
CSL Limited Response

OFTA Consultation Paper: Spectrum
Utilization Fee for Spectrum Assigned
Administratively

3 March 2011

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1 Introduction

CSL Limited (**CSL**) thanks the Office of the Telecommunications Authority (**OFTA**) for providing the opportunity to respond to the consultation paper “Spectrum Utilization Fee for Spectrum Assigned Administratively” (dated 26 November 2010) (**Consultation Paper**).

CSL would be pleased to provide any further information or assistance that OFTA may need in relation to this submission.

2 Executive Summary

CSL supports the move in Hong Kong towards a market-based spectrum regime. We recognise that a spectrum utilisation fee, properly structured and calculated, is an effective mechanism for promoting economically efficient use of spectrum by encouraging users of spectrum bands which are in high demand to switch to using less congested spectrum or fixed network based alternatives where those alternatives are viable.

General response to the Consultation Paper

CSL has previously made submissions to the Government on the key issues that it believes should be taken into account in setting spectrum fees in Hong Kong (**CSL SPF Submissions**).¹ We maintain this approach in this response to the Consultation Paper, and we reiterate the following relevant points:

- Principles informing the calculation and application of spectrum fees should be consistent and transparent. The fees should be determined in a clear, consistent and competitively neutral manner. If the governing principles are not clear, consistent and transparent, or if the fees are determined arbitrarily without consultation with the relevant stakeholders and not taking into account current market forces and international best practices, such spectrum fees may deter efficient investment decisions and distort the market; and
- The SUF should not be considered in isolation: in particular, applicable administration and licence fees should be reassessed against any proposed SUF (as OFTA has already proposed in relation to some aspects of the SUF²).

In keeping with the views we have expressed previously, CSL supports OFTA's proposal to determine the SUF price based on a least cost alternative (**LCA**) method. We request that OFTA further consider refining its approach to calculating the SUF in order to maximise incentives for spectrum rights holders to use spectrum efficiently or to move to alternative technology. We also consider that in the interests of transparency, OFTA should provide greater clarity to stakeholders about:

- the circumstances in which OFTA will take the view that the SUF should include a premium for exclusive use. In our view there is insufficient detail in the Consultation Paper to allow stakeholders to determine whether their use or proposed use of the affected spectrum will attract the proposed 6 fold exclusivity factor;
- whether in fact any WBLRS licences will survive in respect of rights over the affected spectrum bands and, if so, how OFTA intends to "normalize" SUF fees payable as between any surviving WBLRS licences and any new UC licences.³

CSL agrees with the Consultant Report's recommendations⁴ that prior to implementing the SUF, OFTA should review their other related policy settings and reconsider whether other measures might also impact on incentives for spectrum use, such as:

¹ Hong Kong CSL Limited and New World PCS Limited (2 Feb 2007), "The submissions of Hong Kong CSL Limited and New World PCS Limited in response to the 'Consultation paper on Proposed Spectrum Policy Framework' released on 25 October 2006 by the Communications and Technology Branch of the Commerce, Industry and Technology Bureau", <http://www.cedb.gov.hk/ctb/eng/telecom/doc/17%20-%20Hong%20Kong%20CSL%20and%20New%20World%20PCS.pdf>.

² See, for instance, OFTA's discussion regarding the SUF for UC and WBLRS licensees on p29 of the Consultation Paper.

³ As foreshadowed in paragraph 53 of the Consultation Paper.

- revising policies for access to hilltop sites;
- moving to a common basis for management fees for fixed link and possibly private mobile radio users; and
- charging SUFs or other fees to government users to encourage more efficient government use of spectrum.

Specific amendments to the approach in the Consultation Paper

The approach proposed in the Consultation Paper is a constructive step towards achieving a level of consistent and transparent spectrum pricing policy and, if properly implemented, we consider would improve incentives for efficient use of spectrum in Hong Kong.

This approach could be further developed to better achieve these aims. In particular, the SUF should only apply where the following cumulative criteria are satisfied:

- the spectrum is currently administratively assigned;
- the spectrum has not been assigned by and is not suitable for allocation via a commercial competitive process (e.g. by auction);
- the spectrum within the geographical area of interest (which may cover all of Hong Kong) has at least 75% occupancy;
- demand for that particular band is expected to exceed supply within 5 years; and
- no exemption applies.

The same test should be applied at each review, and the SUF should be withdrawn if these criteria are no longer satisfied in respect of a particular spectrum band.

The alternative modes of provision that are considered in calculating the costs of the LCA in order to set the SUF should only include practically viable alternatives, for which a level of actual competition exists. CSL proposes that at least two providers of relevant services would be an appropriate test.

Long term approach – SUF and spectrum trading measures

In the longer term, CSL submits that an SUF based on opportunity cost, imposed as a stand-alone measure to improve incentives for efficient use, may be a greater administrative burden than complementary or alternative measures to promote efficient use of spectrum, such as spectrum sharing or spectrum trading and spectrum liberalisation. Without these complementary or alternative measures, imposition of an SUF would not represent a significant move away from the now outdated control and command approach to spectrum management in Hong Kong.

Therefore, the proposal to impose an SUF based on LCA should be complemented by steps to introduce spectrum trading. As we outlined in our submissions to the Government in response to their consultation on the Radio Spectrum Policy Framework⁵

⁴ Plum Consulting (December 2009), "Study on Radio Spectrum Pricing: Final Report – A report for OFTA", <http://www.ofa.gov.hk/en/report-paper-guide/report/rp20101126.pdf>

⁵ See fn 1 at p 33.

(Framework), we believe that secondary trading is a critical aspect of a market-based regime and is a measure supported by a significant number of other countries, including the USA, UK and New Zealand.⁶

⁶ See Section 3.9 of the CSL SPF Submissions.

3 Responses to Questions posed in the Consultation Paper

Question 1:

Do you agree that SUF for administratively assigned spectrum should only be applicable to the congested frequency bands based on the criteria of congestion given in paragraph 22 of the Consultation Paper?

CSL agrees with the Consultant Report (which has been adopted by OFTA in the Consultation Paper) that SUFs should only be applicable to licensees who have been allocated spectrum administratively in bands that are congested.

CSL agrees that it is unnecessary and inappropriate to impose a spectrum utilisation fee in respect of allocations in frequency bands which are not congested or where there are no competitive alternatives available to the spectrum user. To do this could deter use of the band leaving it idle to no social or economic benefit to the wider community.

Imposing SUF on low-demand bands would be inefficient

Imposing a charge on the use of the spectrum in low-demand bands would also be inconsistent with the requirement under section 32G of the Telecommunications Ordinance, which provides that Authority's approach to spectrum management must promote the efficient allocation and use of spectrum as a public resource of Hong Kong. It would also defeat one of the central policy objectives set out in the Framework, which is to:

"... facilitate the most economically and socially efficient use of spectrum with a view to attaining maximum benefit for the community".

As Professor Martin Cave stated in his 2002 report to OFCOM⁷:

"If the right incentives to use spectrum efficiently are not in place, then, as the Government recognised when it proposed implementing market mechanisms for managing spectrum, 'a self-perpetuating vicious circle of hoarding and shortage can develop'. This will lead to a misallocation of resources in the economy, with consequent damage to economic efficiency, productivity and output.

If however the right incentives are in place, then the economy will benefit as individual users economise on their use of spectrum. The gains will partly come from the fact that spectrum is not wasted. But the most significant gains will come from added dynamic efficiency, i.e. more innovation and greater competition in the markets in which spectrum is used, as new entrants and new technologies win access to spectrum."

This is also consistent with a reading of the Framework which gives the SCED power to determine an SUF for administratively assigned spectrum to reflect its opportunity cost. Implicit in this section of the Framework is the assumption that any fee should be zero if the opportunity cost is zero, and the opportunity cost is zero where because there is no

⁷ Professor M Cave (March 2002), *Review of Radio Spectrum Management*, <http://www.cochrane.org.uk/inside/uk-radio-spectrum-managment.pdf> at page 103.

competing demand between interested parties there is no party that is deprived of the ability to use the spectrum.

Levying the fee on congested bands is also consistent with international best practice. The UK is the leader in administrative incentive pricing, having imposed such a system in 1998. Australia, Singapore and some other countries also charge a fee on congested bands.

What should the SUF threshold be?

The question then becomes what should be the appropriate measure of congestion and what should the threshold for the imposition of a spectrum utilisation fee be?

OFTA has proposed that an SUF should be imposed if the following congestion criteria are met:⁸

- the frequency band is at least 75% occupied; and
- the demand based on the current use of the frequency band is expected to grow over time (for instance in the next 3 to 5 years) or a high potential demand for alternative use is expected.

In proposing these criteria, OFTA has not specified the basis on which it will determine occupancy of the band for the purposes of applying the 75% test, or its rationale for setting the threshold at 75%. However, the consultant's report considered whether 75% or more of the available spectrum in a band had been allocated, and determined those spectrum bands with less than 25% vacancy (based on allocation tables published by OFTA) to be congested.

Treatment of the 11GHz band in the Consultant Report and Consultation Paper

We note that the Consultant Report recommended that the 11 GHz band be treated as a congested band by including it in the SUF proposed for the 5-10GHz range. This recommendation was based on the fact that at the time of the report, OFTA was making new assignments in the band and was experiencing additional requests for assignments in the band from non-government users, fixed network operators and mobile network operators. The congestion threshold was expected to be reached for that band in the near term and well before any SUF review would occur (such reviews are proposed to occur every 5 years).

The Consultation Paper then explains that in the period between when the Consultant Report was finalised and the Consultation Paper was released, occupancy levels in the 11 GHz band changed as a result of requests for assignment of the bands for fixed links and that the band had become congested as a result of the assignment.

However, CSL believes that the second criterion should only be used *in addition* to the 75% occupancy test and should not be used independently or as an alternative to the 75% occupancy test. In other words, the second criterion should not be used to draw into consideration other bands which do not already meet the 75% occupancy test. This is because, as noted above, it is only appropriate to impose an SUF where it is necessary to intervene to free up congested spectrum and not to pre-empt congestion on the basis of projected or surmised future uses of spectrum that might not eventuate.

⁸ Para 22

Forbearance from SUF where future use of alternative technology eases congestion

CSL also considers that the same test used to impose the SUF should be a trigger for withdrawing the SUF. That is, if an alternative technology becomes the preferred technology it is likely that spectrum users will return their allocations, moving off radiofrequency spectrum and onto alternative technology, and congestion in the relevant band together with future demand for that spectrum would decline. In this case and in similar cases, there should be scope for the OFTA to forbear from imposing an SUF given that the SUF would no longer be justified under the proposed test.

Summary

CSL considers the proposed test acceptable, provided that the OFTA clarifies that an SUF would only be imposed if all of the following cumulative criteria are satisfied:

- the spectrum is currently administratively assigned;
- the spectrum has not been assigned by and is not suitable for allocation via a commercial competitive process (e.g., auction);
- the spectrum within the geographical area of interest (which may cover all of Hong Kong) has at least 75% occupancy. We note that while the Consultant Report dismissed any analysis of congestion on a more localised basis, the Consultation Paper does not specify whether the same approach would be adopted by the OFTA going forward);
- demand is expected to exceed supply within 5 years; and
- no exemption applies.

The same test should be applied at each review and the SUF should be withdrawn if these criteria are no longer satisfied in respect of a particular spectrum band.

Question 2:

Do you agree that SUF levied on the administratively assigned spectrum should be based on the LCA approach?

CSL supports an approach which would calculate the SUF as the difference between the cost of current use and the next least cost alternative approach.

However, CSL considers that only those alternative modes of supply which are real practical substitutes, in terms of capacity and availability, should be factored into the comparison.

Application of LCA pricing

LCA pricing should only be applied when there is at least two legitimate viable alternative that is cost effective from a business perspective. Failure to do so could prevent firms (and consumers) from gaining the benefits that can often only be delivered via a wireless solution.

Consideration should be given to the real factors that impact on the ability of a network operator to switch to the alternatives. In particular, the assessment of legitimate viable alternatives should include a consideration of the following factors:

- lead times for provisioning alternative technology options (therefore whether the switch is realistically likely to occur prior to the date of the next proposed review of SUF); and
- whether there is effective competition in alternative modes (that is whether there are at least two providers of the relevant alternative).

These are also practical considerations which depend on localised factors that will impact on the decisions of an operator on a link-by-link basis (the Consultant Report makes reference to factors of this kind⁹).

CSL's view is that if the list of alternatives to the provision of fixed microwave links identified by the consultant were applied on a case-by-case basis and the practical considerations we suggest above are factored in, then in many cases it is likely that there will be no viable alternative to microwave links. In such a scenario where no viable alternative can be identified, the applicable SUF should be the SUF charged for the next highest frequency band where there is at least one viable alternative available (which in turns allows for an accurate calculation of the SUF).

Finally, CSL considers that OFTA should also reassess the existing licence fees for the affected administratively-assigned frequency allocations, in light of the proposed SUF. Further, in setting the LCA pricing, OFTA should take into account all cost factors including licence fees, capital requirements and maintenance requirements. We expand on these points in our response to Questions 3 and 7 below.

Question 3:

Do you agree with the approach on setting the SUF for congested frequency bands for fixed links (assigned under FTNS/FC/UC licence and WBLRS licence) mentioned in the above paragraphs [of the Consultation Paper]?

CSL broadly agrees with OFTA's proposed approach. CSL makes the following suggestions in relation to how OFTA's proposed approach can be further refined and improved.

Calculation of LCA at the 10GHz "tipping point"

As referred to in the Consultant Report¹⁰, at the 10 GHz point there is a tipping point between the relevant lowest cost alternatives. On one side of this point, the SUF is based on the cost of using higher and uncongested frequencies and on the other side of this point, the SUF is based on the cost of using public leased lines (in some cases including the cost of a fibre extension). It is not clear whether each time these are assessed the OFTA will revisit this analysis on a case by case basis, or rely on the cost calculations in the table, and if so, which will be the relevant LCA for the relevant allocation. All stakeholders would benefit from OFTA clarifying this - in particular, what the approach will be in relation to allocations which sit directly on the switching point for these cost calculations. CSL submits that in such cases, or where the applicable frequency band overlaps between two bands that have different licence fees or SUFs (for instance, as reflected in the current licence fee arrangement for the 11GHz spectrum

⁹ Study on Radio Spectrum Pricing System: Final Report, A report for OFTA, Plum, December 2010 at page 55.

¹⁰ See pages 59 to 62 of the Consultant Report.

band)¹¹, the lower cost SUF result should prevail. Using the lower cost result in setting the applicable fees for licensees when such crossover occurs will result in a fairer result for licensees while still allowing OFTA to achieve its SUF objectives.

Setting of SUF for the 11GHz band

A further consideration is that use of the 11GHz band for fixed links is subject to minimum path length requirements in Hong Kong. CSL believes that it is important for these technical licensing requirements to be applied to both incumbent and new licensees of 11GHz spectrum for fixed links. In addition to the minimum path length requirements already specified by OFTA, CSL considers that it may also be appropriate to impose a minimum bandwidth requirement per link for this particular congested band. A measure of this kind is likely to further promote efficient use of the spectrum. Presently, the current users of the 11GHz band may be using older technologies that do not support high bandwidth. If those users upgraded to present technologies then it is likely that they could use higher frequency bands, and this would, in turn, assist to ease congestion in the 11GHz band.

Consideration of licence fees in setting SUF

CSL notes that OFTA's proposed approach does not entirely address the discrepancies between the pricing of spectrum which arise because of the different pricing as between UC and WBLRS licences. In particular, CSL believes that the OFTA should clarify what steps it intends to take to normalise the difference in fees payable between the two types of licences so that the end result is each licensee pays a similar amount.¹² This is further discussed by CSL in its response to question 7 below.

Further to this, in general CSL emphasises the importance of OFTA giving particular consideration to the existing applicable licence fee (both in terms of the current licence rate and the amount of licence fees paid by said licensee in the past) in setting the applicable SUF, in order to ensure a fair result for telecommunication providers (i.e. OFTA should consider the total licence fee and SUF payable in its assessment of what the appropriate SUF should be).

Issues regarding exclusive v. non-exclusive allocation of spectrum and setting SUF

The Consultation Paper proposes that the SUF for an exclusive allocation will be charged at six times the SUF for a non-exclusive allocation.¹³ However, OFTA has not elaborated on whether an allocation will be exclusive based on how the carrier sought to be licensed or on how OFTA determined the spectrum would be allocated. For transparency and predictability, OFTA should clarify the criteria that it intends to apply in determining whether to grant an exclusive allocation for a relevant spectrum band. In addition, OFTA should further clarify how "exclusive use" will be defined, or whether operators will have discretion in determining what "exclusive use" means in practice.

CSL submits that where a licensee has been granted exclusive use of a particular spectrum frequency band, there should be no technical restrictions on how such spectrum is used by said licensee (e.g. in relation to minimum path lengths), since the

¹¹ With the 11GHz band (i.e. 10,700MHz to 11,700 MHz, as identified on page 19 of the Consultation Paper), the 10,700 to 10,999 MHz band attracts a higher licence fee than the >11,000 MHz band (as set out in footnote 12 on page 20 of the Consultation Paper).

¹² See paragraph 54 of the Consultation Paper.

¹³ See paragraph 37 of the Consultation Paper.

licensee will have strong commercial incentives to efficiently use such spectrum and may be hindered by further external restrictions.

Where OFTA does set technical restrictions for licensees who have received non-exclusive spectrum allocations, CSL submits that two key technical requirements that should be imposed on such non-exclusive use are maximum and minimum bandwidth use by the licensee. This will allow OFTA to further designate the technical boundaries for such spectrum allocation, ensuring maximum efficiency of spectrum use¹⁴.

Other considerations for SUF calculation

CSL submits that for clarity, OFTA should confirm that any SUF calculations made by it will include and take into consideration the capital and secondary investment costs required for licensees to purchase and maintain relevant equipment for spectrum usage (such as microwave equipment).

CSL notes that OFTA proposes to round up and round down the LCA cost calculations from the Consultant Report, seemingly to arrive at round figures for the relevant calculations.¹⁵ CSL considers that this rounding is unnecessary.

Question 4:

Do you agree with the approach on setting the SUF for congested frequency bands for ENG/OB links (assigned under FTNS/FC/UC licence) mentioned in the above paragraphs [of the Consultation Paper]?

CSL offers no comments in response to this question.

Question 5:

Do you agree with the approach on setting the SUF for congested frequency bands for satellite uplinks mentioned in the above paragraphs [of the Consultation Paper]?

CSL offers no comments in response to this question.

Question 6:

Do you agree that SUF should be imposed as annual payments regardless of the valid duration of the licence?

CSL agrees with OFTA's proposed approach.

¹⁴ For instance, a user sending a 1Gbps stream over a 10km link will likely be more spectrally efficient than another user sending a 2Mbps stream over the same link distance. Such maximum and minimum bandwidth restrictions will assist in achieving such an objective.

¹⁵ See paragraph 36 of the Consultation Paper.

To require an upfront payment representing the SUF over the entire duration of the licence would be incompatible with OFTA's objective to ensure that there are ongoing incentives for licensees to make efficient use of their licence (as opposed to holding on to the licence).

An annual payment system would balance the interests of OFTA (in creating ongoing incentives for licence holders to use their allocated spectrum) and licence holders (for their business and cash flow interests).

Question 7:

Do you agree that fixed links operated by mobile carriers should be assigned under UC licence (instead of WBLRS licence) and thus be charged with the relevant SUF accordingly?

CSL agrees with OFTA's proposed approach to this question. CSL believes that an equitable approach for all operators (regardless of the type of business) is important if the spectrum efficiency goals are to be achieved and if the intention is to create a level playing field within the telecommunications markets.

CSL agrees with the approach noted in the Consultation Paper which would seek to bring remaining WBLRS licences in affected spectrum bands in line with licences issued under the UC licensing regime in respect of the same affected bands.¹⁶

Currently, fixed links assigned to mobile operators are used for establishing and maintaining wideband links and relay stations for the sole purpose of providing their mobile service¹⁷. CSL submits that such new allocations in the affected bands should occur under UC licences that grant licensees all rights that they would have under UC licences generally, but which should also include the right for the licensee to use the allocated spectrum to provide wholesale services to third parties as well as for providing the licensee's own mobile services. In the interests of equity, CSL also supports moving mobile carriers who are currently operating fixed links under WBLRS licences in the affected bands to UC licences upon expiry. However, CSL considers that OFTA should provide stakeholders with greater clarity of how this is proposed to occur, and whether any WBLRS licences in respect of the affected bands will survive after the imposition of the SUF.

CSL emphasises the importance of keeping the total fee (i.e. SUF plus licence fee) payable to an identical level under both the UC and WBLRS licences, having regard to any licence fee paid to OFTA. For fairness, OFTA should consider imposing identical fees on all UC and WBLRS licence holders regardless of whether they are mobile carriers or other carriers), and in particular the proposed table of SUF prices on page 20 should be updated to reflect this. This is relevant as the Consultation Paper appears to consider only mobile operators in the context of this paragraph, yet there may be other operators (not mobile operators) who can be allocated spectrum under WBLRS licences – these operators should be considered equally along with mobile operators.

¹⁶ As set out, in particular, in Telecommunication Authority (May 2008), "Licensing Framework for Unified Carriage Licence", <http://www.ictregulationtoolkit.org/en/Publication.3420.html> (accessed 18 February 2011).

¹⁷ This restriction is specified at p.68 of Schedule 3 of CSL's UC licence – see http://www.ofta.gov.hk/en/tele-lic/licence/ucl_008.pdf

Question 8:

Do you agree that SUF should be applied to all users of the designated congested frequency bands irrespective of the time when the licence of the user is due for renewal?

CSL agrees with OFTA's proposed approach to this question.

CSL supports a consistent approach (in the form of the same SUF) being applied to all new and existing licensees in the spectrum bands in respect of which OFTA proposes to impose an SUF. An inconsistent approach would give existing licensees a disincentive to abandon the spectrum (as they may not be charged the SUF). Such a development would be contrary to the SUF's primary objective of moving users to alternatives away from the congested bands.

CSL also supports OFTA's approach being consistent with the Consultant Report, the views of which we agree with in relation to this question 8.

Question 9:

Do you agree with the transitional arrangements for implementing the SUF charging scheme (i.e. the grace period, the phase-in introduction of the SUF and the one-off grant arrangement) as proposed in paragraph 57 of the Consultation Paper?

CSL agrees with OFTA that a grace period, phased-in introduction of the SUF and once-off grant arrangement are appropriate measures to ease the industry into the new arrangements.

As discussed above at questions 7 and 8, CSL emphasises the importance of consistent SUF pricing for all existing and future licensees, regardless of the relevant licence starting date or duration and regardless of whether they are mobile operators or otherwise.

CSL believes that the dates for such phase-in introduction and grace periods should be fixed, with new licensees (who may be newly licensed within the transitional period) enjoying the provisions of such periods from whatever time they become a licensee until the transitional arrangements expire. This is consistent with the notion of fairness highlighted throughout the Consultation Paper and Consultant Report in relation to fairness between existing and new licensees.

As we referred to above, it is not clear from the Consultation Paper how OFTA proposes to replace existing WBLRS licences for mobile carriers in the affected bands with updated UC licences in the affected bands and how this will occur relative to the transitional periods proposed. In this respect CSL considers that it is important to encourage those transitioning from the WBLRS licence to UC licence to move off the spectrum. However, as paragraph 4.3 of the Radio Spectrum Policy Framework suggests, a 3 year grace period would be more appropriate if OFTA proposes to vary or withdraw existing licences that are held by mobile or wireless carriers.

Regardless of the duration of the grace period, CSL considers that the grace period should not be seen as a barrier to reallocation of any spectrum freed up as a result of the introduction of the SUF and that new licences can and should be issued during the transitional phase to ensure that spectrum is not left idle during the transition.

Question 10:

Do you agree that the SUF charging scheme should be reviewed every five years?

CSL broadly agrees with OFTA's proposed approach to this question and supports its intentions to review the SUF scheme every five years.

CSL recognises that there is a need for these reviews to occur regularly so that the imposition, calculation and withdrawal of an SUF can occur dynamically in response to the changes in demand for radiofrequency across the spectrum from time to time. For example, the SUF (if successful) will likely mean certain congested bands at present will not be congested in future, but there may in turn be technological developments which will place pressure on other currently non-congested bands.

However, CSL is concerned that OFTA will incur considerable overhead costs in undertaking each review of the SUF pricing, and that there is potential for these cost to be passed onto operators (and, in turn, consumers) to cover the administrative costs for OFTA. For this reason CSL considers it important to set the timing for such reviews in a way which balances the requirements of administrative efficiency with those for determining the optimum use of the spectrum resource. For these reasons CSL supports OFTA's proposal to review the SUF charging scheme every five years.

CSL also considers that a fixed, five-year review period would give greater commercial confidence to the telecommunications industry and enable more effective future investment planning for stakeholders.