularly. Our customers benefit from being able to avoid staggeringly high roaming charges and that their customers and friends from home are able to contact them without incurring international call charges while they are abroad.

We are constantly investigating new opportunities to allow us to expand the Truphone Zone and looking for innovative ways to improve customer service.

The proposed transaction

We have reviewed the Consultation Paper and the application made by HKT Limited (the "Purchaser"). CSLNWM (the "Target") is currently the immediate parent company of HKCSL, the MNO which currently provides wholesale services to Truphone HK in Hong Kong. As Truphone HK is a licensed service based operator, an active participant in the retail telecommunications market in Hong Kong, and a stakeholder in the proposed transaction, Truphone considers that the proposed transaction if it proceeds will impact on Truphone significantly.

Our concerns

We now set out below our particular concerns in detail and in response to the questions whether the Proposed Transaction would have, or be likely to have, the SLC effect in a telecommunications market, or if there would be such an effect, whether the proposed change would have, or be likely to have, a benefit to the public that would outweigh any detriment to the public that would be, or would likely to be, constituted by any such SLC effect.

SLC – the wholesale market

MVNOs are the innovators of the mobile communications market because of their need to gain market share by reasons other than solely price. As a prime example, Truphone has brought to the market two services – the widespread use of the multi IMSI SIM to allow

customers to be “local” in many countries and the Truphone App which allows free VoIP capabilities.

The ability to purchase services on a wholesale basis on fair and reasonable terms from a network operator with a robust network is critical to Truphone being able to continue to serve its customers and to innovate and compete in the Hong Kong market. Competition between MNOs at the wholesale level is what allows us to obtain those services on fair and reasonable terms. Any dampening of that competition could have serious commercial consequences for our business and MVNO operators in Hong Kong more broadly.

If MNOs, in a more concentrated market, decide not to sell access to their networks to MVNOs, MVNOs will be eliminated from the market and consumers will be deprived of the benefits of innovation and price competition that they provide to consumers. Thus, the CA, if it allows the proposed transactions to proceed, should put in place measures to ensure the MNOs’ conduct in the Market will not result in a substantial lessening of competition in the Market because of its likely ultimate impact on consumers.

HKT’s application contends (at pages 19 – 22) that the proposed transaction will not have, or be likely to have, the effect of SLC in a telecommunications market. It asserts that the relevant product market for analysis is the supply of mobile services and that the relevant geographic market is Hong Kong. Truphone agrees that the relevant geographic market is Hong Kong. However, we believe that the impact of the proposed transaction should be assessed on supply of mobile services at both the retail and wholesale levels.

We believe that it is essential that the wholesale market be considered separately to understand how it will be impacted by the acquisition.

Truphone does not have access to information that would allow it to make a detailed analysis of the likely state of wholesale competition after the proposed acquisition and to compare that to the existing state of competition in that market. The necessary data and information are not publicly available. However, CA has the powers to obtain that information and the expertise to make that analysis, and in Truphone’s opinion, it is essential that it does so.

We do know that the Target is an active and effective competitor in wholesale telecommunications market in Hong Kong. Its exit from the market will undoubtedly detract from the level of competition that exists for the provision of services on a wholesale basis.

We believe that HKT foresees concerns in the wholesale market for mobile services because it has pre-emptively offered an assurance to the regulator that (at page 6):

“HKT would continue to provide wholesale services now provided by CSL and HKT (eg, MVNO, resale and network sharing arrangements)”

This assurance is not nearly sufficient to address our concern. It may allow Truphone to insist upon the continued provision of services under the existing agreement until it expires but gives no certainty as to either the ability for Truphone to obtain services after that date or the fairness of the terms that might be offered in relation to any renewal of the agreement or any fresh agreement.

We are concerned at the prospect of the Market becoming oligopolised or even monopolised, if the proposed transaction is permitted to proceed. If the CA grants its consent, we believe a way to ensure the continued provision of wholesale services on fair terms is for the CA to make its consent subject to a sufficiently detailed direction to the Purchaser in relation to it continuing to provide services to MVNOs and for it to be prepared to intervene in the case of disputes.

Li family control of mobile market

According to BNP Paribas Research Report published on 8 November 2013, the mobile subscriber market share as of first half of 2013 is as follows:

(a) HKT (12.8%);

(b) CSL (30.2%);

(c) Three Hong Kong (26.1%);

(d) SmarTone (13.8%); and

(e) China Mobile (17.1%)¹. As such, it is expected that after the proposed transaction concludes, the Li family, with its interests in both Hutchison and HKT will control around 69.1% of the mobile subscriber market.

Thus, rather than this acquisition being described as a five to four situation, it is better described as a four to three situation. When that is combined with HKT alone large fixed line market share, we believe that could give rise to real opportunities to dominate communications services markets in Hong Kong.

We note the comments of analysts at Barclays who estimate that the combined HKT and CSL mobile business in Hong Kong will have a wireless services revenue market share of 39.1%, while Hutchison Telecom will have a 29.6% share². Barclays expects the four players to raise tariffs and reduce marketing expenditure. We believe that translates to a prediction of a likelihood of less price competition, post the acquisition.

In respect of 3G spectrum, at present China Mobile has no 3G spectrum and operates 3G

¹ See Exhibit 10 at <http://www.bnppresearch.com/ResearchFiles/28708/Hutchison-081113.pdf>

² See <http://www.scmp.com/business/companies/article/1388612/consumer-worries-over-li-familys-telecoms-grip-hong-kong-after>

services as an MVNO. After the acquisition, SmarTone will be the only non-Li Family controlled entity from which we are able to obtain 3G services. Such a limited choice is a serious concern to Truphone.

Public benefit - subparagraph 7P(7)(b)

If CA determines after its investigation that there is a likelihood of an SLC, it has three options under paragraph 7P(7)(b):

- (i) refuse to give consent;
- (ii) give consent subject to the direction that the carrier licensee concerned takes the action that the Authority consider necessary to eliminate or avoid any such effect; or
- (iii) give consent without issuing a direction under subparagraph (ii) if the Authority is satisfied that the proposed change would have, or be likely to have, a benefit to the public and that the benefit would outweigh any detriment to the public that would be, or would likely to be, constituted by any such effect.

Truphone is of the opinion that when making its analysis under sub-paragraph (iii), the CA should consider the impact on the public, in the following scenarios:

- (a) if the proposed transaction does not take place;
- (b) if the proposed transaction takes place with no safeguards with the result that there is a substantial lessening of competition in the Market; and
- (c) if the proposed transaction takes place with sufficient safeguards in place to protect the Market.

Truphone is of the opinion that after considering these scenarios, the CA will determine that it is in the public interest to ensure that competition in the Market is maintained and that subparagraph 7P(7)(b)(iii) should not be entertained because of the absence of real evidence of absolute public benefit in HKT's application.

The purported "significant potential public benefits" are described in HKT's submission (at pages 23, 24, 55, 56):

- greater cost efficiency – while it is likely that some efficiencies could be realized, we anticipate that the current scale of both operators is such that they are already operating at a high level of efficiency. That being the case, further efficiency gains are likely to be comparatively small. Not only are greater cost efficiencies by no means assured, it is well understood that the bureaucracy and additional layers of hierarchy that can arise in a much larger organization, can in fact generate

inefficiencies. Decision making processes are lengthened and the business' ability to react and respond to opportunities is severely hampered.

- new mobile technologies – HKT's comment under this heading is merely an example of the previous heading to the extent that they refer to economies of scale in the development of new technologies.
- higher quality services – on this issue HKT makes a broad statement with no specifics as to what quality improvements will be delivered, to whom or when.
- wider environmental benefits – again there is no specific identification of how these benefits will arise except for reducing “unnecessary duplication of infrastructure” leading to “wider environmental benefits”. But it is the case that the infrastructure already exists, so that the duplication has already occurred. There may be very modest benefits associated with no longer needing to maintain that infrastructure after it has been decommissioned but we believe that HKT's claim attempts to exaggerate the benefit.
- numerous minor benefits are then described, each in just one or two sentences with little or no detail that would allow proper evaluation of the extent of the public benefit. For example, WiFi offload will allegedly “significantly improve service quality”. But such an improvement is only likely if the CSL network is currently nearing full utilisation of its data capacity and there is no mention of that as part of the claim.

Overall, there is a complete absence of clarity and specificity around the benefits to the public which HKT is asserting will arise as a result of the proposed transaction. It would, in our view, be unwise to base the granting of consent without issuing a direction under subparagraph (ii), on these purported benefits.

As such, Truphone has a view on the directions that should be imposed if the CA decide that subparagraph (ii) is appropriate. Those views are expressed under the next heading.

Our request to the CA

Truphone has two specific requests to the CA:

1. that it conduct a separate analysis of the market for wholesale mobile services in Hong Kong as part of its consideration of the likelihood of the transaction giving rise to an SLC;
2. that if the CA's analysis results in an assessment that an SLC is likely and if the CA determines that it is still appropriate to consent to the transaction, it's consent should be provided under subparagraph 7P(7)(b)(ii). The consent should be subject to a

direction that HKT must offer to provide wholesale services which are currently provided by CSL and HKT (eg, MVNO, resale and network sharing arrangements), that it must offer to provide those services on fair and reasonable terms (including, as to price) and that for existing parties contracted with CSL or HKT, those terms should be no less advantageous than the terms of the existing contract.

Separate wholesale market analysis

We advocate that the CA undertakes an analysis of the wholesale market for mobile services including endeavouring to understand the preparedness of the other three MNOs to offer services on a wholesale basis. That would include considering whether they currently provide services to one or more MVNOs and inquiring as to whether wholesaling services to MVNOs is a significant part of their business model and future business plans.

If the CA finds a reticence on the part of MNOs to support MVNOs or likelihood that support for MVNOs could be scaled back in the future, then we believe that an SLC in a telecommunications market is likely to occur as a result of the proposed acquisition.

If it is viable, Truphone asks the CA to consider putting in measures to ensure the viability of the Market to be continued.

Direction as part of consent to the application

Following on from the wholesale market analysis that we have advocated the CA to conduct, if it is determined that an SLC is likely, Truphone requests that at a very minimum, a direction should be made under subparagraph 7P(7)(b)(ii) to try to eliminate the impact of the likely SLC.

Such a direction should ensure as far as possible that HKT offers MVNO services on fair and reasonable terms, including pricing. For entities that have existing wholesale telecommunications services agreements with CSL, we believe that "fair and reasonable" should be expanded upon to mean terms that are no less advantageous to the contracted party than the terms of the existing agreement. The outcome for which the regulator should be aiming is the maintenance of the competitiveness of the MVNO, or other wholesale purchaser, as it was foreseen when the original contract was agreed.

Confidentiality

Truphone does not regard any part of this submission as confidential and has no objection to it being published or disclosed to third parties, however, this submission in its entirety is

made on the basis that it is without prejudice to the rights of Truphone and its associated corporate entities.

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