

**Universal Service Contribution -
Confirmed Levels for 2012 and 2013,
and Provisional Level from 1 January 2014**

Statement of the Communications Authority

27 July 2015

INTRODUCTION

The Communications Authority (“CA”) has completed the review of universal service contribution (“USC”) for the two years from 1 January 2012 to 31 December 2013. The review is conducted on the basis of the actual cost and revenue of the universal service provider (“USP”)¹ and in accordance with the revised USC calculation methodology² set out in the CA’s Statement entitled “Review of the Regulatory Framework for Universal Service Arrangements” issued on 8 June 2007 (the “2007 USC Statement”).

2. **The USC for 2012 and 2013 are calculated at HK\$56 million (or 13 cents per telephone number allocated per month)³ and HK\$45.4 million (or 10.3 cents per telephone number allocated per month),⁴ respectively.** These represent a reduction of USC for the two years from the HK\$68 million calculated for 2011.⁵

¹ Pursuant to the terms and conditions of the Unified Carrier Licence (no. 25), PCCW-HKT Telephone Limited and Hong Kong Telecommunications (HKT) Limited (collectively referred to as “HKT”) are jointly and severally liable for the universal service obligation (“USO”) under which HKT is the USP of basic telecommunications service in Hong Kong. The USP is entitled to recover the net cost from the contributing parties for meeting its USO.

² According to the 2007 USC Statement, with effect from 1 July 2007, there would be no USC for buildings connected by at least one alternative self-built fixed customer access network and no USC for payphones in the vicinity of competitive and alternative service. In addition, the aggregation basis would be changed from customer-by-customer to distribution points for USC calculation purpose.

³ The average number of total allocated telephone numbers for the year 2012 was 35.9 million.

⁴ The average number of total allocated telephone numbers for the year 2013 was 36.6 million.

⁵ See paragraph 2 of the CA’s Statement, “Universal Service Contribution – Confirmed Level for the Year 2011, and Provisional Level from 1 January 2012”, dated 2 April 2014.

ACTUAL USC FOR 2012 AND 2013

3. The USC for 2012 at HK\$56 million is made up of a net cost of HK\$26.7 million in serving uneconomic fixed lines and HK\$29.3 million in serving uneconomic payphones. The USC for 2013 at HK\$45.4 million is made up of a net cost of HK\$15.7 million in serving uneconomic fixed lines and HK\$29.7 million in serving uneconomic payphones.

Uneconomic Fixed Lines Aggregated on Distribution Points Basis

4. In accordance with the revised USC calculation methodology, the USC for uneconomic fixed lines is calculated on an aggregated basis for each distribution point of the USP's network. During the two-year period, about 22% of the 89,000 distribution points in the USP's network are uneconomic. They together account for about 5% of the number of fixed lines in service. The USC calculated for uneconomic fixed lines for the two-year period is HK\$42.4 million, or an average of HK\$24 per uneconomic fixed line per month.

5. Table 1 below sets out a breakdown of the distribution points among five regions of Hong Kong and their shares in the net cost for uneconomic fixed lines. In general, the shares in the net cost for uneconomic fixed lines in the rural areas are bigger than their shares in terms of the total number of distribution points. This implies that the proportions of uneconomic distribution points are higher in the rural areas, which is as expected given the higher average net costs of providing fixed telephone service in the rural areas compared with the more developed urban areas.

Table 1: Distribution Points by Region

Region	Share in total number of distribution points (%)	Share in net cost for uneconomic fixed lines (%)	Proportion of uneconomic distribution points (%)
Hong Kong Island	17	9	4
Kowloon	24	16	3
N.T. Developed	42	50	34

Region	Share in total number of distribution points (%)	Share in net cost for uneconomic fixed lines (%)	Proportion of uneconomic distribution points (%)
N.T. Rural	14	23	42
Outlying Islands	3	2	18

Uneconomic Payphones

6. There are around 3,700 eligible payphones in the USP's network and almost all of them are uneconomic for the two-year period. The USC required for the provision of uneconomic payphones for the two-year period amounts to HK\$59 million, or an average of around HK\$670 per uneconomic payphone per month.

7. Table 2 below shows the distribution of payphones among the five regions and their shares in the net cost for uneconomic payphones. Since almost all of the eligible payphones are uneconomic, the proportions of uneconomic payphones are similar among the five regions.

Table 2: Eligible Payphones by Region

Region	Share in total number of eligible payphones (%)	Share in net cost for uneconomic payphones (%)	Proportion of uneconomic payphones (%)
Hong Kong Island	23	23	100
Kowloon	39	38	99
N.T. Developed	31	32	100
N.T. Rural	6	6	100
Outlying Islands	1	1	100

Net USC for 2012 and 2013

8. Pursuant to the CA's Statement of 25 November 1998,⁶ over-compensation received by the USP from local access charge ("LAC") should be used to reduce the USC. Based on the information provided by the USP and the industry, it is estimated that the over-compensation in LAC for 2012 and 2013 are equivalent to around 11 cents and 4.9 cents per telephone number allocated per month, respectively.⁷ After using the over-compensation in LAC to the USP for reducing the USC, **the CA confirms that the net USC for 2012 and 2013 would be HK\$8.8 million and HK\$23.7 million, or 2 cents and 5.4 cents per telephone number allocated per month, respectively.**

9. In the last USC review for 2011, the provisional USC from 1 January 2012 was set at zero level. **The CA has decided to fund the net USC for the two years out of the special revenue pool ("SRP") balance of HK\$2.7 million and the rent and rate recoverable fund balance of HK\$22.7 million, so that the USC contributing parties⁸ are (a) not required to pay USC for 2012; and (b) required to pay 1.6 cents per number allocated per month only for 2013.**

PROVISIONAL USC FROM 1 JANUARY 2014

10. According to the established practice, the provisional rate is usually set at the recently determined actual level. **Based on the USC calculated for 2013, the provisional USC from 1 January 2014 would be set at 10.3 cents per telephone number allocated per month.** The CA will update the actual rate for 2014 and the provisional rate for 2015 and thereafter in the next USC review.

⁶ The CA's Statement, "Local Access Charge and Modified Delivery Fee Arrangements", dated 25 November 1998.

⁷ The drop in over-compensation in LAC for 2013 is due mainly to the implementation of the new LAC regime from 1 July 2013 in which the over-compensation in LAC does not apply (see paragraph 12 below).

⁸ USC contributing parties include unified carrier licensees, local fixed carrier licensees, local fixed telecommunications network services licensees, and mobile carrier licensees authorized to provide local fixed or mobile services, as well as services-based operator licensees authorized to provide Class 1 service, Class 2 service or Class 3 service (mobile virtual network operator services only).

BILLING AND COLLECTION OF USC

11. In accordance with the 2007 USC Statement, when the USC funding is based on the quantity of telephone numbers allocated to licensees starting from May 2009, the USP should take up the role of USC billing and collection at the same time. As such, the Office of the Communications Authority will advise the USP the amount that individual USC contributing party should pay in accordance with the confirmed and provisional levels of USC set out in paragraphs 9 and 10 above, and it is expected that the USP will start billing and collecting the USC directly from the USC contributing parties by 2015 in respect of the confirmed USC for 2013 and by 2016 for the provisional USC for 2014.

CALCULATIONS OF FUTURE USC

New LAC Regulatory Regime

12. The CA's Statement issued in December 2011 set out the arrangements regarding the implementation of a new LAC regulatory regime.⁹ Under the new regime, both fixed network operators and mobile network operators are entitled to collect LAC, and a more market-oriented approach is adopted whereby the level of LAC is set by commercial negotiations by the interconnecting parties. The new LAC regime has come into effect on 1 July 2013, following an 18-month transitional period. As such, the LAC over-compensation, which has hitherto been used for reducing the USC paid to the USP, is no longer available under the new LAC regime.¹⁰ With no LAC over-compensation available to reduce USC for the period from 1 July 2013 onwards, on practical terms, this would mean an increase of USC payable by the USC contributing parties to the USP from 1 July 2013 onwards.

⁹ The CA's Statement, "New Regulatory Regime for Local Access Charge", dated 23 December 2011.

¹⁰ Following a supplementary determination made by the CA on 12 March 2012, the CA permitted, as a transitional measure, the coming into effect of replacement commercial arrangements on LAC that are agreed between the USP and its interconnecting parties to charge LAC at a level different from the level determined by the CA during the transitional period.

Special Revenue Pool

13. A SRP has been set up whereby all unclaimed USC rebate and revenue/income/fee generated (or deemed to be generated) from using the payphone kiosks of the USP for non-public payphone purpose would be used for funding USC related activities.

14. In February 2008, a rental fee of HK\$130 per month was adopted for each payphone kiosk deployed for public Wi-Fi service.¹¹ In the last USC review for 2011, the rental fee from 1 June 2013 was provisionally updated to HK\$191 per month with reference to the changes in Private Retail Rental Index published by the Rating and Valuation Department. Based on the latest indices, the rental fee for the period from 1 June 2013 to 30 September 2014 would be confirmed at HK\$194 per month, and with effect from 1 October 2014, the rental fee would be provisionally updated to HK\$203 per month. The CA will further update the rental fee level in the next USC review.

15. The SRP balance after the update in rental fee above was accumulated to HK\$2.7 million as of 31 December 2014. After funding HK\$2.7 million for part of the net USC for the two-year period as set out in paragraph 9 above, the SRP balance would be reduced to zero.

Rent and Rates Recoverable Fund

16. As promulgated in the USC review in 2013,¹² the Government had revised its past assessment of rent and rates imposed on the USP. With the Government's refund of excess payments made by the USP, it was estimated that there would be a total reduction of around HK\$34.5 million on the past net USC paid to the USP. The amount would be kept in the rent and rate recoverable fund to offset the USC from 1 January 2011 onwards.

17. After the first funding of HK\$11.8 million for part of the net

¹¹ The CA's Statement, "Use of Public Payphone Kiosks on Public Streets and Unleased Government Lands for the Provision of Public Wi-Fi Service", dated 15 February 2008.

¹² See paragraph 15 of the CA's Statement, "Universal Service Contribution – Confirmed Level for the Year 2010, and Provisional Level from 1 January 2011", dated 17 April 2013.

USC for 2011,¹³ the rent and rate recoverable fund balance was reduced to HK\$22.7 million in 2014. After further funding of HK\$22.7 million for part of the net USC for the two-year period as set out in paragraph 9 above, the rent and rate recovery fund balance would be reduced to zero.

18. The CA will continue to administer the existing USC arrangement by calculating the net cost of the USP in meeting the USO in a fair, reasonable and efficient manner, and promulgate the calculated USC levels on a regular basis.

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¹³ See paragraph 9 of the CA's Statement, "Universal Service Contribution – Confirmed Level for the Year 2011, and Provisional Level from 1 January 2012", dated 2 April 2014.